



House of Commons
Treasury Committee

Administration and expenditure of the Chancellor's departments, 2008–09

Seventh Report of Session 2009–10

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

*Ordered by the House of Commons
to be printed 24 February 2010*

HC 156
[incorporating HC 1046 i-iii, Session 2008–09]
Published on 9 March 2010
by authority of the House of Commons
London: The Stationery Office Limited
£0.00

The Treasury Committee

The Treasury Committee is appointed by the House of Commons to examine the expenditure, administration, and policy of HM Treasury, HM Revenue & Customs and associated public bodies.

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A list of Reports of the Committee in the current Parliament is at the back of this volume.

Committee staff

The current staff of the Committee are Eve Samson (Clerk), Andrew Griffiths (Second Clerk and Clerk of the Sub-Committee), Adam Wales, Jay Sheth and Helen Jackson (Committee Specialists), Phil Jones (Senior Committee Assistant), Caroline McElwee (Committee Assistant), Gabrielle Henderson (Committee Support Assistant) and Laura Humble (Media Officer).

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Summary

An Extraordinary Year

HM Treasury and its associated bodies faced extraordinary challenges during 2008–09. We draw out common themes, including the extent to which they have had to take on new activity and/or greatly increase the volume of normal activity. We consider how successful they have been, and the cost in terms of pressure on people and other work. We conclude that it is very difficult to draw final conclusions regarding the level of success that should be attributed to the Treasury and its associated bodies for 2008–09—too much remains unfinished business, including HM Treasury's financial stability interventions and its relationship with UK Financial Investments Ltd (UKFI). We recommend that the Government considers whether the formal terms of the relationship between the Treasury and UKFI need some redefinition in the light of experience.

The Treasury Group's performance against objectives

We assess the Treasury Group's performance against its two Departmental Strategic Objectives. We highlight that only 22% of bodies required to report monthly in-year figures to the Treasury met the standards for timeliness and accuracy, and look forward to seeing a significant improvement next year. We recommend that the Treasury reflects on the terminology used to assess its supporting low inflation indicator as “met-ongoing” appears disingenuous when the target was missed in eleven months out of twelve. We also conclude, in line with our earlier reports, that the Government will fall well short of its Public Service Agreement target to halve the number of children living in poverty by 2010–11.

HM Revenue and Customs

Performance at HMRC remains mixed with considerable room for improvement, and considerable challenges remain to be overcome if HMRC is to achieve this improvement. We express concern at the absence of milestone reporting, and urge HMRC to provide more data in future. Noting a 7% increase in total recorded customer complaints, we urge HMRC to reflect on whether customer experiences of HMRC are yet improving as much as their summary of ‘strong progress’ implies. Highlighting the dire results for HMRC of a February 2009 cross-Government staff survey, we express deep concern about employee engagement at HMRC and its effect on performance. We recommend that HMRC's management re-double their efforts to re-engage with their workforce, and publish a clear and detailed plan to provide focus and direction to their actions. HMRC has been slow to consider the possibility that the terms of its contract with Mapeley could put the latter under immense financial strain. We remain to be convinced that sufficient risk management, including a clear and mutually beneficial way forward, is yet in place.

National Savings and Investments

NS&I was a 'safe haven' for savings at the height of the economic crisis, and successfully processed a record amount of new business. These exceptional circumstances posed a dilemma for NS&I which has to tread a fine line between providing a good deal for its customers and supporting Government macro-economic policy. As extremely testing economic times are by no means at an end, it is likely that NS&I's particular role and priorities will continue to come under scrutiny. NS&I expects to reduce its dependence upon the Post Office. We recommend that the Government considers whether there is a wider public interest in retaining stronger links between the Post Office and NS&I.

The Royal Mint

Profits and average rate of return dropped in 2008–09 compared with 2007–08. We note that the rate of return remains relatively healthy. However, the Royal Mint only returned to profitability in 2006–07, and positive future performance—now as a Government-owned company—cannot be taken for granted.

Other associated bodies

Having been told previously that Ministers would meet with port operators to discuss some of the issues arising from the Valuation Office Agency's revaluation of UK statutory ports, we were dismayed to learn that this has not occurred. We are not impressed by the Government's decision to wash its hands of problems which arise, in part, from its own insensitive handling of port rate revaluation. We recommend that the Government urgently reviews the impact of the revaluation on port occupiers, and publishes its findings.

1 Introduction

The Sub-Committee's scrutiny programme

1. The Treasury Sub-Committee undertakes a regular programme of scrutiny of the administration and expenditure of the Chancellor's departments. In addition to annual hearings with HM Treasury and HM Revenue and Customs (HMRC), the Sub-Committee takes evidence each year from a rotating selection of bodies which fall under the Chancellor's remit. Table 1 summarises the hearings that the Sub-Committee has held in recent Parliamentary sessions.

Table 1: Sub-Committee scrutiny sessions, 2001–02 to 2008–09

Department or body	2001–02 Report	2002–03 Report	2003–04 Report	2004–05 Report	2005–06 Report	2006–07 Report	2007–08 Report	2008–09 Report
Adjudicator's Office ¹		Oct 03				Nov 07		
Debt Management Office		Jun 03			Jan 07		Oct 08	Oct 09
Government Actuary's Dept	Jul 02				Nov 06		Oct 08	
HM Revenue & Customs: Inland Revenue Customs & Excise	Jun 02 Jun 02	Jun 03 Jun 03	Jun 04 Jul 04	Oct 05	Nov 06	Dec 07	Oct 08	Oct 09
HM Treasury		Sep 03	Feb 05†	Nov 05	Oct 06	Nov 07	Oct 08	Nov 09 & Dec 09
National Savings & Investments	Jan 03			Oct 05	Feb 07			Oct 09
Office for National Statistics	Oct 02	Oct 03	Oct 04	Nov 05	#			N/A**
Office of Government Commerce		Jan 04	Apr 04*		May 06	Oct 07		
Royal Mint	Nov 02	Nov 03			Nov 06	Oct 07		Oct 09
Statistics Commission	Oct 02	May 03 Sep 03	Sep 04	Nov 05	#			N/A**
Valuation Office Agency				Oct 05†	Jan 07		Oct 08	

*Notes: * denotes an appointment hearing for new Chairman/Director/Chief Executive; † denotes a part of a wider meeting; # denotes scrutiny of 2005–06 annual reports not undertaken due to inquiry into Independence for statistics published July 2006. ** Since 2008, the Office for National Statistics has become the executive office of the UK Statistics Authority, falling within the remit of the Public Administration Select Committee. The Statistics Commission closed on 31 March 08.*

2. Last session, the Sub-Committee continued this scrutiny cycle, looking at Departmental Annual Reports for 2008–09. The Sub-Committee always examines HM Treasury and HMRC. In addition, the Sub-Committee chose to concentrate on the Debt Management Office (DMO), National Savings and Investments (NS&I), and the Royal Mint. As part of the work leading to this Report, the Sub-Committee took oral evidence from officials from each of these bodies. The Sub-Committee also obtained written evidence on progress against a number of significant current issues from the Government Actuary's Department (GAD), Office of Government Commerce (OGC) and the Valuation Office Agency (VOA), though they are not the primary focus of this report. Key outcomes of this correspondence are covered in section 7. For the first time, the Sub Committee also wrote to the Crown Estate Commissioners as, under the Crown Estate Act 1961, they also report to the Chancellor. Their management of the Crown Estate is now the subject of a separate Sub-Committee inquiry, and accordingly their performance is not assessed in this report. The Sub-Committee concluded its 2008–09 Departmental scrutiny by taking evidence from the Financial Secretary, the Rt Hon Stephen Timms MP, and the Exchequer Secretary, Sarah McCarthy-Fry MP. We are grateful to all those who assisted the Sub-Committee in the course of its inquiry.

Relevant documents

3. Scrutiny has been based largely on the published Reports and Accounts of the Treasury, HMRC and other bodies subject to examination.²

2 HM Treasury, *Annual Report and Accounts 2008–09*, July 2009, HC 611; HM Revenue and Customs, *Departmental Report 2009*, July 2009, CM 7591; HM Revenue and Customs, *2008–09 Accounts*, July 2009, HC 464; Debt Management Office, *Annual Report and Accounts 2008–09*, July 2009, HC 853; National Savings and Investments, *Annual Report and Accounts 2008–09*, July 2009, HC 470; The Royal Mint, *Annual Report and Accounts 2008–09*, June 2009, HC 570

2 An extraordinary year

4. All Treasury-associated bodies faced extraordinary challenges during 2008–09, mainly arising from the need to respond to a growing financial crisis and associated economic downturn. In his foreword to the HM Treasury Annual Report and Accounts 2008–09, the Chancellor of the Exchequer placed these challenges within the context of a world economy that “has faced exceptional pressures through 2007 and 2008, with the financial crisis of late 2008 resulting in the sharpest and most widespread global downturn in well over 60 years” and acknowledged, with a degree of understatement, that “this has been a difficult year for the Treasury”.³ His Permanent Secretary, Sir Nicholas Macpherson, told us that 2008–09 had been “certainly the toughest year in my working life.”⁴

5. We obtained a similar sense of challenging times from other Treasury-associated bodies. For Robert Stheeman, Chief Executive of the DMO:

2008–09 provided the most challenging operational environment to date for the DMO. The requirements of the DMO this year have been greater than ever before and the market conditions in which the DMO had had to operate have been the most difficult in the organisation’s eleven year history.⁵

Lesley Strathie, Chief Executive of HMRC, wrote in HMRC’s Annual Report that “the last year has been one of great change for HM Revenue and Customs” and that “the prospect of a sustained global economic downturn meant we had to fundamentally review the way we delivered our core functions.”⁶ Similarly, Paul Spencer, Chairman of NS&I felt that “this has been an exceptional year, in the truest sense of the word,”⁷ whilst Jane Platt, NS&I’s Chief Executive, told us that “over the last year we have certainly lived through some exceptional times, as we have dealt with the flight to safety post the Lehmans crisis in the autumn”⁸. The full force of this drama was felt less by the Royal Mint, though it too had change to report since in April 2007 the Chancellor announced that it was to be vested into a Government-owned company, with transition expected to be completed by 31 December 2009. Chief Executive Andrew Stafford confirmed to us during oral evidence in October that “yes, we are on track. Everything is being done to complete the process by 31 December.”⁹

6. The rest of this section draws out common themes, including the extent to which the Treasury and its associated bodies have had to take on new activity and/or greatly increase the volume of normal activity. We consider how successful this activity has been, and the cost in terms of pressure on people and other work.

3 HM Treasury, *Annual Report and Accounts 2008–09*, July 2009, HC 611, p 5

4 Q 287

5 Debt Management Office, *Annual Report and Accounts 2008–09*, July 2009, HC 853, p 9

6 HM Revenue and Customs, *Departmental Report 2009*, July 2009, CM 7591, p 8

7 National Savings and Investments, *Annual Report and Accounts 2008–09*, July 2009, HC 470, p 3

8 Q 37

9 Q 82

New activity

HM Treasury

7. Over the course of 2008–09 the Treasury and its associated bodies had to take on a number of new activities. HM Treasury undertook a series of interventions to stabilise the financial system, of which the most novel were:

- the creation of UK Financial Investments Limited to manage, on behalf of the Treasury, the Government's investments in Northern Rock, Royal Bank of Scotland and the Lloyds Group;
- the development of the Asset Protection Scheme to provide protection against future credit losses on certain assets, in exchange for a fee. The terms and nature of the Asset Protection Scheme changed through the year as financial conditions improved; and,
- the establishment of the Asset Purchase Facility, or “quantitative easing” to enable the Bank of England to inject money into the economy through the purchase of assets, primarily Government gilts.

HMRC

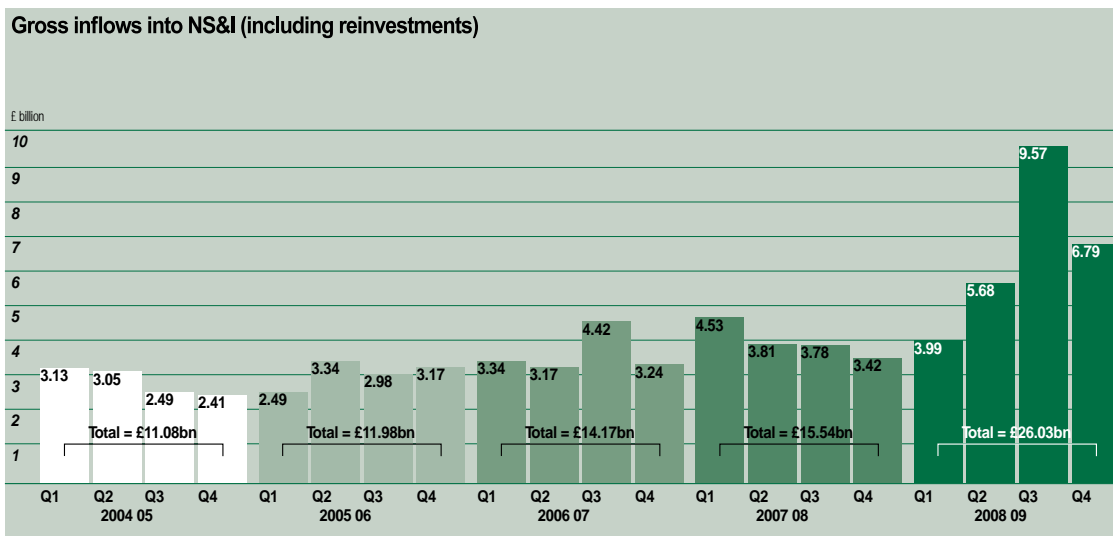
8. As announced in the Chancellor's 2008 Pre-Budget Report, HMRC introduced a new Business Payment Support Service designed to “offer otherwise viable businesses, in temporary financial difficulty, a fast and streamlined service for arranging to pay their tax bills to a timetable they can afford.”¹⁰ In October 2009, Chief Executive Lesley Strathie informed us that “by 11 October we had taken 335,700 calls from businesses and we had arranged more than 217,700 time to pay arrangements worth just over £3.8 billion.”¹¹

NS&I

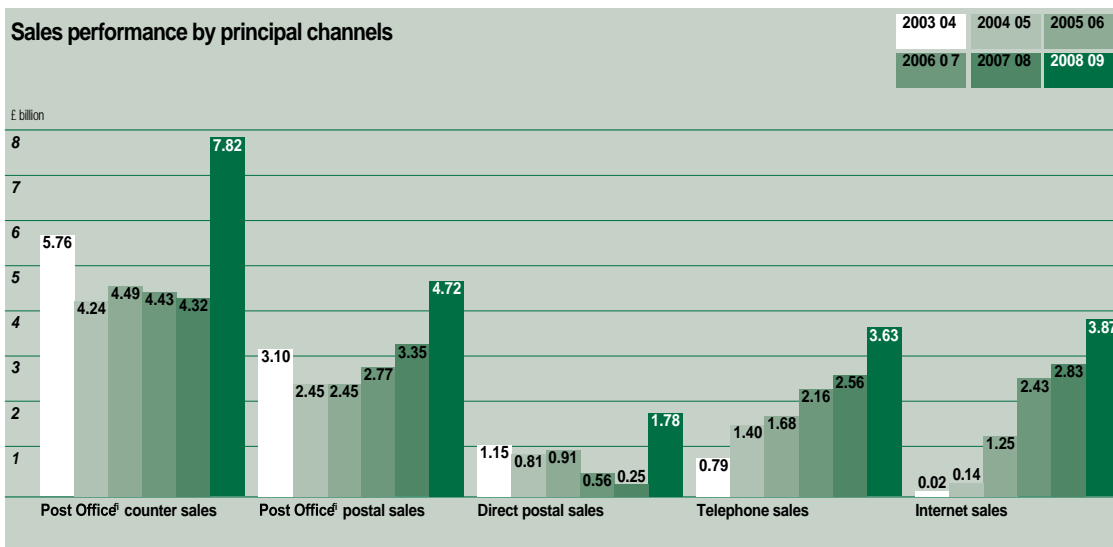
9. Finally, at the height of the financial crisis in autumn 2008, the NS&I became a safe haven for savings as savers lost confidence in private banks and building societies. Net inflows into NS&I (including reinvestments) rose to £9.57 billion in Q3 2008–09, a dramatic increase compared with previous Q3 results of £2.49 billion (2004–05), £2.98 billion (2005–06), £4.42 billion (2006–07) and £3.78 billion (2007–08). As the table below shows, it is also revealing that, over a 5 year period, the next two biggest quarterly net inflows were recorded in Q2 and Q4 2008–09.

10 HM Revenue and Customs, *Departmental Report 2009*, July 2009, Cm 7591, p 26

11 Q 167

Table 2: Gross inflows into NS&I (including reinvestments)¹²

As a consequence, as the table below shows, NS&I took record levels of sales through each of its principal channels—post office counter sales, post office postal sales, direct postal sales, telephone sales and internet sales—during 2008–09.

Table 3: Sales performance by principal channels¹³

High volume of 'normal' activity

HM Treasury and DMO

10. When not taking on new roles, HM Treasury and its associated bodies have also had to handle increased volumes of high priority 'normal' activity. The Treasury still had its full range of objectives to carry out. Robert Stheeman, Chief Executive of the DMO, told us that although over the last year his priorities "have not changed that much. The overall task

12 National Savings and Investments, *Annual Report and Accounts 2008-09*, July 2009, HC 470, p 7

13 *Ibid.*, p 20

that we have been set has become that much larger.”¹⁴ In the case of the DMO, this involved the successful selling of £146.5 billion of gilts through 66 auctions during 2008–09, “by far the highest volume of gilt supply in a financial year...delivered following two major revisions to the financing remit set by HM Treasury.”¹⁵

HMRC

11. HMRC too had to work harder to fulfil its primary tax collection objective during a recession. For example, it had to react quickly to introduce, at short notice, a reduction in VAT. Lesley Strathie told us that “...the huge burden for us was the speed at which we had to implement that change.”¹⁶

Successes?

HM Treasury and DMO

12. HM Treasury and its associated bodies were understandably keen to highlight their successes during the 2008–09 period. In general, HM Treasury sought credit in its Annual Report for taking measures which stabilised the financial system. More specifically, the DMO could point to its continued ability to sell record levels of gilts, and Sir Nicholas Macpherson stressed to us that “the DMO has been remarkably successful at funding sudden needs.”¹⁷

HMRC

13. Lesley Strathie pointed to the creation of the Business Payment Support Service as “a huge success and a real demonstration of how fleet of foot HMRC can be when asked to deliver. Within three weeks we had this service up and running.”¹⁸ She also commented, in relation to the introduction, at short notice, of a reduction in VAT, that “again we did a fantastic job to reach 2,000 businesses and the media and everybody else in the industry to make sure people were in shape to do it.”¹⁹

NS&I

14. Jane Platt, NS&I Chief Executive, told us that:

NS&I and its operating partner, Siemens, did a marvellous job in the face of huge unsolicited volumes in staying open for business. Our contingency plans worked, staff cancelled their holidays, they did extra shift, they really ‘busted a gut’ to be able to make sure that we offered a good service to customers.

14 Q 2

15 Debt Management Office, *Annual Report and Accounts 2008–09*, July 2009, HC 853, p 9

16 Q 190

17 Q 293

18 Q 166

19 Q 190

Asking us to consider “what would have happened if NS&I had not been open for business at a time when people were so concerned about their savings” she recalled visiting NS&I call centres during the ‘flight to safety’ and “listening to people of all ages, some of them in tears, talk about how concerned they were about the safety of their savings” and how experienced NS&I operators “were able to calm people down at a time when emotions were running very high.”²⁰

Measuring performance

15. It is striking that, during the course of 2008-09 HM Treasury, NS&I and the Royal Mint all changed their objectives. Both HM Treasury and NS&I explained their changes as a consequence of the prevailing conditions.

HM Treasury

16. HM Treasury re-wrote indicator outcome 1 (a)—meeting the fiscal rules—of its first Departmental Strategic Objective (DSO). Famously, this indicator outcome used to measure the Government’s performance against the ‘golden rule’ that the central budget be in balance or surplus over the course of an economic cycle. HM Treasury’s 2008 Pre-Budget Report explained that, to achieve its wider financial stability objectives in exceptional circumstances, the Government would depart temporarily from the ‘golden rule’. Accordingly, HM Treasury’s 2009 Annual Report measures performance with regard to meeting the fiscal rules against the following temporary fiscal operating rule:

To set policies to improve the cyclically-adjusted current budget in each year, once the economy emerges from the downturn, so it reaches balance and debt is falling as a proportion of GDP once the global shocks have worked their way through the economy in full.²¹

During oral evidence, we put it to Treasury Permanent Secretary Sir Nicholas Macpherson that this new statement was full of motherhood and apple pie but not a lot of meaning. He responded that:

It is always very important to have some sort of objective or rule to guide fiscal policy. I can remember that under successive governments the objective had changed from time to time, but in terms of credibility one needs something that guides policy.

He accepted though that:

Given the events of last year I would not attach so much importance to the rule as to the actions of the government. There comes a point when you can announce whatever rule you like. What gives you credibility fiscally is what you do.²²

20 Q 39

21 HM Treasury, *Annual Report and Accounts 2008–09*, July 2009, HC 611, p 34

22 Q 313

And admitted that:

There was a debate about whether we should just suspend the rules. Our view and that of the government as a whole was that to suspend the rules would create more uncertainty than if at least we made clear that there was some objective that informed policy and then we would set policy consistent with that objective. I do not believe this rule will be a permanent one.²³

Finally, he pointed out, in a reference to the Government's Fiscal Responsibility Bill, that:

if the government is to legislate a hard budget constraint, which is my understanding of the announcements in September and October, that will provide a harder edge and an opportunity for both the public and parliament to hold the government to account on whether it is hitting the target.²⁴

We remain unconvinced that HM Treasury's present DSO outcome 1(a) temporary indicator serves any real value. We will monitor with interest the extent to which the Fiscal Responsibility Bill, should it become law, comes to provide a rule against which such measurement can be made.

NS&I

17. NS&I's usual first objective is to create at least an agreed amount of 'Value Add' from its products. This is normally a key measure of NS&I performance because it reveals the extent to which it is cheaper for the Government to raise money through NS&I compared with its other sources of financing, such as gilts. During 2008–09, however, NS&I gained Treasury agreement to suspend the Value Add target for 2008–09 and set no Value Add target for 2009–10. NS&I Chief Executive Jane Platt explained to us that:

We temporarily suspended value add at the time when interest rates, the base rate, went down to half a per cent. The base rate has never been that low since the Bank of England was founded and certainly not since Premium Bonds and our other products were introduced. So we looked very carefully at the value add measure and realised that if we did not suspend it, it would drive us to make some very difficult and unfair decisions in terms of pricing for our customers. For example, with base rate at half a per cent, that would assume on our value add measure that the Gilt Office (DMO) would be able to raise financing for 11 or 12 years at less than 0.3%. That is just not true, so therefore we had to suspend the measure because it was distorted and did not give a true measure.²⁵

In other words, the Value Add measure was suspended because, with interest rates so low, and the cost of selling gilts falling accordingly, it was simply impossible in these exceptional circumstances for NS&I to raise money more cheaply than the DMO. She reassured us that "as soon as the comparators which make up that target and benchmark have some

23 Q 314

24 Q 317

25 Q 73

meaning, then we will reintroduce it.”²⁶ She told us that “technically” Value Add could be reintroduced in-year, “but only when the comparators have some meaning.”²⁷ She also observed that a proxy measure which NS&I had worked up with the Treasury focusing on administrative ratios “does indeed show that during the time that Value Add has been suspended so far we are raising money more cost-effectively than the Gilt Office (DMO).”²⁸ **It would have been helpful to have seen NS&I’s proxy measure, and the rationale behind it, clearly set out in its 2008–09 Annual Report. We recommend that, if circumstances do not allow the re-instatement of the Value Add measure during the course of 2009–10, the proxy measure is given greater prominence in next year’s NS&I Annual report.** More fundamentally, the unique circumstances of 2008–09—including the suspension of the Value Add indicator—do raise questions about the main purpose of NS&I, and the extent to which there is a tension between its customer-orientated and Government-orientated aims. We explore this in more detail in Section 5.

Royal Mint

18. The Royal Mint’s first target is to achieve an average rate of return on average capital employed—the target for 2008–09 was 5.1%, which was exceeded. The Royal Mint calculates the average rate of return on average capital employed by expressing profit as a percentage of average capital employed. Profit for this calculation will be taken as the retained profit plus interest and dividend. Average capital employed will be taken as the average of the monthly balance sheet capital employed plus loans and cash. For 2009–10, the Royal Mint has amended the calculation to include Bullion overdrafts within the definition of Average Capital Employed. This was presented to us as a technical change to, as described by Chief Executive Andrew Stafford, “make sure we have a more realistic method of calculating the terms for shareholders.”²⁹ Financial Director Andrew Lawrence informed us that the change “made our target slightly harder, but it is the right decision for the business.”³⁰

Unfinished business

19. As we also noted in our recent Pre-Budget Report,³¹ the UK population is living at a time of great economic (and political) uncertainty. Although the risk of a systemic collapse has now receded—and we acknowledge that some Government measures over the past year have contributed to this—substantial financial and economic challenges remain, and it is too early to draw a line under this extraordinary period.

26 Q 73

27 Q 75

28 Q 75

29 Q 143

30 Q 144

31 Treasury Committee, Fourth Report of Session 2009–10, *Pre-Budget Report 2009*, HC 180

HM Treasury

20. It is hard to put a final evaluation on the success of HM Treasury's financial stability interventions. It is not, for instance, possible at the present time to ascribe a total overall cost to the taxpayer of all the financial interventions. In relation to Government shareholdings, Permanent Secretary Sir Nicholas Macpherson felt that "there was a good chance" that the Government would make a profit on some of them. He noted though that although "there was a trough in January when we made a loss on our shareholdings of £26 billion... a couple of months ago there was a brief period when we were in profit."³² He also noted that HM Treasury had received "quite decent fees" for the credit guarantee scheme and the Asset Protection Scheme, though in a later oral evidence session Exchequer Secretary Sarah McCarthy-Fry MP felt that, with regard to potential losses under the Asset Protection Scheme, "it is an ongoing situation and I do think it is too early to give any timetable or exact figures at this stage."³³ Equally Sir Nicholas Macpherson told us, in answer to our question as to whether quantitative easing is working, that:

This is a very difficult issue to assess because one is assessing against a counterfactual that none of us knows. ...quantitative easing is a journey into the unknown. We do not understand every aspect of it. I am sure that it will keep academics busy for many years to come.³⁴

21. We looked in more detail at the relationship between the Treasury and UK Financial Investments, the organisation which now manages the Government's bank shareholdings. Sir Nicholas Macpherson explained to us that, formally:

UKFI works at arm's length from the Treasury, but there are a number of instruments designed to ensure that it has a very clear framework. It has to agree an investment mandate and business plan with the Treasury. If it is to do anything serious like selling shares in the two major banks that must be cleared with the Chancellor of the Exchequer...Appointments to the board must be approved by the Treasury.³⁵

We examined how the separation of functions between the Treasury and UKFI was working in practice, asking in particular whether the Treasury had shared with UKFI its analysis of the balance sheets of the institutions in which it is now the largest shareholder. Louise Tulett, Group Director of Finance and Procurement, HM Treasury, who sits on the Board of UKFI, told us that:

Everybody is conscious of the controls to protect information to allow only legitimate shareholder information to be known by UKFI and with the Asset

32 Q 292

33 Q 469

34 Q 307

35 Q 299

Protection Scheme, which is now to be administered by an arm's length body in the opposite direction, there is clear water between the two.³⁶

She admitted, however, that “in these early days it is quite difficult to get the demarcation right, but I think we are getting there.”³⁷ When we probed further on where the line was drawn with regard to sharing with UKFI information about the banks' asset bases, she replied that “I do not quite know how we have articulated that line of principle being drawn...”³⁸ In an earlier report³⁹ we stressed how important it was that the arms length relationship between the Treasury and UKFI was clearly defined so that what constituted appropriate behaviour could be clearly discerned. **It appears to us that the relationship between the Treasury and UKFI remains a work in progress, and we recommend that the Government considers whether the formal terms of the relationship need some re-definition in the light of experience. It is important that the lines of demarcation are clear, and reflect the reality on the ground, not least to ensure that other shareholders are properly protected.**

DMO

22. The DMO has a continued requirement to sell unprecedented levels of Government gilts—for 2009–10 it currently has a remit to sell £220 billion gilts—and the outlook is uncertain with the potential for yields to rise and a risk that the market for Government gilts will become saturated. As Chief Executive Robert Stheeman acknowledged to us, “we have been fortunate as well over the last six months in that probably market conditions have been more benign than we and some commentators would have actually expected.”⁴⁰ Benign market conditions for Government gilts are at least in part a consequence of the role of the Bank of England over the past year in acting as a guaranteed final buyer for gilts in pursuit of quantitative easing. Indeed Robert Stheeman stressed to us that “we have to be fully aware and cognisant of the fact that the Bank itself has been buying gilts in the secondary market.”⁴¹ As he explained to us in October, the net impact since the beginning of the 2008–09 financial year of the DMO selling gilts and the Bank of England buying gilts has been “a decline in available gilts in the market by approximately £30 billion.”⁴² Against this background, it is not so surprising that the DMO has been able to raise money “at relatively, in historical terms, cheap levels.”⁴³

23. Robert Stheeman remained confident in the ability of the DMO to continue to sell record levels of gilts, seeing no signs of market saturation. He accepted though that the climate will becoming more challenging when the Bank of England starts to reverse

36 Q 300

37 Q 300

38 Q 302

39 Treasury Committee, Seventh Report of Session 2008–09, *Banking Crisis: dealing with the failure of the UK banks*, HC 416

40 Q 15

41 Q 15

42 Q 16

43 Q 17

quantitative easing, and looks to the DMO to sell still more gilts, observing to us that “exactly where yields would be were the Bank not to buy, I don’t know.”⁴⁴ During our Pre-Budget Report hearings, both the Chancellor and Dave Ramsden, his Chief Economic Adviser, also offered reassurance on future demand for UK gilts. As we noted in our Pre-Budget Report, there remains the risk that the combination of the large amount of gilt auctions planned in 2010–11 and the cessation of quantitative easing will result in an excessive supply of UK gilts onto the market at a time when other governments will be offering similar products, with the possible result that auctions are uncovered and yields increase.

24. The significant deterioration of public finances during the 2009–10 period, casts a long-shadow, with public sector net borrowing projected to be higher than at any time since the Second World War. It follows that **it is very difficult to draw final conclusions regarding the level of success that should be attributed to HM Treasury and its associated bodies for 2008–09—too much remains unfinished business.**

Fallout?

25. Although it is not yet possible fully to gauge the level of success, it is possible to examine some of the costs to date, in terms both of people and effort on other priorities, arising from the need for the Treasury departments to respond to the unique challenges posed during 2008–09.

HM Treasury

26. We looked first at people, taking into account Sir Nicholas Macpherson’s comment that “there are people in the Treasury who have given an extraordinary amount of their time in the past year. A number of people have worked almost day in and day out over many weekends.”⁴⁵ Against this background, we asked Robert Stheeman whether he had enough people to handle DMO’s increased workload, and were assured that “we have had discussions with the Treasury about the resources. We have received the resources that we have requested and we requested more resources, also financial resources, and we have received those.”⁴⁶ We asked a similar question of Sir Nicholas Macpherson about HM Treasury as a whole and received similar assurances that “we have taken in more resources and on the financial stability side in particular the Treasury is much bigger; it has grown in size during this period. All I would say is that it has been helpful to us to have the resources to deal with what we have had to do...”⁴⁷

27. Conscious of the increased risk of overstretch and burn-out, we asked the Treasury whether it was prudent to proceed with its efficiency programmes at a time of greatly enhanced workload. Louise Tulett, The Treasury’s Group Director of Finance and Procurement, accepted that increasing productivity at this time was a major task, but

44 Q 16

45 Q 290

46 Q 35

47 Q 359

affirmed that “it is one that we are on track to deliver.”⁴⁸ Sir Nicholas Macpherson was equally clear that the Treasury should not “give up on the efficiency agenda” not least because it was a means of freeing up more resources and “in a crisis one needs to bring in more resources.”⁴⁹

28. We also asked the Treasury whether other priorities had suffered as a consequence of the additional work required to stabilise the financial system. Unsurprisingly perhaps, Treasury Ministers were reluctant to go into details. Sarah McCarthy-Fry MP accepted that “obviously we have had to prioritise our resources, and there has inevitably been a priority, a focus, on stabilising the banking system”, but she was equally clear that “we have tried not to let the bread-and-butter issues go. We are keeping them on track, but inevitably there has been a prioritisation on the banking stability side.”⁵⁰ When we pressed her on whether any lower priority activities had been stopped, she replied that “we are trying to keep them ticking over.”⁵¹

29. We asked in particular whether the Child Poverty agenda had suffered. The Financial Secretary Rt Hon Stephen Timms MP was quick to reassure us that “in terms of Ministerial commitment, I would not have been able to identify a negative impact from the difficulties that we have seen.”⁵² His Permanent Secretary, though, was prepared to admit that, with regard to the Child Poverty agenda, “inevitably, from a personal perspective I have had less time to devote to the details of this agenda as in previous years because I have had to spend much of the year dealing with the banks and the implications of the recession in terms of monetary and fiscal policy”⁵³ adding that “in terms of my personal time, I must prioritise otherwise, I would never get any sleep at all.”⁵⁴ We look in greater detail at the Treasury’s performance with regard to Child Poverty and its other objectives in the next section.

HMRC

30. HMRC has an ambitious transformation programme to improve its efficiency involving a reduction in the number of people working for it, and a reduction and redistribution of the locations of its businesses. HMRC has already reduced the number of people in its organisation from 105,000 to fewer than 89,000. In her Annual Report Review, Chief Executive Lesley Strathie explained that “such is the scale of our transformation, it is not surprising the past year has been challenging for our employees.”⁵⁵ Indeed, at HMRC the relationship between staff morale, efficiency measures and performance appears to be particularly sensitive, and we explore it in greater detail in Section 4.

48 Q 358

49 Q 359

50 Q 388

51 Q 389

52 Q 390

53 Q 381

54 Q 382

55 HM Revenue and Customs, *Departmental Report 2009*, July 2009, CM 7591, p 9

Conclusion

31. We appreciate the magnitude of the challenges faced by HM Treasury and its associated bodies during the course of this extraordinary year, and commend the extent to which the workforce has been willing to go the extra mile in response to these challenges. It is important though that Departments do not take this commitment for granted and continue to monitor for signs of burn-out and over-stretch. This is particularly important because, as we have highlighted above and in other recent reports, the challenges posed during this extraordinary period remain very much ongoing business.

32. In the remainder of this report, we examine individually and in greater detail the performance of HM Treasury and its associated bodies. We look first at the Treasury Group's performance against its objectives.

3 The Treasury Group's performance against objectives

33. The Treasury Group consists of HM Treasury, DMO and The Office of Government Commerce (OGC). In 2008–09, the Treasury Group reported against two Departmental Objectives:

DSO1: Maintaining Sound Public Finances; and,

DSO2: Ensuring high and sustainable levels of economic growth, well-being and prosperity for all.

It also reported against Public Service Agreement 9—ending Child Poverty (PSA9)—for which it has the lead responsibility.

34. The Treasury rated its overall performance against DSO1 as 'Some Progress'. It recorded 'strong progress' against three DSO1 outcomes:

- professionalising and modernising the finance function in government;
- professionalising and modernising the procurement function in government; and,
- managing government cash, debt and reserves efficiently and effectively.

It recorded 'no progress' against one DSO1 outcome:

- managing public spending.

Finally, two DSO1 outcomes were not assessed:

- meeting the fiscal rules; and,
- ensuring that the tax yield is sustainable and risks managed.

The Treasury rated its DSO2 overall performance as 'some progress'. It recorded 'some progress' against five DSO2 outcomes:

- promoting the efficiency and fairness of the tax system;
- supporting fair, stable and efficient financial markets;
- raising productivity with sustainable improvements in the economic performance of all English regions including narrowing the gap in growth rates between the best and worst regions;
- protecting the environment in an economically efficient and sustainable way; and,
- pursuing increased productivity and efficiency in the EU, international financial stability and increased global prosperity.

It recorded a 'met-ongoing' assessment against one DSO2 outcome:

- supporting low inflation.

Two DSO2 outcomes were not assessed:

- improving the incentives and means to work; supporting children and pensioners; and helping people plan and save for the future; and,
- improving the quality and value for money of public services.

The Treasury recorded 'no progress' against PSA9:

- halve the number of children in poverty by 2010–11, on the way to eradicating child poverty by 2020.

This section looks at both DSOs and the PSA, and also looks at the Treasury's progress towards introducing International Finance Reporting Standards (IFRS) across Departments and publishing Whole Government Accounts (WGA).

DSO1

35. In the previous section, we questioned whether, as currently defined, the indicator for the first, and yet to be assessed, DSO1 outcome— outcome 1(a) meeting the fiscal rules— could ever meaningfully be assessed. In this section, we turn our attention to one of the DSO1 outcomes which was assessed. During our Treasury evidence sessions, we probed the extent to which some of the underlying data for DSO Outcome—1d(i)— Professionalising and modernising the finance function in Government—supported the Treasury's assessment of 'strong progress,' drawing the Permanent Secretary's attention to the fact that of the 59 bodies required to report monthly in-year figures to the Treasury in 2008–09 an average of just 13 (22%) regularly met all agreed standards for timeliness and accuracy.⁵⁶ He responded that

These targets are very new and are part of raising the bar in terms of departmental performance. This is particularly about the quality of monthly reporting of spending in the Treasury. All departments are on an upward trajectory, but what that statistic reveals is that there is a lot more to be done.⁵⁷

He accepted that "you can do quite a lot" to improve departmental performance here, and suggested that "moral-suasion"—creating "quite a lot of peer pressure"—could play a key role, as could "more direct mechanisms" through the Cabinet Office's capability review programme and his own relationship with other departmental permanent secretaries.⁵⁸

56 HM Treasury, *Annual Report and Accounts 2008–09*, July 2009, HC 611, p 39

57 Q 321

58 Q 322

36. We also put Treasury Ministers on the spot. Exchequer Secretary Sarah McCarthy-Fry MP asserted that the poor outcome to date “does not mean we are not on the right track”⁵⁹ and pointed to “a review of the Corporate Governance Code”⁶⁰ as evidence that the Government was taking action further to improve the finance function in Government. **We look forward to seeing a significant improvement in the timeliness and accuracy of Departmental monthly in-year monitoring figures next year, as the actions highlighted by the Permanent Secretary and Minister take effect.**

DSO2

37. Under DSO2, we queried first how the Treasury justified a “met-ongoing” assessment against its supporting low inflation outcome—DSO Outcome 2(a) supporting low inflation—given that, as shown in the table below, in 2008-09 it missed its inflation target⁶¹ in three out of four quarters and that, by its own admission, “since May 2008 and until recently, CPI inflation has exceeded the threshold above which the Governor of the Bank of England is required to write an open letter to the Chancellor, as set out in the remit for the MPC.”⁶²

Table 4: Inflation performance 2008–09⁶³

	2008 Q2	2008 Q3	2008 Q4	2009 Q1
Average CPI (per cent)	3.4	4.8	3.9	3.0

38. The Permanent Secretary defended the assessment on the grounds that “inflation came back rapidly to within the range...what matters is what the average inflation rate is over a long period and it is very close to the 2% target.”⁶⁴ Exchequer Secretary Sarah McCarthy-Fry MP similarly justified the assessment “presumably because we got there at the end of the year.”⁶⁵ A subsequent supplementary memorandum from the Treasury confirmed that:

The rationale behind the ‘met-ongoing’ assessment is that consumer price inflation (CPI) hasn’t been more than 1% above or below the 2% target since February, but also that the monetary policy framework allows the Monetary Policy Committee to look through short-term fluctuations to keep inflation at target over the medium term. As the latest MPC remit states:

The Framework takes into account that any economy at some point can suffer from external events or temporary difficulties. The framework is based on the recognition

59 Q 417

60 Q 418

61 2% as measured by the 12 month increase in the consumer prices index (CPI).The target allows for fluctuation of 1% above or below the 2% target

62 HM Treasury, *Annual Report and Accounts 2008–09*, July 2009, HC 611, p 54

63 *Ibid.*, p 55

64 Q 325

65 Q 435

that the actual inflation rate will on occasions depart from its target as a result of shocks and disturbances. Attempts to keep inflation at the inflation target in these circumstances may cause undesirable volatility in output.

Whilst we understand the logic of the Treasury's position, it still appears disingenuous to claim, with no further explanation, that a target has been met when that target has in fact been missed in eleven months out of twelve, and we recommend that the Treasury reflects on the terminology used to assess this indicator.

39. We also probed the Treasury on a second DSO2 outcome—improving incentives and means to work; supporting children and pensioners and helping people plan and save for the future. We expressed our disappointment that neither of the indicators against which this outcome will in future be assessed related to the supporting pensioners element. As we put it to both the Permanent Secretary and Ministers, this is an important area not least because large numbers of pensioners are paying tax on their savings when they should not. The Permanent Secretary told us that he was “sorry that this section does not contain a reference to pensioners” and that “we will endeavour to do better next year.”⁶⁶ **We recommend that the next Treasury Committee test whether this commitment to provide a DSO2 indicator for pensioners has been fulfilled next year.**

PSA9—Child Poverty

40. We have regularly scrutinised the Government's progress towards its ambitious and challenging child poverty targets, and warned of the growing risk that it would fail to meet them—most recently in our *Pre-Budget Report 2009*.⁶⁷ During our Annual Report hearings, we were concerned by the lack of detailed knowledge displayed by Permanent Secretary Sir Nicholas Macpherson on this key area of Treasury responsibility, drawing from him the admission that “from a personal perspective I have had less time to devote to the details of this agenda as in previous years.”⁶⁸ With regard to reaching interim and final child poverty targets, we were also less than reassured by his observation that:

there are trends at work in the economy which mean one is running quite hard sometimes to stand still. I am optimistic that those measures [taken by the Government in recent Budgets] will have a positive impact on people's lives. What I am less confident about is that they will translate on a one-to-one basis in the child poverty statistics.

He went on to explain that one of the trends “is due to the effect of globalisation. There are huge forces at work in our society that tend to stretch the income distribution.”⁶⁹ Although Ministers were more upbeat about the potential for, in the words of Financial Secretary the

66 Q 330

67 Treasury Committee, Fourth Report of Session 2009–10, *Pre-Budget Report 2009*, HC 180

68 Q 381

69 Q 386

Rt Hon Stephen Timms MP, “further substantial progress”, even he accepted that “hitting the 2010 target would be a stretch”.⁷⁰

41. On the weight of evidence from both our 2009 Annual Report and 2009 Pre-Budget Report hearings, the Government will fall well short of its target to halve the numbers of children living in poverty⁷¹ by 2010–11. **We reiterate, therefore, our 2009 Pre-Budget Report recommendation that the Government clearly sets out the steps it proposes to take to move nearer its 2010–11 target in the time available and to achieve the eradication of child poverty by 2020.**

Implementation of International Financial Reporting Standards

42. The Government has committed to preparing public sector accounts in accordance with International Financial Reporting Standards (IFRS). In our report last year⁷² we noted that the Government’s timetable for achieving this had slipped from 2008–09 to 2009–10. In oral hearings this year, Ministers confirmed that the implementation of IFRS to the revised timescale remains “important”⁷³. Ministers also reassured us that the Government remains on-track to publish Whole of Government (WGA) accounts for the first time in July 2010 for the 2009–10 financial year.⁷⁴ In our Pre-Budget Report we noted that while PFI contracts will show on balance sheet in departmental accounts prepared under IFRS, they will not appear in the calculations of net debt in whole of government accounts. **We reiterate our view that future Pre-Budget and Budget Reports should include a reconciliation between Public Sector Net Debt calculated on a national accounts basis, and the same figure calculated using the IFRS principles which apply to departmental accounts.**

70 Q 456

71 From the 1998–99 benchmark figure of 3.4m in relative poverty. The current relative poverty figure is 2.9m.

72 Treasury Committee, First Report of Session 2008–09, *Administration and expenditure of the Chancellor's departments 2007–08*, HC 35

73 Q 537

74 Q 544

4 HMRC

Background

43. Her Majesty's Revenue and Customs (HMRC) was formed in April 2005 when the Inland Revenue merged with HM Customs and Excise. The Department is responsible for administering the UK tax system, collecting revenue and paying entitlements. During 2008–09, as we noted in section 2, HMRC had a particularly challenging working environment. The onset of recession made HMRC's prime tasks of collecting revenue and paying entitlements more difficult, whilst its Transformation Programme continued to drive the department to improve performance whilst delivering substantial efficiency savings at the same time. During our inquiry, we sought to establish whether HMRC was rising to these formidable challenges or whether it was at risk of sinking beneath them. Accordingly, in this section we assess HMRC's performance during 2008–09 and look at the three areas of great risk if performance is to be improved in the future: staff morale; its IT systems; and, its contract with Mapeley.

Performance—DSO1

44. We looked first at HMRC's performance against its first Departmental Strategic Objective (DSO1—to improve the extent to which individuals and businesses pay the amount of tax due and receive the credits and payments to which they were entitled. On the tax collection side, the total revenue collected by HMRC fell from £457.4 billion in 2007–08 to £435.7 billion in 2008–09, a decrease of 4.7% or £21.7bn. The total revenue collected as a percentage of GDP also fell from 32.2% in 2007–08 to 30.5% in 2008–09. We asked Chief Executive Lesley Strathie, whether this outcome was unavoidable given declining economic performance or whether it reflected increased tax avoidance. She replied that:

The analysis would suggest that most of this is due to the economy. As you know, figures get revised at Budget time and the Pre-Budget Report, but what we are seeing is very much the impact on the economy. Where VAT is concerned you also had the reduction in the rate of VAT and an increase in debt.⁷⁵

She argued further that there was “lots of evidence”⁷⁶ to show that HMRC's anti-avoidance strategy was working. This is though not reflected in the Annual Report which records⁷⁷ that it is too early to give an assessment of HMRC's efforts to increase tax and National Insurance contributions actually received relative to the amounts that should be received. This paucity of milestone data is echoed elsewhere, and we comment further on this in subsequent paragraphs. More reassuringly, during our inquiry into the Pre-Budget Report,

75 Q 178

76 Q 181

77 DSO1 Indicator 1: By 2010–11 increase tax and National Insurance contributions actually received relative to the amounts that should be received, achieving over 2008–09 to 2010–11 at least the levels set out in the Public Service Agreement targets for 2007–08

John Whiting, Tax Policy Director, Chartered Institute of Taxation and Low Incomes, also affirmed that he found the Department's anti-avoidance strategies to be "basically pretty effective."⁷⁸

45. We looked next at HMRC's performance with regard to paying-out entitlements. Specifically we examined Working Tax Credits, the take up of which is—like tax avoidance above—one of the performance indicators for DSO1. Robert Summersgill, HMRC Director Benefits and Credit, told us that HMRC's target here is by 2010–11 to increase the take up of Working Tax Credit from a 2006–07 baseline of 57% to "into the 60s,"⁷⁹ which would be a caseload increase of "100,000 by spring 2011."⁸⁰

46. Richard Summersgill, explained why the base-line take up of working tax credit, a benefit for "people who do not have caring responsibilities for children anymore"⁸¹ was so much lower than take-up for child tax credit (around 80% take-up) and for child benefit (around 90% take-up), observing that:

...there are two particular groups that we are trying to focus on: couples over 50 and young men over 25 which tend to be the groups in particular that are more resistant to taking up working tax credit. Quite a lot of our activity is focused at those groups.

47. We were somewhat concerned to note that HMRC does not intend to publish an indication of progress for working tax credit take-up until Spring 2010. As we have also previously noted, there is a similar lack of transparency in HMRC's Annual Report on tax avoidance. In all, the Annual Report records no milestones against three out of the four performance indicators for DSO1. Furthermore, the one milestone that is recorded—progress with regard to reducing the level of incorrect tax credit payments made as a result of error and fraud—dates back to 2007–08 so is hardly an indicator of current performance. The box below provides a summary:

DSO1 – Overall summary – Not yet assessed

Indicator 1: By 2010–11, increase tax and National Insurance contributions actually received relative to the amounts that should be received, achieving over 2008–09 to 2010–11 at least the levels set out in the Public Service Agreement targets for 2007–08.

Latest Assessment: It is too early to give an assessment but provisional estimates will be published in the Autumn Performance Report 2009.

Indicator 2: By 2010–11 reduce the level of incorrect tax credit payments made as a result of error and fraud as a percentage of finalised entitlement, to no more than 5%.

78 Treasury Committee, Fourth Report of Session 2009–10, *Pre-Budget Report 2009*, HC 180

79 Q 212

80 Q 212

81 Q 211

Latest Assessment: Because this is an absolute measure (5% of the finalised entitlement) no baseline is needed. Latest annual assessment for 2007–08 published in July 2009 shows a central estimate for the level of error and fraud at 8.6%. As this result reflects a period prior to the implementation of our new strategy this is not unexpected and we will still expect to meet our target of reducing error and fraud to 5% by March 2011.

Indicator 3: By 2010–11, increase the take up of Working Tax Credits

Latest Assessment: Progress will be measured against the 2006–07 baseline of 57% published in the 'Child Tax Credit and Working Tax Credit Take-up rates' document. The next measurement point will be Spring 2010. Our internal indicators show that we are on track to deliver this indicator. This DSO has been supplemented with the Budget announcement that we will increase the number WTC only claimants, a sub-set of those claiming WTC, by 100,000 by March 2011.

Indicator 4: By 2010–11, at least maintain take up levels of Child Tax Credit and Child Benefit

Latest Assessment: Progress for at least maintaining take up rates for Child Tax Credits (CTC) and Child Benefit (CB). Take up will be measured against the 2006–07 baselines of 81% for CTC published in the 'Child Tax Credit and Working Tax Credit Take-up rates' document and 96% for CB, published in the Autumn Performance Report 2008. The latest figures available are for 2006-07. Our next measurement point will be Spring 2010.

48. We asked HMRC whether this was acceptable, both in terms of transparency and in terms of its own ability to track progress. Chief Executive Lesley Strathie replied that:

I can say very broadly here that we are clear about the strategic objectives and we are clear about the outcomes in terms of each of those pieces of work to do. What we have been developing very clearly are the performance measures that will deliver the outcome because you cannot manage to an outcome base. A lot of these are statistics that will eventually be validated and revised and there is a considerable lag...It is not a do-nothing, it is just when we publish robust series of data.⁸²

Affirming that HMRC in place sufficient measures to indicate the Department's progress against its milestones, she told us that:

...as an executive team in HMRC, we have the data flows once a month where we take a view from those measures whether we think we are on course or not. If we look at the £7 billion target [for reducing tax avoidance losses between 2008-0-9 and 2010–11]” we have over a number of years to close the tax gap then that is

clearly something where we measure our performance and take a judgement of the volatility and, month by month, whether that is telling us we are on target or not.”

49. The absence of regular public reporting on milestones by HMRC is a major obstacle to both effective scrutiny and performance. We believe that HMRC must publish data regularly to chart its level of progress against DSO1 indicators; and set these out in its Annual Reports. We believe this is essential for the tax gaps to be closed and for the assessment accuracy and take-up of the working tax credit to be improved, especially for those without children, and those whose incomes and jobs are volatile and constantly changing.

Performance—DSO2

50. HMRC's second DSO is to improve customers' experience of HMRC and improve the UK business environment. This DSO has two outcomes—understanding customers and their needs, and making it easy for customers to get things right. HMRC reported strong progress against these outcomes. However, there are areas of concern. As the table below shows, HMRC recorded 87,179 customer complaints in 2008-09, an increase of 5,804 or 7% on 2007-08. In some areas, such as National Operational Services, and Stamps and Taxes, there has been a considerable fall in complaints. In other areas however, there have been substantial increases: Call Centre complaints have risen by 1,739 or 29%; Processing Office complaints have risen by 4,797 or 38%; and Online Service complaints have risen by 929 or 181%:

Table 5: Number of complaints received by HMRC by business activity⁸³

Business Activity	2007-08	2008-09
Charities Assets and Residence	801	1,134
Child Benefit Office	2,612	2,374
Contact Centres	5,905	7,644
Debt Management and Banking	4,204	4,267
Enquiry Centres	99	65
Local Compliance	2,583	2,275
Law Enforcement	1,567	1,443
Processing Offices	12,467	17,264
National Teams & Special Civil Investigation	2,350	1,140
National Insurance Contributions	4,496	3,597
National Operational Services	1,232	580
Online Services	514	1,443
Stamps and Taxes	1,867	584
Tax Credit Offices	38,528	41,107
Valuation Office Agency	2,150	2,362
Totals	81,375	87,179

Note: we paid redress of £2.69m, in respect of our mistakes and unreasonable delays compared to £2.65m paid during 2007-08 and £2.46m paid during 2006-07. This is based on ex-gratia and ex-statutory redress payments paid in the year.

51. Lesley Strathie told us that “a very large chunk of those complaints have been about rudeness or tone or the way that we handled them rather than the subject matter in the first instance”⁸⁴ and emphasised that “one of the steps we have taken on the analysis of the numbers...is to address the manner in which we deal with people”.⁸⁵

52. Contact centres are a key point of customer interaction. Although she told us that “our contact centres have come on in leaps and bounds in this past year”, complaints have gone up and, perhaps not unrelated to this, on average across 2008–09, HMRC Contact Centres answered only 57% of all call attempts to their helplines. HMRC state that their performance is significantly affected by three key peaks of contact—Tax Credits Renewals (April to August), Child Benefit and return to education notifications (August and September) and the Self Assessment filing deadline (January), but that performance outside these peaks is better and that they answered 75% of call attempts for all but three weeks in the non-peak period. Even this off-peak rate though falls short, by a considerable margin, of their target to answer more than 90% of all call attempts by April 2011. Furthermore, the peak times themselves account in total for seven months—over half the year.

53. We were concerned that if the across year average was 57%, and the off-peak average was 75%, the average call response rates for the peak periods—not published by HMRC—must have been very low indeed. At our request, HMRC provided a more detailed breakdown—published below—which includes a call response rate low of 33% for July 08. The table also substantiates the Chief Executive’s claim that HMRC had “moved the call answering up quite a bit since then [2008–09],”⁸⁶ though there is still some way to go before the response rate can be said to be at an acceptable level.

Table 6: HMRC Call Response rates 2008–09 & 2009–10⁸⁷

Month	Peak Period (highlighted)	% Call Attempts Answered 08/09	% Call Attempts Answered 09/10
Apr	New Tax Year - PAYE Coding / Tax Credit Renewals	56%	77%
May	PAYE Coding / Tax Credit Renewals	44%	68%
Jun	Tax Credit Renewals	50%	80%
Jul	Tax Credit Renewals	33%	68%
Aug	Tax Credit Terminations and Child Benefit Full Time Non Advanced Education (FTNAE) Notifications	66%	73%
Sep	Child Benefit FTNAE Notifications	52%	74%
Oct		76%	
Nov		86%	
Dec		85%	

84 Q 200

85 Q 200

86 Q 204

87 Ev 93

Jan	Online Services / Taxes Helplines Final Filing date for SA Tax Returns	61%	
Feb		84%	
Mar		78%	
Total		57%	

54. In its Annual Report 2009, HMRC claims⁸⁸ that it is hitting its target to improve customers' experience, and that "results indicate that customer satisfaction exceeds our target levels."⁸⁹ We find it hard to reconcile these claims with its customer complaint levels and call response rates. Whilst we accept that these are not the whole picture, **we urge HMRC to reflect on whether customer experiences of HMRC are yet improving as much as the DSO2 "strong progress" summary implies. In particular, call response rates—though improving—remain at unacceptably low levels. The April 2011 target of answering 90% of calls remains challenging and will continue to require the attention of senior management.**

HMRC's transformation programme

55. Since its birth in 2005, HMRC has been a Department constantly going through changes. It has reduced its staff numbers by over 17,000 over a period of five years, and has relocated offices to reach further efficiency targets. Nor is this process yet at an end.

56. The transformation programme has been, and continues to be, very challenging for HMRC. There is evidence that it has had a knock-on effect on performance. As we noted with concern in a previous report,⁹⁰ eight out of ten areas assessed under HMRC's 2007 Capability Review required further development. We asked Chief Executive Lesley Strathie for her assessment of where HMRC stood two years after the Capability Review. She replied that "we feel that we have moved forward enormously but we still recognise that there is a lot more to do and we have plans about what we will do."⁹¹ She felt that "in most areas we have moved forward at least one level and in a couple of areas we think we have moved forward two."⁹² Her Minister, the Rt Hon Stephens Timms MP was equally upbeat, telling us that "HMRC has achieved an extraordinary amount in a relatively short time under enormous pressure."⁹³

57. When she gave evidence in October, she noted that the Cabinet Office capability team was in the process of conducting a two year re-review, and would be reporting on their self-assessment shortly. The Capability Re-Review was subsequently published in December 09, providing only partial vindication of her stance. Sir Gus O'Donnell, Cabinet

88 HM Revenue and Customs, *Departmental Report 2009*, July 2009, Cm 7691, p 50

89 *Ibid.*, p 52

90 Treasury Committee, First Report of Session 2008–09, *Administration and expenditure of the Chancellor's departments, 2007–08*, HC 35

91 Q 154

92 Q 155

93 Q 478

Secretary and Head of the Home Civil Service congratulated HMRC on making good progress over the two years, noting in particular its effectiveness in providing well-structured and practical support in response to the changing economic conditions. However, whilst she had hoped that HMRC would move forward in most areas, it has in fact only moved forward in three out of ten. Also, whilst the Chief Executive had hoped that HMRC would move forward two categories in two areas, HMRC has in fact moved forward two categories in only one—‘set direction’. Seven ‘development areas’ remain of which one—‘ignite passion, pace and drive’—is assessed as an ‘urgent’ development area. Sir Gus O’Donnell also notes that “HMRC faces a huge transformation challenge which will take both time and leadership attention, in particular to rebuild staff confidence in HMRC’s leadership and inspire staff to be a part of HMRC’s future.”⁹⁴

58. On balance, performance at HMRC remains mixed with considerable room for improvement, and considerable challenges remain to be overcome if HMRC is to achieve this improvement. In the remainder of this section, we take a closer look at three of the main challenges.

Staff morale

59. In a previous report, drawing on an NAO assessment of HMRC’s transformation programme,⁹⁵ we observed that:

We note the National Audit Office’s assertion that, in order to maximise the benefits of its Transformation Programme, HMRC must convince staff of its benefits. The low levels of morale within the Department are startling with profound potential impacts on both the Transformation Programme and core service delivery. We will continue to monitor the efforts made by senior management to improve matters. We seek an explanation of how Ministers will monitor and report progress.⁹⁶

More recently, the Cabinet Office Capability Re-review also highlighted the need to rebuild staff confidence and inspire staff. It is understandable that staff morale at HMRC should be fragile. Since its conception, HMRC has been a Department under pressure to find efficiencies by way of staff reductions and relocations. The table below shows the number of full time equivalents in post over the past five years. Some 16,818 full time posts will have been removed by the end of 2008–09 since 2004–05, and a further 3,811 will be cut in the twelve months to the end of 2009–10:

94 Civil Service Capability Reviews, *HM Revenue and Customs: Progress and Next steps*, December 2009, p 7

95 National Audit Office, *HM Revenue and Customs Transformation Programme*, July 2008, p 6

96 Treasury Committee, First Report of Session 2008–09, *Administration and expenditure of the Chancellor’s departments 2007–08*, HC 35, p 28

Table 7: HMRC Staffing Numbers⁹⁷

	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09 (plans)	2009-10 (plans)
Permanent staff	95,896	98,821	95,337	91,373	85,769	82,003	78,192
Overtime	1,452	822	783	750	1,032	503	503
Total	97,348	99,643	96,120	92,123	86,801	82,506	78,695

Table excludes Valuation Office Agency staff. 2003–04 figures are pre-merge. 2009-10 planned figures include Detection/UKBA

60. In view of our previous conclusions, we were particularly concerned by the dire results for HMRC of a cross-Government staff survey pilot study conducted in February 2009. This survey assessed employee engagement at HMRC both in percentage terms and ranked against the responses of staff in ten other Government Departments.

61. Out of the 67 ranked questions, HMRC is top in relation to 2 questions regarding data handling and data security, which does at least provide an indication that lessons have been learnt since the loss of the child benefit data of 25 million people in 2007–08. However, HMRC is ranked 10th (out of 11) for 22 questions, and 11th for 31 questions. The following box captures some of the low-lights:

HMRC as a whole is well managed—11% positive.

HMRC ranks 11th out of 11 Departments and this score is 16% lower than the median score across the other Departments taking part.

I feel that change is well managed in HMRC—11% positive.

HMRC ranks 11th out of 11 Departments and this score is 9% lower than the median score across the other Departments.

When changes are made they are usually for the better—9% positive.

HMRC ranks 11th out of 11 Departments and this is 10% lower than the median score across the other Departments.

Overall, I have confidence in the Senior Civil Servants in HMRC—11% positive.

HMRC ranks 11th out of 11 Departments and this score is 21% lower than the median score across the other Departments.

HMRC energises me to 'go the extra mile'—12% positive.

HMRC ranks 11th out of 11 Departments and this is 17% lower than the median score across the other Departments.

- *I have confidence in the decisions my line manager makes*—56% positive.

HMRC ranks 10th out of 11 Departments and this score is 12% lower than the median score across the other Departments.

- *My line manager motivates and inspires me to be more effective in my job*—47% positive.

HMRC ranks 10th out of 11 Departments and this score is 10% lower than the median score across the other Departments.

- The **Employee Engagement score**, consisting of three elements (speaking positively about the organisation, wishing to stay, and going the extra mile) was 32%.

This is 16% lower than the median score across the 11 Government Departments.

62. We asked the Chief Executive what she could say to convince us that HMRC senior management was taking its staff with them. She replied, frankly, that “in short, the survey tells us we are not and we take that incredibly seriously.”⁹⁸ A further challenge she drew out was that, not only does she have an unhappy workforce, she has an unhappy workforce that intends to stay with the organisation.

63. We questioned her as to what effect a disengaged workforce with poor morale was having on performance—whether, for instance, HMRC had lost out on tax revenue. She replied that “I do not believe so, but I do not know so.”⁹⁹ Her Minister, the Rt Hon Stephen Timms also stated that he did not have a projection for tax collection losses due to low morale¹⁰⁰ but he did affirm that “the evidence that high morale leads to good performance is compelling.”¹⁰¹

64. Finally, we asked Lesley Strathie what plans she had in place to address the morale—and performance—issues raised by the survey. She recognised that her workforce needed clarity “about whether they have a future in the department, what that future looks like...”¹⁰², and stressed that “my job, I believe, is to be absolutely honest with our people”¹⁰³ including “if at the end of the day there is not a job.”¹⁰⁴ She also saw a need to build up the tax profession to “upskill and accredit our people.”¹⁰⁵ She acknowledged too that management needed to do more, telling us that “many of our managers do not believe they

98 Q 156

99 Q 164

100 Q 488

101 Q 486

102 Q 156

103 Q 157

104 Q 157

105 Q 255

need to change, and clearly we all need to change.”¹⁰⁶ This is particularly concerning, given that much of the most severe criticism in the survey is aimed at management, especially senior management.

65. Without downplaying the significance of the survey, she also suggested that it did not tell the whole story:

...I would say that every week I visit a part of HMRC and every week I see people working incredibly hard, incredibly proud of what they do and working flat out to close the tax gap or hit any of our other priorities...I do not take the survey as the only measure of morale, that is my point, but I do take it really seriously that people want to stay with us but do not want to recommend us or say that they are proud to work for us.¹⁰⁷

66. We are deeply concerned about employee engagement at HMRC and its effect on performance. We accept that the relatively new senior management team is aware of the issue, and takes its implications seriously. Nonetheless, we are deeply troubled by the apparent absence of any detailed plan to ameliorate the situation. We recommend that HMRC's management re-double their efforts to re-engage with their workforce, and publish a clear and detailed plan to provide focus and direction to their actions. We will continue to monitor this issue closely.

IT

67. We have assessed HMRC's IT performance in previous reports. HMRC is a large organisation dealing with a wide range of taxes. In a note to the Committee, it stated that there are 92 systems which are critical to HMRC's core processes. Many of these IT systems have had substantial investment in recent years, but progress has been uneven.

68. In a previous report,¹⁰⁸ we recommended that HMRC improve its contracts with IT providers, noting that one new IT system had been delayed by a year. One consequence of this delay is that, during 2008–09, the number of open cases (where a case requires manual clerical attention) increased from 16.2 million in 2007–08 to 35 million. Against this background, we were surprised to see HMRC declare in its Annual Report that “HMRC has been hailed as a shining example of how to use technology to take government services to a new level.”¹⁰⁹ Lesley Strathie, however, remained bullish about HMRC's IT progress, including a new agreement with its suppliers under the Aspire contract “which will significantly reduce cost for department over the coming years.”¹¹⁰

106 Q 256

107 Q 159

108 Treasury Committee, First Report of Session 2008–09, *Administration and expenditure of the Chancellor's departments, 2007–08*, HC 35

109 HM Revenue and Customs, *Departmental Report 2009*, July 2009, Cm 7691, p 11

110 Q 238

69. Future performance at HMRC is highly dependent upon improvements to its IT systems. We will continue to monitor progress of its IT up-grading progress, including the new Aspire contract.

Mapeley contract

70. In 2001 the Inland Revenue and HM Customs & Excise signed a 20-year contract with Mapeley STEPS Contractor Limited, in order to rationalise its estate. Under the terms of the contract, HMRC can hand over to Mapeley up to 60% of its estate and incur no penalties, so long as Mapeley receives 12 months notice for each transfer. There is an annual limit of how much space the Department can return to Mapeley in one year, but if this allowance is not used it can be rolled forwards to the following year.

71. Under the STEPS deal (the Strategic Transfer of the Estate to the Private Sector), the Department sold 132 freehold properties to Mapeley and now leases them back. Mapeley manages these, and 459 properties the Department leases from third-party landlords, and provides facilities management and maintenance services on the total 591 properties in return for fixed monthly payments from the Department.

72. Once transferred, Mapeley takes on all the risk of running the properties, and any risks associated with fluctuations in value of the estate. At one level, this appears a very good contract for HMRC, giving it a high degree of flexibility with a sizeable chunk of risk transferred to Mapeley. We have, however, expressed concern about Mapeley's performance in previous reports—for instance last year¹¹¹ we expressed concern about Mapeley's building maintenance record. Moreover, between our evidence session with HMRC and our evidence session with Ministers, the NAO published a report into the Mapeley deal¹¹² which drew attention to significant underlying weaknesses.

73. The NAO found that Mapeley's bid was £500 million cheaper than other bids. Whilst, therefore HMRC received a good price for the contract, there were risks associated with the aggressively low nature of Mapeley's bid and its status as a new company entering the market. Mapeley's bid was based on speculative returns from increases in property values over the 20 years, and expected minimal operating profits. It was not altogether surprising therefore that, seven months into the contract, Mapeley approached HMRC with cash problems. In more recent years, HMRC has increased the number of properties it wishes to vacate. However, the NAO found that HMRC did not consider the financial impact of this on Mapeley or the potential consequences for HMRC:

This programme creates financial pressures for Mapeley, further exacerbated by the economic downturn and falling property values. The Department could incur significant costs in the event of Mapeley default, including one-off costs of £40-110

111 Treasury Committee, First Report of Session 2008–09, *Administration and expenditure of the Chancellor's departments, 2007–08*, HC 35, p 31

112 National Audit Office, *HM Revenue and Customs' estate private finance deal eight years on*, December 2009

million for unpaid rent and suppliers. There would also be substantial ongoing costs relating to estates management and increased rent liabilities.¹¹³

The NAO report accepts that HMRC has taken some measures to improve its management of the contract, but stresses that there is still not a fully effective partnership in place.

74. We put it to the Financial Secretary that the Government had still fully to grasp the downside risks of this contract. He replied that:

...we certainly have been considering the issues that might arise with the Mapeley contract, including whether there is a risk to Mapeley and other contingencies that we need to think through. Our view is that we have obtained quite impressive value from the contract...The NAO has said in its new report that a number of things need to be done to ensure that we do secure the full value from that contract over its life. We accept that...¹¹⁴

We pressed him on Mapeley's capacity to absorb a large amount of property being transferred back to it in a recession. He responded that "we are certainly aware of those challenges, which are indeed clear, and we are aware of the risks that they pose to Mapeley, and so HMRC has carried out quite a lot of work to understand the nature of the financial risks to Mapeley and how they can be addressed."¹¹⁵ We further sought clarity as to whether, as the NAO had concluded, HMRC had yet to agree a way forward with Mapeley that avoided placing too much strain on the contract whilst preserving benefit for HMRC. In supplementary written evidence, the Government informed us that:

a financial model has been constructed which shows the impact of a variety of factors on Mapeley's financial viability...Mapeley were fully consulted during the development of the model and provided property specific data and management information relating to their own cash flows. These inputs are fed into the model so that it can be used for robust decision-making...HMRC has discussed the results of the initial modelling with Mapeley with a view to identifying the options for maximizing HMRC's capacity to use the STEPS contract to generate financial efficiencies, whilst ensuring the ongoing financial viability of the partnership arrangement¹¹⁶

The supplementary evidence concludes that "through this planning and the work on Mapeley's financial viability, HMRC's Executive Committee is confident in its ability to manage any risks to its estates management plans effectively."¹¹⁷

75. It seems clear from the recent NAO report into the HMRC contract with Mapeley, that HMRC has been slow to consider the possibility that the terms of the contract could put the latter under immense financial strain. It appears that HMRC believed it

113 National Audit Office, *HM Revenue and Customs' estate private finance deal eight years on*, December 2009, p 6

114 Q 420

115 Q 423

116 Ev 110

117 Ev 110

had transferred all substantive risks to Mapeley, and did not envisage the possibility of the risks returning to them if Mapeley should default. We accept HMRC is now taking steps to improve its management of the contract. We remain to be convinced, however, that sufficient risk management, including a clear and mutually beneficial way forward, is yet in place, and will return to this topic in future evidence sessions.

5 NS&I

76. Established in 1861, NS&I was originally known as the Post Office Savings Bank. It became a Government Department in 1964, then an Executive Agency of the Chancellor of the Exchequer in 1996, and was re-branded as NS&I in 2002. NS&I is one of the largest savings organisations in the UK, with investments of over £97 billion at the end of March 2009 (representing 12.24% of National Debt) and annual flows in excess of £35 billion.

77. NS&I's vision is “securing a better financial future for our customers by providing the most valued and trusted savings experience.”¹¹⁸ However, as confirmed by its mission statement, it is part of the UK's debt management arrangements:

Our overall aim is to help reduce the cost to the taxpayer of government borrowing now and in the future. With this in mind, our single, long-term strategic objective is to provide the Government with cost-effective retail finance compared with raising funds on the wholesale market.

Future challenges for NS&I

78. As we noted in section 2, from September 2009 NS&I successfully processed a record amount of new business as—at the height of the economic crisis—customers prized Government-backed security for their savings over the higher interest rates offered by commercial savings institutions. These exceptional circumstances posed a particular dilemma for NS&I which, as presently constituted as an Executive agency of the Treasury, has to tread a fine line between providing a good deal for its customers (its vision) and supporting Government macro-economic policy (its mission). During 2008–09 the risk to the Government was that NS&I was becoming too attractive to customers, at a time when it was seeking to re-inject confidence into the commercial banking system. Equally though, closing NS&I to new business could also jeopardise public confidence and hence financial stability. Jane Platt, NS&I's Chief Executive, explained to us the reasoning at the time:

In August of last year we were on track to be raising £4 billion of net financing for the Treasury, which was the agreed amount we had set off to raise. After the Lehmans crisis it was very, very clear that we were going to be receiving a large volume of unsolicited funds coming into NS&I, and at that point we had to make a decision. Do we stay open for business and allow net financing to rise very well above the amount we had previously agreed, or should we actually stop not only marketing our products but also allowing people to invest in them.¹¹⁹

The solution agreed between the Treasury and NS&I was for NS&I, during the autumn and winter of 2008-09, to “cease all discretionary marketing but stay open for business...Because you could imagine what would have happened if NS&I had not been open for business at a time when people were so concerned about their savings.”¹²⁰ NS&I

¹¹⁸ National Savings and Investments, *Annual Report and Accounts 2008–09*, July 2009, HC 470, p 2

¹¹⁹ Q 39

¹²⁰ Q 39

also reduced its interest rates across its product range. For example the interest rate on premium bonds fell from 3.4% on 1 May 2008 to 1.0% on 1 April 2009. Fixed interest savings certificates offered at 3.5% AER in June 2008, were available at 0.95% AER in February 2009.

79. At one level this was a pragmatic response to a tricky dilemma, essentially aimed at curbing the volume of new business by ensuring that NS&I did not draw attention to itself. It does though show that, at the bottom line, the NS&I is there for the Government rather than customers. We put this assessment directly to Exchequer Secretary Sarah McCarthy-Fry MP, who endorsed it:

Q529 Mr Brady: Can I ask what NS&I's top priority for the future should be? Is it there to provide value for its customers or to support government macroeconomic policy?

Sarah McCarthy-Fry: The sole aim of NS&I is to reduce cost to the taxpayer of Government borrowing now and in the future, and they do that through the sale of savings and investment products to the retail market.

Q530 Mr Brady: So it is not there for its customers; it is there for Government macroeconomic policy?

Sarah McCarthy-Fry: That is the purpose of it, and, obviously, if they can help their consumers and their customers—they do not set out to be the absolute best buy, so in that sense they are not setting out to attract the customers. Their aim is to reduce the cost to the taxpayer of Government borrowing.

80. As we noted in section 2, and in other recent reports, extremely testing economic times are by no means at an end, and it is likely that NS&I's particular role and priorities will continue to come under scrutiny. For example, so long as Northern Rock exists as a fully nationalised bank, NS&I's unique selling point as the safest haven for savings appears compromised. There is also the risk that, as confidence in the commercial sector returns, the NS&I will experience a 'flight from safety.' Equally, so long as interest rates remain low, and commercial savings institutions remain under pressure to recover their positions, NS&I will be vulnerable to accusations that its more attractive products constitute unfair competition. It is noteworthy, in this context, that NS&I's net financing target for 2009–10 is to maintain a neutral position. NS&I and the Treasury will have to steer a careful course over the next few years.

Siemens contract

81. NS&I signed a public/private partnership contract with Siemens in 1999 for ten years, subsequently extended to fifteen years, for the provision of operational services such as call centres and back office product processing. Noting that the amount paid to Siemens had increased by about £20,000 during 2008–09, we sought confirmation that this contract represented value for money. Steve Owen, NS&I's Channel Delivery and Management Director, confirmed to us that he was satisfied that Siemens was not making excessive profit, asserting that "we did a great deal of work to ensure the amount we paid to Siemens

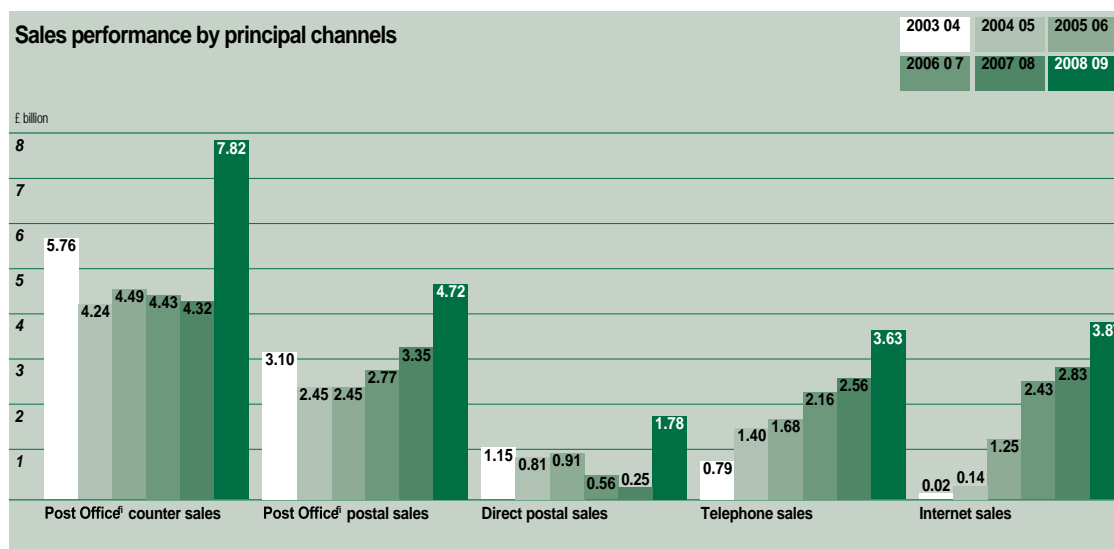
was the correct sum¹²¹ and that “we do continue to monitor on an ongoing basis.”¹²² He also explained, in more detail, that:

...The other element that gives me confidence that the amount we paid is not excessive is that we can compare it with the average costs at the original tendering back in 1999 to see if we were paying more or less per transaction or per customer than we were when we went to the market for a competitive tender. And we are actually paying significantly less than we were back in 1999 per customer or per transaction.¹²³

Post Office contract

82. Finally, we asked NS&I about the future of its relationship with the Post Office. The Post Office is currently NS&I's core distributor, selling NS&I products over the counter and through postal sales. As the table below shows, a disproportionately large amount of the additional NS&I sales during 2008–09 were conducted over the counter at the Post Office. Jane Platt told us that “last year the percentage of business that we did through the Post Office was about 60%”¹²⁴ explaining that “there was definitely a discernible trend that because people were very concerned about security overall, it was important for them to have the physical transaction and a piece of paper that was stamped in the Post Office when they actually invested their savings.”¹²⁵

Table 8: Sales performance by principal channels¹²⁶



83. In the future, NS&I expects to reduce its dependence upon the Post Office as it looks to develop other channels—postal, telephone and internet. So, in 2009–10, when, as noted

121 Q 57

122 Q 58

123 Q 58

124 Q 62

125 Q 65

126 National Savings and Investments, *Annual Report and Accounts 2008–09*, July 2009, HC 470, p 20

previously NS&I is aiming to balance inflows and outflows, without any overall business growth, it is expecting the percentage of business conducted through the Post Office to fall to 50%.

84. Whilst it is perfectly reasonable for NS&I to focus on its own future, its plans to reduce its dependence upon the Post Office do play into a wider debate about how best to secure the future of the Post Office network. The Government provides a Social Network payment to sustain the Post Office network which amounts to £150m a year. Last year, at the behest of the Government, the Business, and Enterprise Committee¹²⁷ considered what services could be provided by the post office network to secure its future viability. In its report—“Post Offices—securing their future”—the Committee noted the disjunction between the Government’s recognition that the Post Office network performs a vital function and individual departments’ actions in reducing use of the post office to drive down their costs. The Business and Enterprise Committee concluded:

it is bizarre that government policy recognises the value of the network, but that individual departments do not see that they have a role in making sure that everybody, not just the web enabled, has access to their services, and that taking this seriously by using the post office network more could contribute to wider policy aims...¹²⁸

Whilst we recognise that it may make business sense for NS&I to move away from the Post Office, it is a Government-owned body. We recommend, therefore, that the Government considers whether there is a wider public interest in retaining stronger links between the Post Office and NS&I both to ensure that all sections of the public have easy access to NS&I products and to help secure the future of Post Offices.

127 Now the Business, Innovation and Skills Committee

128 Business and Enterprise Committee; Eighth Report of Session 2008-09, *Post Offices—scrutinising their future*, HC 371-i, para 85

6 The Royal Mint

Background

85. The activities of the Royal Mint consist of the manufacture and supply of circulating and commemorative coins in the UK and overseas, the manufacture and supply of official medals, seals and dies, and the marketing of technical services relating to the manufacturing of coins and blanks.

86. The Royal Mint has been operating as a Trading Fund since 1 April 1975 and on 1 April 1990 became an Executive Agency of HM Treasury. The Chancellor of the Exchequer is the Master of the Mint, and on 21 April 2009 he announced that the Royal Mint would be vested into a Government-owned company by 31 December 2009.

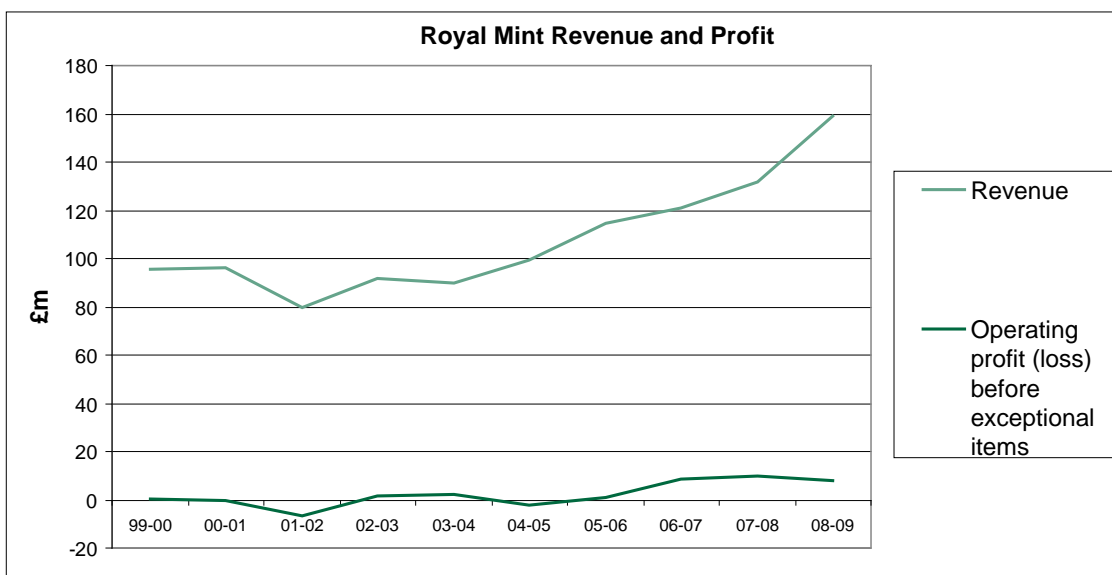
87. During 2008–09, as a trading fund, the Royal Mint operated on commercial lines but was legally required to manage its funded operations so that the revenue of the fund was sufficient to meet its outgoings and that any operating loss in one year was made good in subsequent years. In this section we assess its performance during 2008–09, and the implications of the vesting decision.

Performance

88. In 2008–09, Operating profit before exceptional items and interest was £8.2 million based on sales of £159 million, compared to a higher profit of £9.6 million on lower sales of £131.8 million in 2007–08. Profit after exceptional items and interest was £4.3 million compared to £7.2 million for the previous year. The average rate of return, therefore, dropped from 9.2% in 2007–08 to 7.1% in 2008–09. This measure is used as a key ministerial target for the Royal Mint. The target was set at 5.1% in 2008–09 and was therefore achieved. It is set at a more challenging 10% in 2009–10.

89. As can be seen in the table below, the Royal Mint has had a varied financial performance over recent years, and following a period of losses returned to profitability in 2006–07:

Table 9: Royal Mint revenue and profit



90. During our evidence session with the Royal Mint, we expressed concern that a drop in profit and rate of return based on an increasing value of sales suggested that the Mint’s new management team was not fully sustaining recent improvements. Chief Executive Andrew Stafford explained these figures by referring to the changing nature of the Royal Mint’s business mix, observing that:

the mix of our business did change quite substantially year on year, particularly in the commemorative coin business where a lot of the turnover in the last twelve months was from bullion coin as people sought to buy more gold coins at a much lower margin than our collector coins.

Consequently, he felt that, though his average rate of return on capital employed had gone down, “it is still a very healthy return for a manufacturing organisation.”¹²⁹ He also did not see a declining average rate of return on capital employed turning into a trend as “if I look at our current strategy for this year we are increasing our circulating coin business overseas and as a result we are now seeing a dramatic improvement again.”¹³⁰

91. We accept that Royal Mint rates of return will be affected by changes in consumer demand for products of varying margins of profitability, and note that the rate of return remains relatively healthy at 7.1%. However, given that Royal Mint only returned to profit in 2006–07, positive future performance can not be taken for granted and we will monitor, with interest, the level of profit the Royal Mint declares for 2009–10 and whether it succeeds in meeting its 10% average rate of return target.

129 Q 80

130 Q 81

Change in accounting policy

92. In 2008–09 the Royal Mint transferred an exceptionally large amount—£8,004,000—from its revaluation reserve to its profit and loss account.¹³¹ The revaluation reserve is a non-distributable reserve and records the gains or losses on assets as they are revalued. By transferring them to the profit and loss account, they were transferred to a distributable reserve, which shareholders could use to extract money in the form of dividends.

93. The following table, extracted from the relevant years' "Movement in Capital and Reserves (Government Funds)" tables, compares the figures transferred in previous years:

Table 10: Royal Mint Movement in Capital and Reserves

Year	Description	Revaluation Reserve £'000	Profit and Loss Account £'000
2008-09	Transfers	(8,004)	8,004
2007-08	Transfers relating to depreciation	(241)	241
2006-07	Reclassification	(202)	202
2005-06	Reclassification to distributable reserves	(188)	188

94. In a supplementary note¹³², the Royal Mint attributed the bulk of the transfer (£7,086,000) to a change in accounting policy regarding the valuation of the 'Base Stock' of metals held by the Mint.

95. In previous years, the stock was measured on a historical cost basis. This means that the value of the metal in the accounts was the price at which it was purchased. An adjustment would then be put through at the year end to reflect the fact that metal prices may have moved from the purchase date. Royal Mint stated that this method was inconsistent with UK Generally Accepted Accounting Principles (UK GAAP), the principles to which Government Departments and bodies must adhere in preparing accounts.

96. During 2008–09 the Royal Mint changed their stock accounting policy to a First-In-First-Out (FIFO) basis, which they felt was consistent with UK GAAP. Under the FIFO arrangement, the Royal Mint works on the basis that the oldest metals brought are recorded as sold first. This means that any remainder stock left at the year end will be recent purchases closer to current market value. This change was disclosed as part of Note 1 of the accounts which states;

The Royal Mint has reviewed its method of accounting for metal stocks. A standard costing system of valuing metal stocks has been introduced and all metal stocks are

¹³¹ The Royal Mint, *Annual Report and Accounts 2008–09*, June 2009, HC 570, p 41

¹³² Ev 99

valued on a FIFO basis. The change in method has not had a material impact on the financial statements.¹³³

97. The Committee is pleased that the Royal Mint has changed its accounting policy to ensure consistency with UK GAAP and we note the disclosure in the accounts. However, given the size of the adjustment, we do not believe that the disclosure is detailed enough for the reader of the accounts to understand the reasons for the change in the reserves. We recommend that any future changes in accounting policy of this nature are more clearly explained, with the reasons behind such changes provided in the accounts, especially where previous policies are found to be non-compliant with UK GAAP.

Vesting

98. Plans to vest the Royal Mint, turning it into a Government owned company, were first announced in December 2004. These were put on hold in 2006 pending the recruitment of a new Chief Executive.¹³⁴ On 21 April 2009 the Chancellor of the Exchequer announced that the Royal Mint would be vested into a company by the end of 2009.

99. The Government's rationale for vesting is that it will allow the Royal Mint to take advantage of wider commercial opportunities, including potentially the introduction of private capital. We asked Andrew Stafford if he could elaborate on the advantages of vesting as a Government owned company. He offered two specific things:

one is the acquisition of other organisations which would allow us to expand internationally, and secondly undertaking joint ventures with overseas partners to enable us to penetrate markets, for example Asia, where we have a presence but we would need to have a greater level of presence for a manufacturing capability. Both of those things, whether it is an acquisition or a joint venture, would clearly require a capital injection into the business. If the Treasury did not feel that that was a good use of public money to make those investments, then clearly private capital is an alternative way of pursuing both joint ventures and acquisitions.¹³⁵

He went on to clarify that he was “not necessarily” looking solely at commercial opportunities overseas:

For example, one or two of the acquisitions that could be undertaken in the business would be for UK operations, which could be combined with the Llantrisant operation. So there are specific opportunities in the UK as well as overseas.¹³⁶

100. We asked Andrew Stafford whether the timing was right given the economic climate and that the Royal Mint had only recently returned to profitability. He responded that:

133 The Royal Mint, *Annual Report and Accounts 2008–09*, June 2009, HC 570, p 46

134 The Royal Mint, *Annual Report and Accounts 2007–08*, June 2008, HC 570, p 15

135 Q 94

136 Q 96

...We have demonstrated now for the third consecutive year that this business is a successful business making a good return for its shareholder. We have a long-term strategy in place involving both growth in our UK commemorative coin business and in our international circulating coin business. We have secured long-term contracts in major overseas markets such as Russia. We have secured a major capital investment programme for the business to increase our manufacturing capability, so we believe that the strategy and the capability are in place for long-term sustainable, profitable growth.¹³⁷

He would not be drawn on whether the long-term strategy included privatisation. Exchequer Secretary Sarah McCarthy-Fry MP was also coy on this point, simply asserting that “the current view is that the purpose of vesting was not as a prelude to privatisation.”¹³⁸

137 Q 83

138 Q 510

7 Other associated bodies

101. Although they are not the main subject of our scrutiny this year, we did write to the Treasury's other associated bodies to solicit updates on key issues, and also raised some of them with Ministers. In this section we highlight two of the outcomes that emerged from this process.

Valuation Office Authority

102. Last year, we expressed our concern at the manner in which the revaluation of UK statutory ports had been handled and implemented. We noted in particular that Port Occupiers are facing bills for backdated business rates which do not take account of payments they have already made to Port Operators towards rates. We recommended that the Government take steps to ensure that the financial liabilities faced by Port Occupiers take such payments into account. In its response to our report, although the Government did not agree with all our reasoning it did tell us that "Ministers are meeting representatives of some of the port operators to discuss the issues."¹³⁹ We were, therefore, dismayed to learn from Rt Hon Stephen Timms that "this is clearly a matter between the ports and their tenants"¹⁴⁰ and that "I am not aware of ministers having been involved in that."¹⁴¹

103. We are not impressed by the Government's decision to wash its hands of problems which arise, in part, from its own insensitive handling of port rate revaluation. We recommend that the Government urgently reviews the impact of the port revaluation on port occupiers, and publishes its findings.

Government Actuary's Department

104. We asked GAD about its overall finances, and sought information in particular on its response to the economic crisis, performance, staffing, VIP events, miners pension scheme and new accommodation. We were impressed by the clear and informative GAD response to our letter. We were pleased to see that GAD has had a successful year. We did note though that GAD has been unable to move into a new office as planned, and now expects to stay at Finlaison House for the foreseeable future. GAD drew our attention to the fact that "as a result of our failure to move, our finances are very vulnerable to sub-tenants leaving. We could in the next year or two face a hit to our net costs of over £1M based on what may or may not happen. We are in discussions with Treasury and OGC about managing this potential exposure."¹⁴² **We will continue to monitor the financial risk to GAD arising from the need to remain at Finlaison House, and request that, in its**

¹³⁹ Treasury Committee, *Administration and expenditure of the Chancellor's departments, 2007–08: Government Response to the Committee's First Report of Session 2008–09*, April 2009, HC 419, p 17

¹⁴⁰ Q 512

¹⁴¹ Q 513

¹⁴² Ev 118

response to this report, the Government explains its contingency plans for GAD in the event that sub-tenants leave.

Conclusions and recommendations

Measuring Performance

1. We remain unconvinced that HM Treasury's present DSO outcome 1(a) temporary indicator serves any real value. We will monitor with interest the extent to which the Fiscal Responsibility Bill, should it become law, comes to provide a rule against which such measurement can be made. (Paragraph 16)
2. It would have been helpful to have seen NS&I's proxy measure, and the rationale behind it, clearly set out in its 2008–09 Annual Report. We recommend that, if circumstances do not allow the re-instatement of the Value Add measure during the course of 2009–10, the proxy measure is given greater prominence in next year's NS&I Annual Report. (Paragraph 17)

Unfinished Business

3. It appears to us that the relationship between the Treasury and UKFI remains a work in progress, and we recommend that the Government considers whether the formal terms of the relationship need some re-definition in the light of experience. It is important that the lines of demarcation are clear, and reflect the reality on the ground, not least to ensure that other shareholders are properly protected. (Paragraph 21)
4. It is very difficult to draw final conclusions regarding the level of success that should be attributed to HM Treasury and its associated bodies for 2008–09—too much remains unfinished business. (Paragraph 24)
5. We appreciate the magnitude of the challenges faced by HM Treasury and its associated bodies during the course of this extraordinary year, and commend the extent to which the workforce has been willing to go the extra mile in response to these challenges. It is important though that Departments do not take this commitment for granted and continue to monitor for signs of burn-out and over-stretch. This is particularly important because, as we have highlighted above and in other recent reports, the challenges posed during this extraordinary period remain very much ongoing business. (Paragraph 31)

DS01

6. We look forward to seeing a significant improvement in the timeliness and accuracy of Departmental monthly in-year monitoring figures next year, as the actions highlighted by the Permanent Secretary and Minister take effect. (Paragraph 36)
7. Whilst we understand the logic of the Treasury's position, it still appears disingenuous to claim, with no further explanation, that a target has been met when that target has in fact been missed in eleven months out of twelve, and we recommend that the Treasury reflects on the terminology used to assess this indicator. (Paragraph 38)

8. We recommend that the next Treasury Committee test whether this commitment to provide a DSO2 indicator for pensioners has been fulfilled next year. (Paragraph 39)

PSA9—Child Poverty

9. We reiterate our 2009 Pre-Budget Report recommendation that the Government clearly sets out the steps it proposes to take to move nearer its 2010–11 target in the time available and to achieve the eradication of child poverty by 2020. (Paragraph 41)

Implementation of International Financial Reporting Standards

10. We reiterate our view that future Pre-Budget and Budget Reports should include a reconciliation between Public Sector Net Debt calculated on a national accounts basis, and the same figure calculated using the IFRS principles which apply to departmental accounts. (Paragraph 42)

HMRC

11. The absence of regular public reporting on milestones by HMRC is a major obstacle to both effective scrutiny and performance. We believe that HMRC must publish data regularly to chart its level of progress against DSO1 indicators; and set these out in its Annual Reports. We believe this is essential for the tax gaps to be closed and for the assessment accuracy and take-up of the working tax credit to be improved, especially for those without children, and those whose incomes and jobs are volatile and constantly changing. (Paragraph 49)
12. We urge HMRC to reflect on whether customer experiences of HMRC are yet improving as much as the DSO2 “strong progress” summary implies. In particular, call response rates—though improving—remain at unacceptably low levels. The April 2011 target of answering 90% of calls remains challenging and will continue to require the attention of senior management. (Paragraph 54)
13. On balance, performance at HMRC remains mixed with considerable room for improvement, and considerable challenges remain to be overcome if HMRC is to achieve this improvement. (Paragraph 58)
14. We are deeply concerned about employee engagement at HMRC and its effect on performance. We accept that the relatively new senior management team is aware of the issue, and takes its implications seriously. Nonetheless, we are deeply troubled by the apparent absence of any detailed plan to ameliorate the situation. We recommend that HMRC’s management re-double their efforts to re-engage with their workforce, and publish a clear and detailed plan to provide focus and direction to their actions. We will continue to monitor this issue closely. (Paragraph 66)
15. Future performance at HMRC is highly dependent upon improvements to its IT systems. We will continue to monitor progress of its IT up-grading progress, including the new Aspire contract. (Paragraph 69)
16. It seems clear from the recent NAO report into the HMRC contract with Mapeley, that HMRC has been slow to consider the possibility that the terms of the contract

could put the latter under immense financial strain. It appears that HMRC believed it had transferred all substantive risks to Mapeley, and did not envisage the possibility of the risks returning to them if Mapeley should default. We accept HMRC is now taking steps to improve its management of the contract. We remain to be convinced, however, that sufficient risk management, including a clear and mutually beneficial way forward, is yet in place, and will return to this topic in future evidence sessions. (Paragraph 75)

NS&I

17. Whilst we recognise that it may make business sense for NS&I to move away from the Post Office, it is a Government-owned body. We recommend, therefore, that the Government considers whether there is a wider public interest in retaining stronger links between the Post Office and NS&I both to ensure that all sections of the public have easy access to NS&I products and to help secure the future of Post Offices. (Paragraph 84)

Royal Mint

18. We accept that Royal Mint rates of return will be affected by changes in consumer demand for products of varying margins of profitability, and note that the rate of return remains relatively healthy at 7.1%. However, given that Royal Mint only returned to profit in 2006–07, positive future performance can not be taken for granted and we will monitor, with interest, the level of profit the Royal Mint declares for 2009–10 and whether it succeeds in meeting its 10% average rate of return target. (Paragraph 91)
19. The Committee is pleased that the Royal Mint has changed its accounting policy to ensure consistency with UK GAAP and we note the disclosure in the accounts. However, given the size of the adjustment, we do not believe that the disclosure is detailed enough for the reader of the accounts to understand the reasons for the change in the reserves. We recommend that any future changes in accounting policy of this nature are more clearly explained, with the reasons behind such changes provided in the accounts, especially where previous policies are found to be non-compliant with UK GAAP. (Paragraph 97)

Valuation Office Agency

20. We are not impressed by the Government's decision to wash its hands of problems which arise, in part, from its own insensitive handling of port rate revaluation. We recommend that the Government urgently reviews the impact of the port revaluation on port occupiers, and publishes its findings. (Paragraph 103)

Government Actuary's Department

21. We will continue to monitor the financial risk to GAD arising from the need to remain at Finlaison House, and request that, in its response to this report, the

Government explains its contingency plans for GAD in the event that sub-tenants leave. (Paragraph 104)

Formal Minutes of the Treasury Sub-Committee

Wednesday 24 February 2010

Members present:

Mr Michael Fallon, in the Chair

Nick Ainger	Mr Mark Todd
Jim Cousins	Mr Andrew Tyrie
John McFall	Sir Peter Viggers
John Thurso	

Draft Report (*Administration and expenditure of the Chancellor's departments, 2008–09*), proposed by the Chairman, brought up and read.

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

Paragraphs 1 to 104 read and agreed to.

Summary read and agreed to.

Resolved, That the Report be the First Report of the Sub-Committee to the Committee.

Ordered, That the Chairman make the Report to the Committee.

[Adjourned till Wednesday 3 March at 2.15 pm]

Formal Minutes of the Treasury Committee

Wednesday 24 February 2010

Members present:

John McFall, in the Chair

Nick Ainger	Mr Mark Todd
Jim Cousins	Mr Andrew Tyrie
Mr Michael Fallon	Sir Peter Viggers
John Thurso	

Draft Report (*Administration and expenditure of the Chancellor's departments, 2008–09*), proposed by the Chairman, brought up and read.

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

Paragraphs 1 to 104 read and agreed to.

Summary read and agreed to.

Resolved, That the Report be the Seventh Report of the Committee to the House.

Ordered, That the Chairman make the Report to the Committee.

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

Written evidence was ordered to be reported to the House for printing with the Report, together with written evidence reported and ordered to be published on 12 January.

[Adjourned till Tuesday 2 March at 9.15 am

Witnesses

Wednesday 21 October 2009

Mr Robert Stheeman, Chief Executive, **Ms Jo Whelan**, Deputy Chief Executive and **Mr Jim Juffs**, Chief Operating Officer, Debt Management Office Page
Ev 1

Ms Jane Platt, Chief Executive, Director of Savings, and **Mr Steve Owen**, Channel Delivery and Management Director, National Savings and Investments Ev 6

Mr Andrew Stafford, Chief Executive, and **Mr Adam Lawrence**, Finance Director, Royal Mint Ev 10

Wednesday 28 October 2009

Ms Lesley Strathie, Permanent Secretary and Chief Executive, **Mr Simon Bowles**, Chief Finance Officer, and **Mr Richard Summersgill**, Director Benefits and Credits, HM Revenue and Customs Ev 17

Wednesday 11 November 2009

Sir Nicholas Macpherson, Permanent Secretary, and **Ms Louise Tulett**, Group Director of Finance and Procurement, HM Treasury Ev 31

Tuesday 8 December 2009

Rt Hon Stephen Timms MP, Financial Secretary, **Sarah McCarthy-Fry MP**, Exchequer Secretary, HM Treasury Ev 43

List of written evidence

1	HM Revenue and Customs Spring Supplementary Estimates Memorandum 2008-09	Ev 58
2	HM Treasury Revised Spring Supplementary Estimates Memorandum 2008-09	Ev 63
3	Government Actuary's Department Main Estimate memorandum 2009-10	Ev 67
4	HM Revenue and Customs Estimates Memorandum 2009–10	Ev 70
5	HM Treasury Estimates Memorandum 2009-10	Ev 78
6	HM Treasury Winter Supplementary Estimates Memorandum 2009-10	Ev 83
7	HM Revenue and Customs Winter supplementary Estimate Memorandum 2009-10	Ev 85
8	Letter from Penny Ciniewicz, Chief Executive, Valuation Office Agency to the Chairman of the Sub-Committee	Ev 91
9	HM Revenue and Customs	Ev 93
10	Office of Government commerce	Ev 97
11	Royal Mint	Ev 99
12	Crown Estate Commissioners	Ev 100

13	HM Treasury	Ev 104, Ev 109
14	Government Actuary's Department	Ev 113

Reports from the Treasury Committee during the current Parliament

Session 2009–10

First Report	Proposals for European financial supervision: further report	HC 37
Second Report	Work of the Committee 2008-09	HC 134
Third Report	Credit Searches	HC 197
Fourth Report	Pre-Budget Report 2009	HC 180
Fifth Report	Reporting contingent liabilities to Parliament	HC 181
Sixth Report	The failure of the Presbyterian Mutual Society	HC 260

Session 2008–09

First Report	Administration and expenditure of the Chancellor's departments, 2007–08	HC 35
Second Report	Pre-Budget Report 2008	HC 27
Third Report	Work of the Committee, 2007-08	HC 173
Fourth Report	Appointment of Paul Tucker as Deputy Governor of the Bank of England for Financial Stability	HC 34
Fifth Report	Banking Crisis: The impact of the failure of the Icelandic banks	HC 402
Sixth Report	Appointment of Paul Fisher to the Monetary Policy Committee of the Bank of England	HC 419
Seventh Report	Banking Crisis: dealing with the failure of the UK banks	HC 416
Eighth Report	Budget 2009	HC 438
Ninth Report	Banking Crisis: reforming corporate governance and pay in the City	HC 519
Tenth Report	Appointment of Professor David Miles to the Monetary Policy Committee of the Bank of England	HC 765

Eleventh Report	Appointment of Dr Adam Posen to the Monetary Policy Committee	HC 764
Twelfth Report	Banking Crisis: International Dimensions	HC 615
Thirteenth Report	Evaluating the efficiency programme	HC 520
Fourteenth Report	Banking Crisis: Regulation and supervision	HC 767
Fifteenth Report	Mortgage arrears and access to mortgage finance	HC 766
Sixteenth Report	The Committee's Opinion on proposals for European financial regulation	HC 1088

Session 2007–08

First Report	The 2007 Comprehensive Spending Review	HC 55
Second Report	The 2007 Pre-Budget Report	HC 54
Third Report	The Work of the Committee in 2007	HC 230
Fourth Report	Climate change and the Stern Review: the implications for Treasury policy	HC 231
Fifth Report	The run on the Rock	HC 56
Sixth Report	Financial Stability and Transparency	HC 371
Seventh Report	Administration and expenditure of the Chancellor's departments, 2006–07	HC 57
Eighth Report	Re-appointment of Dr Andrew Sentance to the Monetary Policy Committee	HC 454
Ninth Report	The 2008 Budget	HC 430
Tenth Report	Re-appointment of Mervyn King as the Governor of the Bank of England	HC 524
Eleventh Report	Counting the population	HC 183
Twelfth Report	Inherited Estates	HC 496

Thirteenth Report	Budget Measures and Low Income Households	HC 326
Fourteenth Report	Appointment of Lord Turner of Ecchinswell as Chairman of the Financial Services Authority	HC 916
Fifteenth Report	Appointment of Charlie Bean as Deputy Governor of the Bank of England	HC 917
Sixteenth Report	Appointment of Spencer Dale to the Monetary Policy Committee of the Bank of England	HC 1009
Seventeenth Report	Banking Reform	HC 1008

Session 2006–07

First Report	Financial inclusion: the roles of the Government and the FSA, and financial capability	HC 53
Second Report	The 2006 Pre-Budget Report	HC 115
Third Report	Work of the Committee in 2005–06	HC 191
Fourth Report	Are you covered? Travel insurance and its regulation	HC 50
Fifth Report	The 2007 Budget	HC 389
Sixth Report	The 2007 Comprehensive Spending Review: prospects and processes	HC 279
Seventh Report	The Monetary Policy of the Bank of England: re-appointment hearing for Ms Kate Barker and Mr Charlie Bean	HC 569
Eighth Report	Progress on the efficiency programme in the Chancellor's department	HC 483
Ninth Report	Appointment of the Chair of the Statistics Board	HC 934
Tenth Report	Private equity	HC 567
Eleventh Report	Unclaimed assets within the financial system	HC 533
Twelfth Report	The Monetary Policy Committee of the Bank of England: ten years on	HC 299
Thirteenth Report	Financial inclusion follow-up: saving for all and shorter term saving products	HC 504
Fourteenth Report	Globalisation: prospects and policy responses	HC 90

Session 2005–06

First Report	The Monetary Policy Committee of the Bank of England: appointment hearings	HC 525
Second Report	The 2005 Pre-Budget Report	HC 739
Third Report	The Monetary Policy Committee of the Bank of England: appointment hearing for Sir John Gieve	HC 861
Fourth Report	The 2006 Budget	HC 994
Fifth Report	The design of a National Pension Savings Scheme and the role of financial services regulation	HC 1074
Sixth Report	The administration of tax credits	HC 811
Seventh Report	European financial services regulation	HC 778
Eighth Report	Bank of England Monetary Policy Committee: appointment hearing for Professor David Blanchflower	HC 1121
Ninth Report	Globalisation: the role of the IMF	HC 875
Tenth Report	Independence for statistics	HC 1111
Eleventh Report	The Monetary Policy Committee of the Bank of England: appointment hearings for Professor Tim Besley and Dr Andrew Sentance	HC 1595
Twelfth Report	Financial inclusion: credit, savings, advice and insurance	HC 848
Thirteenth Report	"Banking the unbanked": banking services, the Post Office Card Account, and financial inclusion	HC 1717

Oral evidence

Taken before the Treasury Committee (Treasury Sub Committee) on Wednesday 21 October 2009

Members present

Mr Michael Fallon, in the Chair

Nick Ainger
Mr Graham Brady
Mr Colin Breed
Jim Cousins
Ms Sally Keeble
Mr Andrew Love

John McFall
John Thurso
Mr Mark Todd
Mr Andrew Tyrrie
Sir Peter Viggers

Witnesses: **Mr Robert Stheeman**, Chief Executive, **Ms Jo Whelan**, Deputy Chief Executive, and **Mr Jim Juffs**, Chief Operating Officer, Debt Management Office, gave evidence.

Q1 Chairman: Robert Stheeman, I welcome you back to the Sub-Committee. Could you introduce yourself formally and your team, please?

Mr Stheeman: Certainly. I am Robert Stheeman, Chief Executive of the Debt Management Office, to my left is Jo Whelan, the Deputy Chief Executive and the Joint Head of Policy and Markets, and to my right is Jim Juffs, the Chief Operating Officer.

Q2 Chairman: Thank you very much. How have your priorities changed over the last year?

Mr Stheeman: Fundamentally, they have not changed that much. The overall task that we have been set has become that much larger, but the actual nature of the priority remains very much the same. It has always been for us to focus as much as possible on delivering the remit as smoothly and successfully as possible and that has not changed despite that it is much larger in size.

Q3 Chairman: So it is simply the quantum of the task that has changed?

Mr Stheeman: Absolutely.

Q4 Chairman: Given how closely you are now working with the Treasury, does it make sense to retain the office as an autonomous agency?

Mr Stheeman: In my opinion, my personal opinion, of course—and I would say this, wouldn't I?—yes, it does because we are a very focused, professional, small outfit which has to interact directly on a daily basis with the market in particular. We need to also provide market intelligence where necessary to the Treasury. I think all those are things which if you are actually within one bigger, larger department you could potentially lose that focus. It also helps us, I think, attract key staff, motivate people because they know what they are there for. I think one of the key issues for us is simply being able to say, "This is our focus. We are not distracted by other things," and I think the separate agency status helps, even though we are under no illusions that we are somehow independent, we are a legal part of the Treasury.

Q5 Chairman: But you are also working for the Bank of England. You have provided nearly a billion pounds to purchase assets under that facility, have you not?

Mr Stheeman: We do not work for the Bank of England directly, if you like, we work for the Treasury in providing the financing for indeed the non-QE part of the asset purchase facility. That is absolutely right, but I think it is quite important to note that what we are doing is ultimately providing exactly the same function that we have always provided, which is to meet the cash needs of the Exchequer.

Q6 Chairman: For the first time that Standard & Poor's has downgraded its sphere of the UK economy to negative from stable. Do you have regular meetings with the credit rating agencies?

Mr Stheeman: In the DMO we do not have very many meetings. We have on occasion had meetings but the main part of those meetings is conducted usually within the Treasury with a focus on the fiscal side in particular, rather than just the debt management side. We have on occasion, as I say, had a visit, I can recall, earlier this year from one of the rating agencies ourselves and we are obviously happy to provide them with whatever information they want, but their focus is usually about the fiscal position rather than purely about debt management.

Q7 Chairman: But there would be an effect, would there not, on your work if the credit rating dropped further?

Mr Stheeman: Absolutely, and clearly we watch very carefully what the rating agencies opine. At the same time, that effect is likely to manifest itself, if at all, in the price. It is not necessarily going to manifest itself in, if you like, the longer term issues for us, in the way we access the market or the strategy that we are trying to pursue, or the advice that we would give the Treasury.

Q8 Chairman: So you do not have contingency plans to meet a sudden drop in the rating?

Mr Stheeman: Not directly because first of all that almost presupposes that something like that could or would, or will happen. We do not know. The rating agencies ultimately provide an opinion. It is their opinion. Does it have an effect on the market? It may do, and I would imagine that any downgrade, any formal downgrade—and we have only so far had the outlook changed—could move the market, but in my experience our sense is that actually rating agencies are what we would call lagging rather than leading indicators. By the time they have opined, the market itself has probably to a large extent already moved and discounted that information in the market.

Q9 Sir Peter Viggers: You explained the preference for longer dated gilts in your annual reports in 2007–08, pointing out the advantages in terms of cost, yet the number of short dated gilts that you have issued recently, the proportion, has increased considerably. Could you comment on that?

Mr Stheeman: Certainly. We very much remain very keen to issue as much long-dated paper as we possibly can, in particular because we regard it as generally cost-effective—we know the pension fund demand is out there—but as the financing requirement has risen as dramatically as it has it has forced us to go to that part of the curve which is the deepest and provides the most liquidity and enables us, if you like, to raise large amounts of cash in a relatively short period of time. To give you an example of that, a little over a year ago the average size of our short-dated auctions, anything up to seven years, was usually in the region of three, sometimes three and a half billion. This year they are five billion, so we have been able to increase the average size of those auctions significantly. The average size of long-dated auctions remained unchanged more or less at around two, two and a quarter, two and a half billion.

Q10 Sir Peter Viggers: Is the appetite for short-dated gilts linked with overseas development?

Mr Stheeman: Certainly overseas investors, if and when they are active in the market, it tends to be primarily in the shorter end of the market, occasionally also the medium sector up to ten years, but they are generally focused very much on shorter maturities, that is absolutely correct.

Q11 Sir Peter Viggers: How do you anticipate that you will replace the short dated gilts when they mature?

Mr Stheeman: That depends very much on how the financing requirement evolves over the next few years and the size and the nature of that requirement over the next few years. We still, I think, will certainly continue with our aim to try and focus as much as possible on spreading the issuance out across all maturities, but it could be that if the financing requirement were to decline I think it is reasonable to assume, as long as there is no major shift in the shape of the yield or something that

would suggest it will be an extremely expensive strategy, that we will try as much as possible to spread that issuance around and that could lead to a decline in short dated issuance again.

Q12 Sir Peter Viggers: Do you have any national security concerns arising from an increased reliance on overseas buyers?

Mr Stheeman: Not really. You are talking ultimately about investors in debt. It is not the same thing as investing in equity. Overseas investors do not have voting rights. I think that the portion of overseas investors that we have in our portfolio, which is about a third, is not unduly high. If you look at the fact that we have got about a third overseas, a third with the pension fund industry, I think that gives us a sort of what I would call balance and probably a diversification in our investor base which is actually quite positive.

Q13 Sir Peter Viggers: If there were uncovered auctions, what is plan B?

Mr Stheeman: Well, we would probably follow exactly the same procedure that we followed earlier this year when we did have an uncovered auction, which means that we make up the shortfall in our cash and management operations. The simple fact is that we will take directly on our own books, on the Debt Management Account, the full amount of the gilts that has been issued from the National Loans Fund and we will fund that ourselves. Then we have a procedure whereby there is a short period where we do not try and sell those gilts back into the market so that the market can, if it wants, adjust and then we sell that subsequently into the market. We would follow that procedure again because we believe the market places a lot of value and emphasis on the predictability of that system and not being surprised by any actions that we would then take perhaps to make up that shortfall.

Q14 Mr Breed: In your statement in the report and accounts you indicate that the DMO has received a remit in 2009–10 which will again require a record level of gilt sales of 220 billion. Is that a realistic amount of debt to sell in 2009–10?

Mr Stheeman: I think so. We are more than halfway through the year. We have done, I think, just a little bit over 135 billion so far, but to me the best indication of that is probably due not to what we have done just since 1 April but on an annual rolling basis actually since this time last year, which was the moment we had to step up issuance so much at the time of the bank recapitalisation actually we have issued, I think, over 200 billion already in the last twelve months.

Q15 Mr Breed: In that case, is the market not becoming saturated with UK gilts?

Mr Stheeman: I do not see a sign of that. That does not mean that we are complacent or that we in any way underestimate the scale of the challenge. I think we have been fortunate as well over the last six months in that probably market conditions have been more benign than we and some commentators

21 October 2009 Mr Robert Stheeman, Ms Jo Whelan and Mr Jim Juffs

would have actually expected. But we do not see signs of saturation. The auction programme has gone relatively well. Auctions have tended, since the uncovered auction, to be relatively well covered. The market has held up relatively well, but I would also stress against a very benign backdrop and, of course, we have to be fully aware and cognisant of the fact that the Bank itself has been buying gilts in the secondary market.

Q16 Ms Keeble: What effect is QE having on the current view of the sales? You referred to it briefly earlier.

Mr Stheeman: It's clearly having an effect. It is incredibly hard to try and quantify what that effect is. I think that what it has certainly done is helped create the benign conditions I was referring to. The best example of that is that we have to acknowledge that since the beginning of this financial year net gilt issuance—net in terms of what we have provided to the market in terms of supply—that has been, as I say, 135 billion, but at the same time the Bank has taken out 160 billion from the market, so effectively we have had a decline in available gilts in the market by approximately 30 billion. So that is actually almost a net decline in gilt supply, so there clearly has been an effect. My opinion is that the effect is shown in the yield levels that we currently see across all maturities because the Bank is now buying across all maturities. Exactly where yields would be were the Bank not to buy, I don't know.

Q17 Ms Keeble: Do you want to make a comment on the current yield levels?

Mr Stheeman: I would say two things there, and it is quite important for me to stress that we genuinely in all the debt management policy advice we give to the Treasury, the decisions we take, we do not, if you like, attempt to finesse the level of yields or try and take advantage of current levels. The only obvious comment I would make is that we are in some maturities across the board at intergenerational lows when it comes to yields, so the one positive factor which must exist is that we are currently raising money at relatively, in historical terms, cheap levels.

Q18 Ms Keeble: Which is a positive statement about confidence in the UK?

Mr Stheeman: It may be. I think it is ultimately very simply a question of supply and demand.

Q19 Ms Keeble: I just wanted to check up on one question to follow on from what Peter Viggers asked previously, which is that you have introduced the use of mini-tenders in syndicated programmes, increases of short dated gilts and the increase in overseas investors. Do you see any risk in that change in profile of what you are doing, or do you think it will all just proceed smoothly?

Mr Stheeman: The way I think I can best try and answer that question is to say that we fundamentally need an efficient, well-functioning and deep gilt market for us to be able to raise the money that we do. That is absolutely critical. So I think it is fair to say that everything that we try and do in terms of our

strategy is around facilitating the distribution mechanism for gilts. So you mentioned mini-tenders, and the various things, syndications, that we have introduced this year, are primarily designed to smooth the distribution process for our gilt programme. As long as we have this well-functioning market, I believe that we will be able to continue to deliver the remit successfully. But having that is incredibly important.

Q20 Mr Tyrie: What discussions do you have with the Bank of England before you make gilt disposals, before you go out and sell gilts?

Mr Stheeman: Virtually none. I mean, we clearly talk to the Bank of England on an operational level, but there is no discussion between us and the Bank in terms of what we would choose as a debt management strategy, in the same way as the Bank would not seek to garner our views in terms of, for instance, the way it carries out QE.

Q21 Mr Tyrie: But they are the biggest investor of the lot. You have just given the figures. You have regular meetings, do you not, with investor groups at the moment to decide what maturities to issue, to find out where the liquidity is in the market, and yet you are not talking to the biggest buyer of the lot?

Mr Stheeman: I think if we were to talk to the Bank about, if you like, the programme or even, dare I say it, as we do with other investors, ask the Bank the question, "What would you like us to issue?" If that was to happen—and I can assure you it certainly does not happen—I think the market would rapidly lose confidence in, if you like, the conduct of both debt management policy and possibly even monetary policy.

Q22 Mr Tyrie: And they are not even sitting in on these investor group meetings?

Mr Stheeman: We have occasionally invited them in the past. Recently they have not joined these meetings but in the past more as an observer so they are aware of what the investor conditions and views are, absolutely. As I say, we talk to them on an operational level, but in terms of trying to separate debt management policy and monetary policy, both we and the Bank are very keen to try and maintain that separation.

Q23 Mr Tyrie: You have described this extremely benign environment in which the Government is taking the lion's share of what you are trying to get out into the market. Not only is that going to stop, it is going to go into reverse, is it not? The Government is going to have to shift this stuff? So the pressure in the gilt market is going to become very severe indeed at some future date. Yields are going to rise, are they not, quite a lot?

Mr Stheeman: I fully accept that and I would be the first to acknowledge that I would accept that whenever the Bank decides both to stop QE and potentially even to reverse it, we will find ourselves in a very different environment. But it goes back to my point, and I completely agree with you, I think yields will rise. I do not know by how much, but they

will rise. But at the same time, in fairness, that is ultimately where the market and this efficient market mechanism that I was referring to kicks in. If the market does its job well and efficiently, then the price of the gilt that we are selling should be able to adjust itself relatively smoothly, but that is absolutely key. We are under no illusions about the challenge ahead!

Q24 John Thurso: I wanted to ask about the Public Works Loan Board. Who would be the best person to answer questions there?

Mr Stheeman: Any of us.

Q25 John Thurso: Well, let me ask the question. The amount lent by the Public Works Loan Board this last year is reported as being about 6 billion, down from 10 billion the previous year. How much of that is through early redemption interest rates causing a drop in lending?

Ms Whelan: We cannot really ascertain exactly an amount that is related to a particular cause, but it is worth noting that in that period interest rates changed quite a bit and that probably led to some local authorities revisiting their Treasury management strategies. We saw, for example, some repayments of the long dated borrowing. There were, repayments across the maturity sectors but mainly in the shorter dated and in the longer dated, and at the same time I understand there was a fall-off in the amount that local authorities had invested. So potentially there were some alterations on both the asset and liability sides of their balance sheets. When we process the loans we are not mandated to ask exactly why they are doing it.

Q26 John Thurso: The point behind this—I am sure you are aware of it—was the Communities and Local Government Committee Report, which cited the November 2007 change in the rates, which meant that actually it was too punitive for local authorities to repay, so they hung onto the loans and then invested the surplus cash. Therefore, when they all got stuck by being in banks in other countries, there was more at risk because they had not repaid loans which they might otherwise do and they called for some pretty urgent review of that. Is that for you to push through?

Ms Whelan: It is partly for us and we have actually got a consultation letter out currently which is being put forward by the Debt Management Office and the PWLB together acting rather on behalf of the Treasury. The whole thing is governed really by a piece of statute about the National Loans Fund, which says that the National Loans Fund must not lend at a loss and in the statute it sets out a certain methodology that can be used that will accord with that statute provision. That allows us, or requires us really, to compute the notional government borrowing rate at the time we make advances. So the methodology that has been in place for a while now is consistent with that. What we are currently consulting on is whether it would be acceptable to stakeholders to slightly change the operational process for that, which we would hope might allow the costs to be slightly lower in future, but we do

need to see what the results of the consultation are as to whether people will find it operationally straightforward to do it according to the way we have suggested it might be done.

Q27 Mr Brady: How worried are you that there might be uncovered auctions in the future?

Mr Stheeman: I would have to logically expect that at one point there will be an uncovered auction. I don't know when that will be. I think I probably said exactly the same thing a year ago, so I apologise, but it is in the nature of the market that from time to time you will have an uncovered auction. My concern, as I said, I think then, is always around the notion that potentially there is something structurally wrong in the remit which would suggest potentially that we are facing not just one uncovered auction but maybe several. Were that to happen, then I will be slightly more concerned, but having said all of that, I do tend occasionally just to point out the auction process, what it is, what it tells you about demand at a certain time, and it really only tells you about demand at the moment you hold the auction, at 10.30 on any given day. I always think it is worth recalling that, for instance, last year, for whatever reason, I think Germany experienced something like ten or so what has been referred to as "technically" uncovered auctions, yet no one suggested fundamentally that there was a problem there with selling Bunds or that there was anything other than a view that German Government Bonds represented the best possible asset in their market. So I am not that concerned, but I would be concerned if it was a sign that the distribution mechanism is not functioning efficiently. I always come back to that point, I know, but that is absolutely key from our perspective.

Q28 Mr Brady: When you had the uncovered auction last year you just do not feel that that was the case, that there was structural bargaining?

Mr Stheeman: I think one of the main reasons for the uncovered auction in March was the volatility that we were experiencing in the market at that time and volatility indeed is something which the market does not like because it impact especially on the risk appetite of our primary dealers, of the Germans, the gilt edge market-makers, and if their risk appetite is diminished, that indeed is something which we are not so happy about, but that is one of the reasons why we have introduced also these supplementary issuance licences this year.

Q29 Mr Brady: Are you planning future syndicated auctions, and if so can you say a word about what the cost of that is as opposed to the cost un-syndicated?

Mr Stheeman: So far we have had the planning assumption this year for this current financial year that we will be doing a total of 25 billion in syndicated auctions. We have completed three so far and the fourth is actually occurring today. We have syndicated a new 50 year conventional gilt seven billion in size, so we have done a very large part of the 25 billion programme in total. The costs have been to date, I think, just over £36 million, which

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have been paid in fees, including today's syndicated auction that is just over another 15 million, so it is just a bit above 50 million in total this year, so far.

Q30 Mr Brady: How does that compare with the cost of unsyndicated?

Mr Stheeman: The costs of mainly auctions? That is a very, very good question. We do not know. We have to guard against the notion that auctions are a cost-free way of issuing debt. They are not. We can easily end up paying sometimes quite large concessions through the auction programme. The big difference between auctions and syndications is that the cost that we are paying for syndications is explicit. We are actually paying them out in hard fees. I am sorely tempted to say that syndication from time to time is potentially a more cost-effective way of issuing large amounts in one go and thereby reducing the number of auctions that we have to hold and thereby reducing arguably the risk premium, whatever that is, that the primary dealers might be charging us in that process.

Q31 Mr Brady: When is it appropriate to hold a mini-tender and how many of them have there been this year?

Mr Stheeman: I think we aim to hold about one once a month. Effectively mini-tenders are nothing more than small auctions. They are mini-auctions. They tend to be in general roughly half the size of an auction. We introduced them for the first time a year ago when the remit was suddenly increased, primarily as a way also, as with syndication, of focusing on long-dated conventional and index-linked issuing because demand sometimes is not always as big as a full auction size that we are trying to get away. The demand can actually be slightly smaller but it does not mean that it is not there and it does not mean that we are not keen to tap into it. So very often a lot of the stresses in the market if a particular bond might be regarded by the market as in very short supply we are able to address that demand by the mini-tender process.

Q32 Mr Brady: Have top-up auctions been successful in 08–09 and 09–10?

Ms Whelan: I think so, very much so, and what we have tried to do there effectively is introduce a mechanism to incentivise bidders at auction by allowing them the option to take up to 10% of their allocation at the clearing price on the same day but a few hours later, at two o'clock. As you would expect, the success can generally be measured, in terms of whether they take it up, as to whether the price is either above or below where it was at the time of the auction. If it is below, obviously the take-up will be very low, but we also think that the primary measure of success is actually just to incentivise bidding. We need to have, if you like, eager bidders at the auction and the top-up facility is one way of trying to achieve that.

Q33 Mr Love: I want to come back to the question you were asked by Mr Tyrie in relation to quantitative easing. While I take on board the point

you made for you to act in concert in some way alongside the Bank of England would be seen very negatively by the marketplace, but it is important that you have a well-functioning market and therefore I wonder if any consideration has been given by the Debt Management Office to whether there needs to be some arrangements made for when the quantitative process reverses?

Mr Stheeman: That is an entirely legitimate process and you are probably very much aware that the Governor of the Bank has said on numerous occasions that when it comes to any disposal of their gilt holdings that they will be actually coordinating and talking to us in that process, and you would expect that on an operational level we will certainly be doing that. I completely agree with the premise of your question. Neither we, nor the Bank, nor the Treasury, or anyone in the authorities has any interest at all in seeing, if you like, a disorderly market or anything which is going to upset the market and the Bank has made that very clear. So we will be talking to them in detail about that.

Q34 Mr Love: I was just going to say that. You indicated earlier on that you have not had any discussions at all with the Bank, as I understood the response you gave. Surely now is the time to be at least exploring what will happen when this process reverses itself?

Mr Stheeman: As I say, on an operational level we will certainly be doing that, but what I am talking about now, if you like, is the operational side and I think the Bank would not be very keen to send a signal, or for us to send a signal that we are, if you like, contemplating a change in direction as far as the Bank is concerned in terms of what they are doing. But when the time comes, I am sure that we will be talking to them in quite a bit of detail. If I could just make one point there. As an example of the cooperation which we have with the Bank, what I describe as operational cooperation, you may be aware that the Bank lends out part of its gilt portfolio that they have purchased through us into the market in order to help facilitate the repo market, and that has been something which the market has welcomed very much indeed. So I think it just underlines how conscious the Bank is of avoiding disruption to the market.

Q35 Chairman: When you came last year we expressed some concern about the capacity of your office to handle this increased workload. I see from your Annual Report that your staff numbers have not in fact gone up. Have you got enough people?

Mr Stheeman: I think we do for the moment. We are a lean organisation and I am quite happy actually that we stay that way. Just so that you know, the Annual Report obviously goes until the end of March. At that time we had the resources and obviously I think we had approximately 90 staff members. That is probably now close to about 110, 115, to be precise about 113, so it actually has gone up and, as you will expect, always when you start adding resources there is always a lag in terms of

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actually getting the right people in place in time. But we have had discussions with the Treasury about the resources. We have received the resources that we have requested and we requested more resources, also financial resources, and we have received those.

Chairman: Good. All right. As you know, we are on a tight timetable today so we are going to leave it there. If we have further questions we will follow them up in writing, but I would like to thank you and your colleagues for appearing today.

Witnesses: **Ms Jane Platt**, Chief Executive, Director of Savings, and **Mr Steve Owen**, Channel Delivery and Management Director, National Savings and Investments, gave evidence.

Q36 Chairman: Jane Platt, can I welcome you back to the Sub-Committee. Could you formally introduce yourself and your colleague, please?

Ms Platt: Certainly. My name is Jane Platt. I am Chief Executive of National Savings and Investments and the Director of Savings, and this is my colleague, Steve Owen, who is Director of Channel Delivery and Management.

Q37 Chairman: We have about thirty minutes for this session, because we want to squeeze in the Royal Mint, before our vote. Your vision is to provide guaranteed savings for customers, but your mission is to raise cost-effective finance for the Government. Has that conflict got worse over the last year?

Ms Platt: Over the last year we have certainly lived through some exceptional times as we have dealt with the flight to safety post the Lehmans crisis in the autumn and over that period it has been very important to us to balance the interests of: our customers, of the Government in the form of net financing, and financial stability. So in fact over that period our key remit of raising cost-effective net financing has been reinforced, but so has the importance of us behaving straightforwardly and honestly with our customer base.

Q38 Chairman: But what criteria do you use to determine a fair rate of interest for your customers?

Ms Platt: In terms of determining our pricing, we look at a number of things. We look at our position in the competitor tables, we look at base rates and we look at the amount of net financing that we need to generate. So we calibrate these things, bearing in mind, of course, the need to make sure that we behave appropriately at a time when the banks and building societies are rebuilding their balance sheets to make sure that we have a suitable blend of rates across the various products that we market.

Q39 Chairman: You mentioned the flight to safety, but you ceased discretionary marketing during the autumn and winter. Why was that? Why did you not want to encourage additional funding?

Ms Platt: In August of last year we were on track to be raising 4 billion of net financing for the Treasury, which was the agreed amount we had set off to raise. After the Lehmans crisis it was very, very clear that we were going to be receiving a large volume of unsolicited funds coming into NS&I, and at that point we had to make a decision. Do we stay open for business and allow net financing to rise very well above the amount we had previously agreed, or should we actually stop not only marketing our

products but also allowing people to invest in them? We took the decision with the Treasury that we should cease all discretionary marketing but stay open for business and I think that NS&I and its operating partner, Siemens, did a marvellous job in the face of huge unsolicited volumes in staying open for business. Our contingency plans worked, staff cancelled their holidays, they did extra shifts, they really "busted a gut" to be able to make sure that we offered a good service to customers. Because you could imagine what would have happened if NS&I had not been open for business at a time when people were so concerned about their savings. I was up in our call centres just very shortly after the flight to safety and listening to people of all ages, some of them in tears, talk about how concerned they were about the safety of their savings. And of course NS&I's call centres are staffed by people who generally have some 22 years of experience and they were able to calm people down at a time when emotions were running very high. So I think that NS&I has really proved itself as the cornerstone, a robust cornerstone, of the savings market in an extraordinary time.

Q40 Chairman: It seems odd in the middle of the period to actually discourage people from saving with you, given you are a savings body?

Ms Platt: We certainly were not discouraging them in any way. We stayed open for them.

Q41 Chairman: But you stopped the marketing?

Ms Platt: We stopped the marketing, but—

Q42 Chairman: How is that not discouraging?

Ms Platt: It is very different to cease marketing than to be actively discouraging people moving towards us. At that point, of course, it was not clear how long the flight to safety would go on for, whether the measures that were being taken by the Government would be successful. We had no idea how long that flight to safety would last, so we just wanted to make sure we stayed open for business, that people could always get through, that our systems were robust and that through all that NS&I and Siemens coped extremely well.

Q43 Chairman: Could you explain your net finance target for the current year? It is essentially to maintain the status quo. Why is that?

Ms Platt: After such an extraordinary year last year when our net financing figure was 12.5 billion, we worked with the Treasury to look at our target for this year, which is indeed zero net financing within a

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tolerance of – 2 billion to + 2 billion, and indeed we expected some money to flow out after the flight to safety was over because as more normal circumstances begin to reassert, you would expect some of the money that came in to gently flow out. So we were expecting that to happen, which is why our net finance target is as it is for this year.

Q44 Mr Todd: Can I turn to an issue we have raised previously, which is unclaimed funds? In your accounts for 31 March you have represented that section and it is far from clear whether unclaimed funds have actually gone up or down during the period in question because it is not possible to make a comparison. Have they gone up or down?

Mr Owen: The total level of unclaimed funds using the Government definition and the industry definition is about 452 million, which relates to our account products. If you wish to compare with where we were when we last sat in front of this Sub-Committee, they have gone down a little. The total on a like for like basis would be just over a billion now. We have had a great deal of success in terms of reuniting customers with lost assets both through our free tracing service, which we have run since 2001, but more significantly through our joint approach with the BBA and the BSA in relation to the mylostaccount website, which has reunited some £212 million worth of funds with customers.

Q45 Mr Todd: So if we turn to p.99 of your accounts, how do I reconcile the figures you present there with what you have just said?

Mr Owen: The figures as I have just given them are based on the definition of 15 years without a proactive contact from the customer, which is the definition used by the industry and by Government and which is a different basis for some of these figures.

Q46 Mr Todd: Okay, we will skate over why you use one indicator when you are answering questions and when you are in your accounts you use another, but on this basis it would appear that those figures you have left in your accounts have actually gone up in the period in question and you have taken a number of other elements and placed them into some pool account of some kind somewhere else so that we cannot compare them at all?

Mr Owen: The figures have gone up in terms of p.99. We have grown, of course, quite significantly so you might expect them to go up in accordance with our overall scale and size.

Q47 Mr Todd: But you have grown in terms of new customers. It would be a sad thing if they could come up and claim in such a unique year in which, as your Chief Executive has said, people have been flying to safety. It hardly indicates that they are likely to lose their accounts within 12 months?

Mr Owen: It is quite normal for the customers to leave their funds with us on a long-term basis. Our savings certificate, for example is a five year product and after those five years if the customer takes no

action it rolls over into another five years product, so we need to be quite careful in terms of the definition of unclaimed funds in relation to NS&I products.

Q48 Mr Todd: If the Government were to change its position—and, as you know, we urged it so to do last time in terms of including these in the unclaimed assets scheme. If they were to do that, would that have any operational impact on how you managed your unclaimed funds? You are already obviously attempting to link these funds to their legal owners. If it were moved to the unclaimed assets scheme, what difference would that make?

Mr Owen: We are a little different to the rest of the banking industry in that the money that flows into NS&I we do not hold it, we do not keep it, it flows into the Government coffers and presumably the Government therefore spends it, so it is already being used for the public good effectively through expenditure.

Q49 Mr Todd: I was more interested not in the philosophical argument, which I understand although I do not accept, but in the operational implications of that change.

Mr Owen: In what sense?

Q50 Mr Todd: In other words, if you moved this to the unclaimed assets scheme, would this change the way in which you manage the unclaimed funds that you have been collecting and enumerating, although, as you have just said, you pass them direct to the Treasury anyway?

Mr Owen: As you so rightly say, we do not manage them as such. We already make every effort to reunite the customers with their funds, both through mylostaccount, through using third party databases such as Experian and through some software we use to proactively find customers.

Q51 Mr Todd: So it would not make any difference to what you do?

Mr Owen: Not operationally, no.

Q52 Mr Breed: Could you tell us something about the new banking system that has not quite yet come into being, in particular what sorts of improvements it might bring to your services that you are providing?

Ms Platt: Absolutely. When I was here a little over two years ago I was talking about the modernisation of National Savings & Investments and we are running through a programme of modernising the infrastructure, data centres, our banking engine, and we are transferring our products one by one from the old banking system to the new banking system, and we are doing it on a product by product basis. What customers will see is the ability to manage their products online. Because at the moment already we have an ISA product which customers can not only buy and sell online but they can change their customer details and all those sorts of things. So it is a proper internet service in its fullest sense and what you will see as we move across onto the new banking service is still very high levels of accuracy and all

those good things, but also the ability for customers to manage their holdings online to transfer to new products. So we offer a much slicker and better service for customers. For the Government what you will see is a reduction in our overall cost base, which means that over time we will be able to offer cost-effective services to areas and groups of customers that at the moment are not cost-effective for us to offer products for. So it will have the benefit of reducing our cost base but also mean that it is cost-effective, because our costs are lower, to provide our products for areas of the market that we are currently not servicing.

Q53 Mr Breed: So it will not be a banking system that can be provided to those who want just a basic bank account and find it difficult to obtain one from normal High Street banks as such, is it?

Ms Platt: No, it is a banking engine in terms of allowing us to manage and administer those funds. It is not a retail banking system because we do not offer current accounts and that is not something we have built into our specification.

Q54 Mr Breed: So if there is a sort of launch what you are basically doing is gradually building up a new method of dealing with products for customers as such? Perhaps we were wrong to expect a big launch of something brand new if it was not going to happen. There is not going to be a launch, is there? Essentially you will just over 2009–10 gradually take products onto this system, so there will not be a magnificent launch as such, will there?

Ms Platt: There will be no Big Bang and anyone who works in banking would absolutely avoid such a thing, moving everything all at once, because the risk to 27 million customers of moving from one thing onto a new thing all at once would be a huge, huge risk. So we have taken the prudent approach of moving the products across product by product and for each product there will be a re-launch, there will be an improved service that customers will see and a benefit to Government. So although there is no Big Bang there are tangible benefits.

Q55 Mr Breed: Do you see that when you have actually completed the task of moving everything over you will have to have some sort of marketing campaign to actually stimulate more and more customers and more product sales and that sort of thing, or is it something which is going to be relatively low-key?

Ms Platt: I think that will depend on the discussions we have with the Treasury on our net financing remit because if they set up a net financing remit that is positive and generating a number of billions for the Government, then we would be able to combine our new product launch with marketing to attract funds in. So our marketing is aligned to the requirement for net financing rather than to the requirement of the system.

Q56 Sir Peter Viggers: You signed a public/private partnership contract with Siemens in 1999 for ten years which was subsequently extended to 15 years

and they found themselves under heavy demand during the flight to safety. The amount you have paid to Siemens has increased by about £20,000 over the last couple of years. To what extent do your increased payments to Siemens reflect additional costs to Siemens and to what extent do you think there is additional profit there?

Mr Owen: The flight to safety in terms of the payment to Siemens was round about £12 million in total. Now, that figure covers not just taking in the sales but managing those sales through the life of the contract, through to 2014. Our profit margin within those negotiations with Siemens, which was done some years ago, was 12.5%.

Q57 Sir Peter Viggers: Are you satisfied that changed circumstances mean that the amounts you are paying to them adequately reflects that they are not making excessive profits?

Mr Owen: Yes, I am satisfied. It is very difficult to calculate the precise costs because some of this sits in the future and customer behaviour will drive the actual cost of managing those customers over their total life. If they are very active customers who contact us a great deal, of course it costs more than a customer who puts their money with us and then leaves it there until repayments. But I am satisfied we did a great deal of work to ensure the amount we paid to Siemens was the correct sum.

Q58 Sir Peter Viggers: As circumstances have changed, do you continue to monitor and do you continue to be satisfied that the amount you pay them is satisfactory?

Mr Owen: We do continue to monitor on an ongoing basis. The other element that gives me confidence that the amount we paid is not excessive is that we can compare it with the average costs at the original tendering back in 1999 to see if we were paying more or less per transaction or per customer than we were when we went to the market for a competitive tender. And we are actually paying significantly less than we were back in 1999 per customer or per transaction.

Q59 Sir Peter Viggers: They are responsible for direct channel sales, of course. You had a short advertising campaign in 2009 to encourage greater use of direct channels. How much do you hope to save through promoting greater use of direct channels.

Mr Owen: Our direct channels do save us a great deal of money, primarily because when we bring a customer in direct we only pay one third party and that is Siemens. If we bring money in through the Post Office we pay two third parties, so it is significantly cheaper to bring money in directly as opposed to a High Street partner.

Q60 Sir Peter Viggers: Siemens is responsible for direct sales. Are you saying that the direct sales come direct to you and may not come through Siemens?

Mr Owen: Siemens do all of our processing for us, whether it is direct or indirect. They process everything, so we pay Siemens a different amount if the money comes in through the Internet or the

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telephone compared with if it comes through the post and we pay them less for the direct sales than we do if it comes in through more traditional means because their processing costs are lower.

Q61 Sir Peter Viggers: If you increase direct sales and reduce traditional sales, that must have an impact on those responsible for the traditional sales, namely the Post Office. What would the impact be then?

Mr Owen: It does reduce our payment to the Post Office, yes.

Q62 Sir Peter Viggers: How do you see the distribution of products developing in the coming years?

Ms Platt: I think our strategy is quite clear, that we want to have a robust set of Internet, telephone and postal channels and our relationship with the Post Office remains healthy. Last year the percentage of business that we did through the Post Office was about 60%. I would expect it to be about 50% this year, which is something the Post Office are well aware of and we work very closely with them.

Q63 Ms Keeble: I want to ask about your relationship with the Post Office. You said that you expect the market share that goes through the Post Office to decrease. Is that because you are going to grow the others or is it partly because of the reduction in the Post Office network?

Ms Platt: It is to do with the balance between the various different channels. So overall, for example this year we are not expecting any growth because we are trying to manage our net financing around zero within the band of -2, + 2 billion and the percentage the Post Office will be doing will be about half of the sales which will come in through that channel.

Q64 Ms Keeble: Are you going to be affected by the reduction in the Post Office network and the other various channels, the sales channels? Which ones are you looking to increase and how?

Ms Platt: In terms of the Post Office and its number of branches, in fact the vast majority of sales coming to us come through the Crown branches, so we would not expect to be adversely affected in terms of our sales by any plans that we have seen from the Post Office to date.

Q65 Ms Keeble: Do you not think that you are over-reliant on the Post Office? Looking at the figures, the Post Office counter sales were very sort of static through 2003–04 to 2007–08. Last year it shot up and it practically doubled. I see that your Internet sales have grown but not exponentially. What are you going to do to really expand on your other sales channels?

Ms Platt: Last year was a very unusual year because of the flight to safety and there was definitely a discernible trend that because people were very concerned about security overall, it was important for them to have the physical transaction and a piece of paper that was stamped in the Post Office when they actually invested their savings. So I think there

were very particular reasons why the Post Office counter sales were so disproportionately high potentially last year.

Q66 Ms Keeble: So you are trying to say that people would rush round to Northern Rock and took the money right there and then they rushed round to the Post Office and paid it in? I think you would have to be quite clear if the flight to safety people were choosing to go to the Post Office.

Ms Platt: Not all of the flight to safety people were choosing to go to the Post Office because in fact all of our channels increased their sales last year, but there was a disproportionate increase in the Post Office. It was not just people rushing round from Northern Rock and putting their money straight into the Post Office, it was people looking to invest over the counter and wanting some proof of that.

Q67 Ms Keeble: What are you doing about looking at the products? Could you have an agreement with the Post Office about who provides what type of product, if there are some sorts of areas which they will not go into? Finally, your baby bond product, is that the Child Trust Fund or not?

Ms Platt: I do not think so.

Q68 Ms Keeble: Okay, so the first one is just about the agreement with the Post Office about who sells what?

Ms Platt: We do not have a precise agreement with the Post Office over who sells what, but we have a very good relationship with them and over time we share our plans, they share their plans, and as you will have seen in the last few days we have mutually agreed that our Guaranteed Growth and Income Bonds will no longer be sold in the Post Office but just through our direct channels. That is the result of our strategy to increase the amount we are doing over the Internet and over the telephone. Also they are content with that because they have products which compete in the same space, so it works well for both parties. So we work very closely together in looking at that.

Q69 Ms Keeble: And the baby bond product, is that a Child Trust Fund or not?

Ms Platt: We have Children's Bonus Bonds. We do not have a child's trust fund, but we have a Children's Bonus Bond.

Q70 Ms Keeble: We went into this some time ago when I asked about whether you did a Child Trust Fund and you did not do one. Have you looked at that at all, because given your profile and the assurances people have about those sales, why don't you offer a Child Trust Fund? Why can't you develop one?

Ms Platt: The situation has not really changed since we last spoke about this matter in that we do have a review of our products line from time to time. We had one about 18 months ago and the Child Trust Fund remains a product that we cannot offer on a viable basis in light of our remit.

Q71 Ms Keeble: Why not?

Ms Platt: Because of the expense of creating and running that sort of product. It would not be cost-effective financially for the Government. But we do have an extremely good product in Children's Bonus Bonds and some 5% of our total customers are children who invest either in Children's Bonus Bonds or in Premium Bonds or Capital Bonds.

Q72 Ms Keeble: Can I just ask again on this, because if you say that you are trusted for children's products then why not the Child Trust Fund and why not look at how it can be provided as one of a range of products to make sure that you really can deliver a comprehensive suite of services for children, if you are trusted for that sector?

Ms Platt: We believe we do have a comprehensive range of products for children with the Children's Bonus Bonds, Premium Bonds and the other things that we offer. We have looked at the economics of offering a Child Trust Fund, but unfortunately they do not meet the hurdles of being able to offer such a thing cost-effectively in the context of our overall range.

Q73 Chairman: Just a couple of final questions. Your key efficiency measure, soon to be called "value add", the extent to which it is cheaper to raise money through you than through the rest of the markets was simply suspended last year and has not been reinstated. Why was that? How can you tell how well you are doing if the efficiency targets you have got no longer exist?

Ms Platt: It has been temporarily suspended, so we are all working on the basis that as soon as the comparators which make up that target and benchmark have some meaning, then we will reintroduce it. When I say when the comparators have meaning again, let me just explain. We temporarily suspended value add at the time when interest rates, the base rate, went down to half a per cent. The base rate has never been that low since the Bank of England was founded and certainly not since Premium Bonds and our other products were introduced. So we looked very carefully at the value add measure and realised that if we did not suspend it, it would drive us to make some very difficult and unfair decisions in terms of pricing for our customers. For example, with base rate at half a per cent, that would assume on our value add measure that the Gilt Office (DMO) would be able to raise financing for 11 or 12 years at less than 0.3%. That

is just not true, so therefore we had to suspend the measure because it was distorted and did not give a true measure. However, we have got an efficiency measure—

Q74 Chairman: No, let us just stick with value add. When you say it can be reintroduced, can it now be reintroduced mid-year or would you get away with no measure for the whole of this year?

Ms Platt: We have a measure for this year, which is our efficiency ratio, which looks at the cost of administering the fund against the amount.

Q75 Chairman: Yes, but I am asking you about value add. Could the value add measure be reintroduced in-year?

Ms Platt: Technically it could, but only when the comparators have some meaning. We have got, though, a value proxy measure, which does measure whether we are able to add value against the gilt market. What that has done, and we have worked with the Treasury on this, is to put in place an indicator which does indeed show that during the time that value add has been suspended so far we are raising money more cost-effectively than the Gilt Office (DMO) and I am more than happy to go into the detail of that calculation and the figures if you would like.

Q76 Chairman: I am afraid we do not have time to do that. You have got your own youandyourmoney website alongside the Financial Services Authority's own website on moneymadeclear. Why do you need your own?

Ms Platt: Along with other financial services institutions, we absolutely support the Government's financial capability initiatives. We believe with the NS&I brand we are in a really good position to get people with our 27 million customers, many of whom come to our website on a very regular basis actually looking at this information. And you may be interested that in WH Smith's very shortly we will be putting out some financial services guides. Again, this is very unusual because most people would expect us to have everything focused absolutely on product, but of the eight guides we are putting out six of them are on financial capability and helping to educate the public where we believe NS&I has an important role to play.

Chairman: I am afraid we are out of time. We are going to have to leave it there. If there are further questions we will follow up in writing. Thank you both for attending today.

Witnesses: **Mr Andrew Stafford**, Chief Executive, and **Mr Adam Lawrence**, Finance Director, Royal Mint, gave evidence.

Q77 Chairman: Can I welcome you both. Could you introduce yourselves formally, please?

Mr Stafford: Good afternoon. I am Andrew Stafford, the Chief Executive of the Royal Mint. I have at this moment to make an apology. Mike Davies is the Chairman, but unfortunately he has been unable to make the Committee hearing because

the train service from Coventry was cancelled due to a fatality on the line. We have advised that Adam Lawrence, the Finance Director, was the other witness who was attending, and Adam has made it, but Mike Davies will not be attending and he will be writing to you to send his personal apologies, but it was unavoidable.

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Q78 Chairman: Okay. Your profits are down and your rate of return is down. Why is that?

Mr Stafford: The answer is that our turnover grew year on year—

Q79 Chairman: No, the profit I asked you about.

Mr Stafford: Forgive me, I am just about to say that the mix of our business did change quite substantially year on year, particularly in the commemorative coin business where a lot of the turnover in the last twelve months was from bullion coin as people sought to buy more gold coins at a much lower margin than our collector coins. So our growth in turnover was not comparable with the growth in margins from our commemorative coin business. Therefore, we have seen a reduction in our profitability of the percentage of sales but our return on average capital employed, which is our key measure, clearly performed very well.

Q80 Chairman: But your average rate of return on capital employed has gone down, is that not right?

Mr Stafford: It has gone down, but it is still a very healthy return for a manufacturing organisation. As I said, the principal component of that is the change in mix of the business year on year, predominantly driven by a growth in demand for bullion coin products.

Q81 Chairman: But what is the strategy now if your turnover keeps going up and you make less and less profit? Am I right?

Mr Stafford: Our strategy is very clearly to achieve a better return on average capital employed and if you look at our trend over the last three years then clearly we have made tremendous strides in that area. In-year there was a reduction because of that very reason, but if I look at our current strategy for this year we are increasing our circulating coin business overseas and as a result we are now seeing a dramatic improvement again. You cannot turn off demand for bullion coin products from the consumer when clearly in the economic situation in the UK this year there has been a very strong interest in buying bullion coins.

Q82 Chairman: I am sure my colleagues will follow up on that. The schedule is to turn you into a Government-owned company by December. Are you on track for that?

Mr Stafford: Yes, we are on track. Everything is being done to complete the process by 31 December.

Q83 Chairman: Is this not a risk, launching a new Government-owned company just as it has become profitable again?

Mr Stafford: We believe that we have in place a strategy. We have demonstrated now for the third consecutive year that this business is a successful business making a good return for its shareholder. We have a long-term strategy in place involving both growth in our UK commemorative coin business and in our international circulating coin business.

We have secured long-term contracts in major overseas markets such as Russia. We have secured a major capital investment programme for the business to increase our manufacturing capability, so we believe that the strategy and the capability are in place for long-term sustainable, profitable growth.

Q84 Chairman: If you have got a long-term strategy, does it include full privatisation? Do you expect to be a trading company for ever?

Mr Stafford: That is not a matter for management. The decision of whether or not the Royal Mint is privatised is a matter for the politicians, not for management.

Q85 Chairman: You do not have a view on it?

Mr Stafford: My view is irrelevant. My task is to make sure that I make the maximum return for the shareholder, regardless of who that shareholder is. The shareholder at the moment is the Government and the Government has tasked me with making the maximum return for the shareholder.

Q86 Chairman: I understand that, but I asked you whether you had a view?

Mr Stafford: And I can tell you that I might have a view but my view is irrelevant. That is a matter for the politicians.

Q87 Chairman: So you had a view but—

Mr Stafford: Whether or not I have a view—and I must be absolutely clear on this because my view is irrelevant. It is a matter for me as management to make the return for the shareholder. It is for the shareholder to determine whether or not they wish to privatise the business.

Q88 Nick Ainger: Mr Stafford, Gerry Grimstone's review for the Operational Efficiency Programme made the recommendation that you move to the private sector?

Mr Stafford: Yes.

Q89 Nick Ainger: Did he visit Llantrisant?

Mr Stafford: No, he has not visited Llantrisant.

Q90 Nick Ainger: Did he talk to you?

Mr Stafford: No, he did not.

Q91 Nick Ainger: Do you not find that amazing that someone is suggesting a complete change of the operation of the company and never actually visits its only plant and its management?

Mr Stafford: That is not—again, my task—

Q92 Nick Ainger: Let me turn it around. If you were going to carry out a review of an organisation, would you normally visit that company and also talk to its management?

Mr Stafford: Mr Grimstone is reviewing a number of organisations. It is not for me to comment on which of those organisations it is appropriate—

Q93 Nick Ainger: But were you surprised that your organisation, the Royal Mint, is being reviewed and he did not visit and he did not speak to you?

Mr Stafford: My task is to perform the duties that I am given to perform and I am not going to be drawn on that point because the review has been instructed by the Chancellor and we are performing what we have been asked to undertake in that review and we are complying fully with all the advisers that have been appointed to conduct that review process.

Q94 Nick Ainger: Okay, let us move forward and look at the actual report, your annual report. You say in “Our Future” where you refer to the vesting that, “There is now a strong case for the introduction of private risk capital into the business. This will allow us to pursue new commercial opportunities, expand more rapidly, taking advantage of freedom, flexibility,” et cetera. What commercial areas could you move into that you cannot move into now?

Mr Stafford: Well, there are two very specific things. One is the acquisition of other organisations which would allow us to expand internationally, and secondly undertaking joint ventures with overseas partners to enable us to penetrate markets, for example Asia, where we have a presence but we would need to have a greater level of presence for a manufacturing capability. Both of those things, whether it is an acquisition or a joint venture, would clearly require a capital injection into the business. If the Treasury did not feel that that was a good use of public money to make those investments, then clearly private capital is an alternative way of pursuing both joint ventures and acquisitions.

Q95 Nick Ainger: So let us get it right, you are talking about overseas adventures, not actually investment in the Llantrisant plant?

Mr Stafford: Not necessarily. We have just, for example, already announced a major capital investment programme in the Llantrisant plant, £20 million will be spent over the next twelve months, doubling our capacity for nickel plating. So there is a huge investment within—

Q96 Nick Ainger: But that is under the existing programme. What you have just told us is that the way to expand into new commercial opportunities is actually to have work going abroad?

Mr Stafford: Not necessarily so. For example, one or two of the acquisitions that could be undertaken in the business would be for UK operations, which could be combined with the Llantrisant operation. So there are specific opportunities in the UK as well as overseas.

Nick Ainger: Thank you.

Q97 John Thurso: Following on from that, to what extent is your future success dependent on guaranteed business from the Treasury?

Mr Stafford: The UK Treasury now accounts for less than a quarter of the Royal Mint’s turnover and profitability. We have had a strategy to clearly reduce our dependence because there is no potential for growth by just remaining as the incumbent suppliers

to Her Majesty’s Treasury for UK circulating coin. So in answer to your question, less than a quarter of our turnover and profit is now dependent upon the UK Government.

Q98 John Thurso: A quarter of the turnover?

Mr Stafford: And profit.

Q99 John Thurso: And profit. One of the comments which have been made to us by a private mint is that you have an unfair competitive advantage because of what you get from the Treasury and that if you were to enter into the private sector with that competitive advantage it would be a disadvantage to them and would not be truly competitive. What is your answer to that?

Mr Stafford: Well, the answer is that we have to compete on an international basis with other mints and we win some tenders and we lose some tenders on a cost basis and there will be no difference to whether or not we are owned by Government or owned by the private sector in that regard. With regard to private mints, private mints predominantly make commemorative coins and there is very healthy competition in the market for commemorative coins. We have a very good business in the UK, but there are other UK privately owned mints that also supply commemorative coins.

Q100 John Thurso: You had, I think, a bit of a spat with the Birmingham Mint, which has now been settled, I understand, for a relatively modest amount of money. In the annual report it says there is no basis for a claim. Why did you choose to settle out of court at all?

Mr Stafford: The case goes back a long time, it goes back to 2002 when the matter was—when you say we’ve had a spat, the current management have certainly not had a spat. The Birmingham Mint—

Q101 John Thurso: They inherited one then?

Mr Stafford: They inherited a spat. We sought to resolve this to avoid any further cost to the public purse. We were advised that to take this matter to trial would have incurred at least another three-quarters of a million pounds in legal fees, and even if we had won but not been awarded costs then we could have been incurring significant costs. So to settle the whole matter for £100,000 was a very sensible way of settling the matter and avoiding any further risk to the public purse.

Q102 John Thurso: It was a purely commercial decision?

Mr Stafford: Yes.

John Thurso: One last question, if I may.

Chairman: As briefly as you can, because we are up against the clock.

John Thurso: In that case, that is fine, I am done.

Chairman: We are up against the clock today because we have to finish at half past.

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Q103 Jim Cousins: Mr Stafford, I listened very carefully to the answers you gave to the earlier questions, but as I understood it you already have some relationships with private sector banks?

Mr Stafford: Well, we have some of our banking facilities provided by private sector banks. They are not in any way equity stakes, but we obviously have some of our banking facilities with private sector banks, correct.

Q104 Jim Cousins: And your Russian contract?

Mr Stafford: That is an arm's length commercial arrangement with a private sector organisation in Russia which is the supplier to the Russian Mints. So we contract with an organisation called Tenzor, which in itself then contracts for the supply of coins to the Russian Mint.

Q105 Jim Cousins: So what you are is a trading fund? You are able to enter into these commercial arrangements and in the case of the Russian one, I guess, Russia being Russia—

Mr Stafford: Forgive me, this is us supplying them with a product. This is nothing to do with the way we finance our balance sheet, this is purely—

Q106 Jim Cousins: But it is a long-term arrangement with them?

Mr Stafford: Yes. We have never said we cannot—

Q107 Jim Cousins: How do you carry the risk of that arrangement?

Mr Stafford: Forgive me, we receive a payment up front for the goods before we supply it. We have a very large percentage of the goods paid for before we deliver.

Q108 Jim Cousins: You transferred an unusually large amount of money from your reserves into your profit and loss account last year?

Mr Stafford: I will ask my Finance Director maybe to answer the technical points if I may.

Q109 Jim Cousins: You transferred £8 million into your profit and loss account?

Mr Lawrence: Sorry, that is our profit for the year, so if you look from year to year at our reserves that is the movement in profit.

Q110 Jim Cousins: And that made the total in your profit and loss account—

Mr Lawrence: No, no, that's an impact on profit as well, a shift in reserves

Q111 Jim Cousins: No, no, the total now in your profit and loss account is about £50 million?

Mr Lawrence: That is our retained profits.

Q112 Jim Cousins: Yes, so how much of that might you consider investing in these arrangements that you have referred to?

Mr Lawrence: There is a big difference between retained profits and cash. Retained profits is effectively the built up profits for years and years and years. You wouldn't necessarily reinvest that. That's

the shareholders' capital, so if the shareholder wanted that back we could repatriate that back to the shareholder, which we do via dividends every year.

Q113 Jim Cousins: How much will that be valued at when you become a Government-owned company?

Mr Lawrence: Well, you typically wouldn't value a company based on the retained earnings.

Q114 Jim Cousins: No, it would be transferred into it, would it not?

Mr Lawrence: Probably not. You typically wouldn't do that in this business.

Q115 Jim Cousins: So does that mean the Government this year will get that money back?

Mr Lawrence: No, but if the Government wanted to call back their retained earnings they would be able to call that back via dividends and the shareholder would ask us to repay some dividends if they wanted to do that.

Q116 Jim Cousins: And they have not asked you to do that?

Mr Lawrence: Well, we do. Every year—for the last couple of years—we have given roughly a £4 million dividend.

Q117 Jim Cousins: £4 million, but there is £50 million in the—

Mr Lawrence: But I don't have £50 million of cash to give you. If you want it, I could go and leverage the balance sheet, get a loan and give you some money.

Q118 Jim Cousins: Do forgive me, Mr Stafford was very proper earlier about his powers *vis a vis* ministers. You must understand this Committee has no power to compel you to do anything with your money.

Mr Lawrence: No, I am not meaning you personally, the shareholder. If the shareholder wanted that cash back they could extract it. The way they would have to extract it, though, would be to actually finance up the balance sheet because we don't have enough cash to give you that £50 million.

Q119 Jim Cousins: Your target for return on capital is 10%?

Mr Lawrence: Yes.

Q120 Jim Cousins: In fact I think you achieved that in the year before last. How many redundancies have you declared?

Mr Stafford: Within the last twelve months we have had no redundancies.

Q121 Jim Cousins: And in the twelve months prior to that?

Mr Stafford: In the twelve months prior, I think I am right in saying there were 200.

Q122 Jim Cousins: 200?

Mr Stafford: Sorry, it's the year before that, so for the last two years there have been no redundancies. Forgive me, it was back in 2005–06.

Q123 Jim Cousins: And your present employment is—

Mr Stafford: 765 permanent employees and about approximately 100 temporary employees, which flexes that according to seasonality, but there are 765 permanent employees.

Q124 Jim Cousins: The number of your permanent employees is not going up. Is the number of your casual employees going up?

Mr Stafford: As I say, we have to cope with seasonal peaks but basically we have a very stable workforce and we envisage over the next 12–24 months that we will increase our overall workforce by approximately 100 as we grow the business in commemorative coin for the London 2012 Olympics and we have announced that we expect an increase in our workforce of approximately 100.

Q125 Jim Cousins: Mr Stafford, would you confirm to the Committee that the Treasury guidance is that companies which move from a trading fund status to a Government-owned company status are generally on a path to privatisation?

Mr Stafford: I could not comment on whether or not that is the case because—

Q126 Jim Cousins: You cannot comment on the case that that is in the Treasury guidance?

Mr Stafford: I can't comment on that because the statement around the Royal Mint is that we are moving to a Government-owned company if we go through the vesting process. There is no intended statement of policy to move to privatisation and there has never been any public record of that fact.

Q127 Jim Cousins: The Treasury's guidance, general guidance on these matters is that organisations which move from trading fund status to a Government company status are on a path to privatisation?

Mr Stafford: That is your statement. I can neither confirm nor deny that statement because it is not for me to state what the Treasury's policy is on that matter.

Q128 Jim Cousins: You have never checked back to see that that statement is in the Treasury's general guidance?

Mr Stafford: Whether or not it is in the general guidance, it is not specific to the Royal Mint.

Chairman: We will have to speed up, I am afraid, because these are important issues. Mark Todd, fast, snappy questions, and snappy answers if we can!

Q129 Mr Todd: I will try. You currently outsource a significant portion of your work to third parties in other countries, I think in the USA, Australia—

there are actually some blanks in your report, am I right? Your Finance Director is nodding and you are looking blank!

Mr Stafford: No, I am not, I am trying to understand what you said. When you say “outsource”, we buy in precious metal blanks for our commemorative coins, so the gold and silver blanks for our commemorative issue.

Q130 Mr Todd: Okay, got it. You presumably faced a significant price increase in the last twelve months. Have you had any quality concerns?

Mr Stafford: We have had some quality concerns because when you start moving to new suppliers sometimes you have to be very diligent and ensure they understand the specifications that we demand, which may be higher than those which they have previously been used to, and we have had to work very closely with the suppliers to improve the quality of that.

Q131 Mr Todd: Has there been a transfer of blank production to these overseas locations from the UK or has that been something you have historically tended to source from those?

Mr Stafford: Three years ago there was a decision made to cease production of gold blanks in the Royal Mint because the volumes required were so small relative to the—

Q132 Mr Todd: I think I have heard silver as well, is that right?

Mr Stafford: Yes. So the answer is that a decision was made to cease production of them because the volumes were not sufficient to warrant retaining that production.

Q133 Mr Todd: Okay, now you have seen the outcome in terms of quality and price are you thinking that was the correct judgment to make?

Mr Stafford: We still are very sure that that was the correct decision because we have managed to negotiate better terms and improve the quality substantially over the last twelve months.

Q134 Mr Todd: Have you conducted a valuation of the business as it stands?

Mr Stafford: A valuation of the business? Well, part of the process for the vesting will be to determine what capital structure is appropriate for the new vested organisation.

Q135 Mr Todd: So does that include an exercise of valuing the business?

Mr Stafford: No.

Q136 Mr Todd: For example, for a trade sale?

Mr Stafford: No.

Q137 Sir Peter Viggers: You routinely screen for counterfeit coins and your estimate on that screening is that in October 2008 it was 2.58% of pound coins that were counterfeit?

Mr Stafford: Yes.

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Q138 Sir Peter Viggers: How do you respond to the coverage by a representative of Williams, a firm which make counterfeiting equipment, that in fact the true number of counterfeit coins in circulation is about twice your estimate?

Mr Stafford: We undertake these surveys every six months and we have got data going back several years, and we are very comfortable that our analysis is correct. We take a representative sample and we have statistically proven that there is a consistency in our methodology and therefore the right level is 2.58%.

Q139 Sir Peter Viggers: In 2007, I understand that 97,000 fake coins were removed from circulation, 97,000 for the whole year, whereas in the last quarter of 2008, I understand that 270,000 fake coins were removed. Are those figures right and what do they say?

Mr Stafford: What it says is that we are becoming much more vigilant in the way that coins are removed from circulation, so one of the tasks has been for the banks to improve the method by which their machines in cash centres removed the counterfeit coins from circulation. So the challenge is not to say how many coins there are currently in circulation but to actually remove them from circulation. We have worked very closely with the Serious Organised Crime Agency (SOCA) and with the banks to make sure that our processes for identifying and removing from circulation those counterfeits is much more thorough, and I am very pleased to say that the banks are doing a very good job.

Q140 Sir Peter Viggers: The problem is, of course, that no one has ownership of identifying counterfeit coins. The people who have got counterfeit coins, if they find they have got one it becomes valueless and it is not in your interest or in anyone's interest to damage confidence in the currency system. Do you think that someone should be given responsibility for screening counterfeit coins? Who should be responsible?

Mr Stafford: The people responsible are the banks because they are the people who actually circulate the coins through the system and they have a clear responsibility in their cash centres to identify the counterfeit and the machinery is there that is capable of doing it, and we also have to ensure that the public is well-educated and our task with the Treasury is to provide the education so that people know how to identify counterfeits. It is not our task to remove them.

Q141 Mr Brady: What is your long-term assessment of the demand for circulating coin in this country and in other countries?

Mr Stafford: Our long-term view is that demand for the UK circulation is remarkably robust. If you go back over the last decade, then demand has been almost without exception consistently around 1.3 billion coins per annum. The principal drivers for that demand are (a) removal of coins from circulation because people lose them, either down

the backs of their sofas or in jam jars, and also because when a new store opens, when Tesco opens a new branch, for example, there is the requirement for an injection of more coins into the system. If you look at those two principal drivers, they have been remarkably consistent. We have undertaken some quite detailed research to try and extrapolate what we see the long-term demand being and we can see nothing that is going to materially alter that demand.

Q142 Mr Brady: You do not see a threat from technology, different methods of payment?

Mr Stafford: No, because most transactions involving coins are for values less than £10 and in those situations even the Oystercard, frankly, becomes less attractive. It is really where things like a £5 and £10 note is involved that the crossover takes place.

Q143 Chairman: Can you explain to the Sub-Committee why you have changed the way in which your target one is measured?

Mr Stafford: Yes, it is to make sure we have a more realistic method of calculating the terms for shareholders. I will let the Finance Director who was responsible for recommending that change explain it.

Mr Lawrence: We use bullion to finance our precious metals and the question was asked before about supplying precious blanks from overseas. It is a very effective way of financing our bullion, which can be 20, 30, £40 million at any given time. To put it in perspective, the rates we are pay on that are less than half a per cent per annum, so it is a very effective way of financing our bullion purchases. If we did not change our method of calculation and we came to this Committee and were measured on our performance, we would actually start making some pretty poor decisions. So this actually allows the business to make the best business decision for the business.

Q144 Chairman: Is it in fact easier or harder to increase your average rate of return on the average capital implied?

Mr Lawrence: Technically, when we did the calculation for the prior year we made our target slightly harder, but it is the right decision for the business.

Q145 Chairman: Why did your Target 3 performance decline?

Mr Stafford: Target 3—

Mr Lawrence: Is the delivery of commemorative coins.

Q146 Chairman: Commemorative coin delivery in the UK.

Mr Lawrence: The primary reason is that in the first part of the year we released the new coins, the new reverses, which was the Heraldic symbol, and we had such a fantastic demand for that that it actually put

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us in a backorder situation and that drove us in the first part of the year to mean that we actually couldn't achieve our targets for the whole year.

Q147 Chairman: Why have your debtor numbers nearly doubled?

Mr Lawrence: Again, a very good reason. We had a very, very, very strong quarter four and the relationship in our quarter four, we had a high level of overseas debtors so our business was largely dominated by overseas customers, who typically pay us on 30, 60 day terms, and that was the reason for our increase in debtors. It's just that we had a very good last quarter of the year.

Q148 Chairman: You made quite a well-publicised mistake with the new 20 pence coins. How was that spotted?

Mr Stafford: It was brought to our attention by a coin collector, who identified it. We immediately went through the records to identify how this could have happened and it transpired that on the first day of production of the new reverses on one machine they had replaced the reverse design, i.e. the piece with the new design on it, but they had failed to recognise that on the 20p because of the nature of the design the date had had to be moved from the reverse to the obverse where the Queen's head is. Of course, they first looked and recognised that it still had a right Queen's head on the obverse but failed to recognise that that one needed to be replaced with one with the date on it. It happened on one machine for one shift.

Q149 Chairman: But why did nobody spot it in your organisation?

Mr Stafford: Because the person responsible checked that the dye still had a right Queen's head image on it but failed to identify—so it was an operator error. It caused one machine to produce it on one shift and it was then replaced, so it resulted in from 8.00 am until 1.00 pm on one shift—

Q150 Chairman: How many coins was that?

Mr Stafford: Approximately 200,000.

Q151 Chairman: I understand the operator error, but why did nobody check it? Why did it take a collector to spot it?

Mr Stafford: The answer is because on the initial inspection if you have got the right Queen's image—and all the other denominations did not involve moving the date from the reverse to the obverse, the 20p did, and it was an operator error which should have been spotted. Steps have now been taken to make sure that all obverse dyes involving the 20p have the Queen's image with the date on it.

Q152 Chairman: You have got the 200,00 back? Did you take them out of circulation?

Mr Stafford: No, they are out in circulation. There is nothing wrong with them in circulation, they are perfectly legal tender. It is a bit of a storm in a tea cup.

Chairman: All right, we are going to leave it there. Thank you very much for your evidence today. If we have further questions we may follow up in writing before our report. Thank you both very much.

Wednesday 28 October 2009

Members present

Mr Michael Fallon, in the Chair

Nick Ainger
Mr Colin Breed
Ms Sally Keeble
John McFall

John Thurso
Mr Mark Todd
Mr Andrew Tyrie

Witnesses: **Ms Lesley Strathie**, Permanent Secretary and Chief Executive, **Mr Simon Bowles**, Chief Finance Officer, and **Mr Richard Summersgill**, Director Benefits and Credits, HM Revenue and Customs, gave evidence.

Q153 Chairman: Good afternoon, can I welcome you back to the Sub-Committee; could you introduce yourself formally, please, and your colleagues?

Ms Strathie: I am Lesley Strathie, I am the Chief Executive of Her Majesty's Revenue and Customs, I am the Principal Accounting Officer. On my right is Simon Bowles, the Chief Finance Officer, who joined the Department in March this year and on my left is Richard Summersgill, the Director of Benefits and Credits.

Q154 Chairman: Thank you very much. The Capability Review in 2007 that we referred to in our last Report identified eight areas where you needed to improve, four of them urgently. You have issued your new document, *Purpose, Vision and Way*, you have got a new board, are you now fit for purpose?

Ms Strathie: We are very much fit for purpose but we have just gone through a pretty rigorous self-assessment at the two year stage. We are having our two-year re-review early and the Cabinet Office capability team have been with us until the end of last week. We currently await their findings on our self-assessment and we will issue in due course the results of that. We feel that we have moved forward enormously but we still recognise that there is a lot more to do and we have plans about what we will do.

Q155 Chairman: Two years after that Capability Review are you warning us then that there might still be some areas for improvement?

Ms Strathie: Yes. If we consider the ratings in terms of urgent development areas, development areas right through to strong in green, then our self-assessment has not given us all green, there are many areas where we recognise that we have got more to do and, as I say, we await the capability review team's findings on our self-assessment, and then there is a moderation process beyond. We still think that in most areas we have moved forward at least one level and in a couple of areas we think we have moved forward two.

Q156 Chairman: You carried out a staff survey back in February which showed that 70% of your staff did not think change was well-managed; 67% thought the changes would not be for the better and 64% felt as a whole the service was not well-managed. What can you say to convince us that you are taking your staff with you?

Ms Strathie: In short the survey tells us we are not and we take that incredibly seriously. One of the points that you have not mentioned is that the survey also tells us that amongst our managers many of them do not think they need to change. If we look at the challenge facing the department in terms of the head count reductions that we face, the degree to which our workforce has had to change job, change location and the uncertainty that has been created for many we have a very strong message in the survey of people who want to stay with the organisation but do not feel that they are clear about their future or that they would recommend HMRC as a good place to work. We are re-reviewing now, the survey is live at the moment, it finishes at the end of this week. The survey that is being carried out now is civil service wide—we were part of a pilot of 11 departments then—and it is a slightly different set of questions based on what we learnt from the pilot. Those results will be published in January but we recognise that clarity for our workforce about whether they have a future in the department, what that future looks like and how we are going to manage those people where we do not have a job for them in the future is going to be an ongoing challenge for us.

Q157 Chairman: My colleagues will certainly pick up on that survey later on. I understand by the end of the next financial year you are going to cut a further 3,811 staff; how are you going to do that without further reducing morale?

Ms Strathie: I cannot promise that there is not a danger in morale but given how low our scores are there is not much further to fall. We have a very disengaged workforce if we take it purely on the survey, but I actually think it is part of a basket of measures. My job, I believe, is to be absolutely honest with our people about how many jobs there will be, where they will be, what the opportunities are in all of the support package we have put in in terms of paying for people's transport, laying on different means of them getting to work, covering their extra expense and retraining them, but if at the end of the day there is not a job then we need to be clear and terminate that employment. Everything we are doing at the moment is to avoid compulsory redundancies, to take every step that we can do and currently we have a lot of volunteers. My approach will always be to try and find another job for someone if we can and actually we have managed to find jobs for 1750 people across

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other government departments and so far less than 7,000 people have been severed, all on voluntary terms.

Chairman: Andrew Tyrie, you had a question on this.

Q158 Mr Tyrie: You just said you have a “very disengaged workforce”.

Ms Strathie: According to the survey.

Q159 Mr Tyrie: What is your estimate of the effect that is having on the yield?

Ms Strathie: One could speculate. Very simply, my entire career has been leadership-driven with very large battalions of people and very similar challenges in terms of the balance between what modernisation offers us versus the impact on people and jobs. I would say that every week I visit a part of HMRC and every week I see people working incredibly hard, incredibly proud of what they do and working flat out to close the tax gap or hit any of our other priorities, but at the end of the day we are asking them how they view their department, whether they are proud to work for the department and how they rate senior managers. It shows us very clearly in the survey that people are proud of their own job, they are usually relatively happy with their immediate line manager and then when you ask what do you think of your line manager’s line manager it is less popular and it goes right up. I do not take the survey as the only measure of morale, that is my point, but I do take it really seriously that people want to stay with us but do not want to recommend us or say that they are proud to work for us.

Q160 Mr Tyrie: But you are going to want to take measures to put this right and some of those are going to cost money.

Ms Strathie: Yes.

Q161 Mr Tyrie: The obvious question for those who are going to agree to that, which is ministers, is what is the return, what is the output measure that you are going to ministers with, saying I need to do something about morale because if I do I get the following return?

Ms Strathie: At the moment we are very focused on those people who are in parts of our estate which are non-strategic sites, where we have already announced and ministers have already announced that we will be withdrawing our operations from those sites, and we are refining the dates for each of those and serving notice on them, and we have a programme of work which is focused. Money is made available from Treasury through our end year flexibility, to target those people as a last opportunity, can we find any way that they can move to another job and, if not, to do it. It is expensive to sever and we need the balance between those people who can be genuinely redeployed somewhere else and those people who are stranded.

Q162 Mr Tyrie: But you have not made an estimate of what it is costing you.

Ms Strathie: We know what we have spent so far—

Q163 Mr Tyrie: The question is what is it costing you in lost output, lost tax yield, that is the question.

Ms Strathie: I do not think we can.

Q164 Mr Tyrie: Not a penny. Have you lost any tax yield as a consequence of the fact that your department has poor morale?

Ms Strathie: I do not believe so, but I do not know so.

Q165 Mr Tyrie: It is just a quality of life factor in the building then, as far as the public is concerned we do not want to spend a penny on it.

Ms Strathie: The vast majority of our intervention yield comes through our large business effort and our litigation strategy so in terms of the total workforce that we have many of the people who will have to terminate their employment are people who have been with us long serving but in essence the world has moved on and the systems, processes, structures by which we achieve the yield have changed significantly.

Chairman: We need to move on; we can come back to some of these points. Colin Breed.

Q166 Mr Breed: Can we move on to tax collection which I suppose must be one of the most important areas, hopefully, of your activity. Between last November and June this year you agreed 158,000 time to pay arrangements; how many did you expect to agree, what was your forecast back at that time and then perhaps looking forward how many more do you expect to agree? We are trying to get an idea of the volume of these requests?

Ms Strathie: The first thing to say is that I consider this a huge success and a real demonstration of how fleet of foot HMRC can be when asked to deliver. Within three weeks we had this service up and running. We have always had time to pay; this was about broadening access and us scaling it up.

Q167 Mr Breed: Is that 158,000 extra ones or 158,000 including all the ones that you would have had anyway?

Ms Strathie: That is the total but we were doing this on a very rapid service on the telephone which was the modern part. By 11 October we had taken 335,700 calls from businesses and we had arranged more than 217,700 time to pay arrangements worth just over £3.8 billion.

Q168 Mr Breed: Where did the 158,000 come from then?

Ms Strathie: That was probably the latest briefing that you have there, I am talking about now, as of October 2009. It is an on-going service.

Q169 Mr Breed: The number at the end of that period was less than the peak of it at some stage. You are saying you did 217,000.

Ms Strathie: At October 2009, this month, the latest total is now 217,700 worth over £3.8 billion. In terms of delivering against those arrangements we have a success rate above 90% so we see that we have supported business through this difficult time but also we have brought more business into compliant regimes.

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Q170 Mr Breed: 10% have basically failed to honour their agreement, is that it, did not pay you anything in the end?

Ms Strathie: I used the term over 90% because I am not talking about a statistically valid series here, I am talking about where we have got to and what we are scoring, and some of that is on a sample basis. We know that that is a high level of compliance.

Q171 Mr Breed: Have you had repeat requests?

Ms Strathie: Yes, I believe that in those figures, although I cannot give you the details, if you consider VAT is something that is quarterly paid then there may be a case where we give someone a time to pay regime, they deliver on that and then there may be another time to pay regime on another head of duty.

Q172 Mr Breed: Are you reviewing the criteria, making it stricter or keeping it about the same or what?

Ms Strathie: When I say we got this up and running in three weeks time on the scale that we were doing it, it is something that is constantly under review and we are now developing robust systems and measures because we believe that this is something that will be with us for quite a long time.

Q173 Mr Breed: Are you more robust in refusing them now than you were a year ago?

Ms Strathie: I do not know what the figures were a year ago in terms of refusals.

Q174 Mr Breed: Do you know what the criteria were a year ago?

Ms Strathie: Yes.

Q175 Mr Breed: Are they stricter now?

Ms Strathie: It is very clear: if someone cannot pay they cannot pay, that criterion does not change. The extent to which we would look very, very hard in terms of who they were paying—it remains at the end of the day that the business has got to be viable, we have to believe that they can pay over a period of time and that criteria has never changed, we have just really marketed the service and encouraged people to come to us and get into a compliant regime rather than go below our radar if you like and us spend a lot of resource trying to get there.

Q176 Mr Breed: Next Saturday it is the deadline for paper tax returns coming in. As you will be aware there is a potential postal strike action planned for three days from Thursday.

Ms Strathie: Yes.

Q177 Mr Breed: Can you provide reassurance that no one who posts their paper tax return before Saturday will be fined for a late return?

Ms Strathie: I can give you assurance that we will take the postal strike into account. There is a legal deadline, as I am sure you know, but we will be very reasonable in terms of paper returns. We would

encourage everybody to file online rather than use the paper return as the safer option.

Q178 Mr Breed: The total revenue collected declined last year by about 5%; how confident are you that this reflects declining economic performance rather than increased tax avoidance?

Ms Strathie: The analysis would suggest that most of this is due to the economy. As you know, figures get revised at Budget time and the Pre-Budget Report, but what we are seeing is very much the impact on the economy. Where VAT is concerned you also had the reduction in the rate of VAT and an increase in debt.

Q179 Mr Breed: Have you made any estimate at all of how much tax is being avoided that you might have wished to have had?

Ms Strathie: I do not think that is something that I can answer. We have issued figures on avoidance in the past in terms of best estimate³, but it is not a figure I can quote to you today.

Q180 Mr Breed: We have had evidence here that clever firms of accountants and clever departments of banks are utilising the complexity of the tax code to devise ever more ingenious ways of selling a particular product to customers and clients in order for them to avoid paying tax, and that one of their ploys is that they actually come down to you and get a seal of approval before they go and sell it in the market. How much are you aware of that and what are you doing to actually counteract it?

Ms Strathie: We are absolutely aware that avoidance schemes are there, that avoidance is legal and that schemes need to be registered with us. Where at any point we believe that there is aggressive selling of avoidance, or indeed that any avoidance is on the borders of legality, our first test is always the policy intent: what was the tax policy designed to do and is this deliberately against the intent? Then we take measures pretty quickly to address that in legislation.

Q181 Mr Breed: You are aware, for instance, that agency workers for a variety of organisations are now being registered in the Isle of Man so they need not pay tax and national insurance?

Ms Strathie: We have issued quite a lot on avoidance, we have got lots of evidence to show that our anti-avoidance strategy is working and it is a constant, as you will see in each Finance Bill, to address any areas where we think it is absolutely outside the policy intent.

¹ *Note by witness:* In March 2008 HMRC released details of some analysis from 2005 that attempted to derive estimates of the direct tax gap at the start of the decade—see www.hmrc.gov.uk/research/measuring-tax-gap.pdf. This included a very broad brush estimate, for conditions in 2002–03, of direct tax avoided of £5bn—£15bn. As HMRC has made clear, these figures are far from certain and came from assumptions based upon agents fees reported in the accountancy press, which are likely to include commercial tax planning as well as the use of artificial avoidance schemes.

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Q182 Mr Breed: What are you doing to ensure that more people, particularly older people, actually pay the right amount of tax?

Ms Strathie: This is an area that the NAO have just looked at and indeed we signed off our report. This week in a very phased way once again we are contacting our pensioner population with a tax back campaign to target those people who may have savings interest where they have paid tax at 20% where 10% would apply, so we are trying to encourage customers to come to us so that we can make sure they have paid the right amount.

Q183 Mr Breed: How will you know whether that has worked or not?

Ms Strathie: We will measure it like any campaign, what is the response we get. The lives of pensioners have become pretty complex over the years with state pension, multiple occupational pensions and savings, and if you consider that many, many pensioners have just been in PAYE or the benefits system before they become pensioners, there is then a whole new world into self assessment. We are working closely with DWP and other partners to try to look at the whole end-to-end system and improve it.

Q184 Mr Breed: Just a couple of questions on VAT, how do you think business has been affected by the reduction in VAT to 15%?

Ms Strathie: Most businesses would say this was just a huge administrative burden and it does not make any difference, and I can appreciate it was an administrative burden. Other people will judge in the fullness of time whether it had an impact or not but I do sense that people do not feel the same when you add 2.5% to the rate of tax as they do when you take it away, and of course that rate will be returned, I believe, at midnight on 31 December, so time will tell.

Q185 Mr Breed: Is that a good date to return?

Ms Strathie: I do not set that date and many people have made representations that it is a difficult time.

Q186 Mr Breed: Would you agree with them?

Ms Strathie: When you have to reorganise all your systems it is an additional chore. If there is going to be any change on that the Chancellor will announce it.

Q187 Mr Breed: If the Government suddenly had a bout of commonsense and changed it to, say, the end of January, would that cause a great deal of problem to you?

Ms Strathie: This is a business issue.

Q188 Mr Breed: Would it make any difference to you?

Ms Strathie: Clearly it would make a difference to the overall receipts if spending levels on VAT-rated products remained the same.

Q189 Mr Breed: But not administratively.

Ms Strathie: The administration is on business with the increase here.

Q190 Mr Breed: Has there been a huge administrative burden on HMRC for the change in the VAT?

Ms Strathie: No, the huge burden for us was the speed at which we had to implement that change, and again we did a fantastic job to reach 2,000 businesses and the media and everybody else in the industry to make sure people were in shape to do it. It is really important that we understand here that product maintenance is for HMRC but we are the non-ministerial departmental collectors of tax.

Q191 Mr Breed: Changing the VAT change-back to, say, 31 January, would not cause you any great administrative problems or expense—you the Department.

Ms Strathie: Me personally, no.

Q192 John Thurso: Can we turn to departmental strategic objectives and DSO1. There are four indicators for DSO1 and I understand that only one of those has been assessed; why is that?

Ms Strathie: Can you tell me, in terms of being assessed?

Q193 John Thurso: For example, if I take indicator one, which is by 2011 to increase tax and national insurance contributions actually received relative to the amounts that should be received, achieving over 2008–09 to 2010–11 at least the levels set out in the public service agreement targets for 2007–08. The assessment is that it is too early to give us an assessment but provisional estimates will be published in the Autumn Performance Report—as an example.

Mr Bowles: In this situation it is early days on that particular indicator. We will be publishing, as you say, in the Autumn Performance Report when we will give a fuller indication of that performance.

Q194 John Thurso: You are assessing three of the other indicators in 2010; indicator four, the latest figures available are for 2006–07, our next measurement is in spring 2010. What I am asking is, is that adequate? Given that you have got a strategic departmental objective should we not have an annual assessment thereof?

Ms Strathie: I can say very broadly here that we are clear about the strategic objectives and we are clear about the outcomes in terms of each of those pieces of work to do. What we have been developing very clearly are the performance measures that will deliver the outcome because you cannot manage to an outcome base. A lot of these are statistics that will eventually be validated and revised and there is a considerable lag, so as we set all the objectives and the 21 new indicators we have been building the performance measures and then the key management indicators that go behind. It is not a do-nothing, it is just when we publish robust series of data.

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Q195 John Thurso: What I am really aiming at is that departmental strategic objectives are what a private business would call its core objectives that it is seeking to achieve. In most businesses that might run over three or five years but will be a part of each year's business plan and there will be a series of actions to indicate that you are on track, there will be mileposts.

Ms Strathie: Yes.

Q196 John Thurso: It seems a little odd to me that there do not appear to be mileposts; I was just wondering if you have them and if you are making an assessment.

Ms Strathie: We have an annual assessment and we have a number of indicators. If I think of what we do as an executive team in HMRC, we have the data flows once a month where we take a view from those measures whether we think we are on course or not. If we are looking at the £7 billion target we have over a number of years to close the tax gap then that is clearly something where we measure our performance and take a judgment of the volatility and, month by month, whether that is telling us we are on target or not.

Q197 John Thurso: Do you think you have sufficient ways of measuring and sufficient measurements taken to be able to monitor those activities to give you a clear idea?

Ms Strathie: I think we do. If I give you an example at the moment, the volatility month by month in each of the separate heads of duty means you can read very little into a month but we can immediately look at what is coming in against each of those management indicators to say whether that is on course or not. So on DSO1 at the moment we have moved month by month towards there could be another challenge of a billion and we need to have more action to we are about 0.2% ahead at the moment, but the level of tax due, the number of rebates—because clearly people are not due to pay the same tax in the current economic conditions—makes some of that looking like for like over other years more difficult to judge.

Q198 John Thurso: Can we turn to your number two which is related to improving customer experiences; how do you measure customer satisfaction?

Ms Strathie: We have a measure, we have an ongoing survey, and it covers the totality of our business and as the sample comes in each month and builds the information then if we are going according to target that is great and we learn from that, we celebrate it, where we dip below we then go back and do much more in depth questioning to find out where we have gone wrong². Currently at the moment we have had great news in our tax credit space, we have gone through the summer renewals and we took a lot of

action to make sure that we moved resources around to be able to manage that smoothly while we landed our new service for PAYE and national insurance. We have some impacts in our business tax area, with less satisfaction, we have seen some impact amongst agents with less satisfaction and we are drilling down to understand whether it was something we did and could have avoided or it was as we prioritised things that were there perhaps some people who felt they got less of a service.

Q199 John Thurso: Is your survey system something that is an internal system that you have constructed or is it one that is external and would meet some of the ISO requirements?

Ms Strathie: No, it is external but we do have a customer unit in the department and the customer unit leads on all of this, working with the whole supply chain—agents, third parties, welfare, policies et cetera—to build up what is really important to the customer and then to test our actions and their satisfaction. We will be launching quite soon our HMRC charter which sets out very, very clearly at the end of our consultation what people can expect from us in standard and what we expect from the people who have to deal with us in return. That will be led by Dave Hartnett, the second permanent secretary to the department and our most senior tax professional, and this will be independent in judging the standards for each of our lines of business.

Q200 John Thurso: At Annex E in your report, "Statistics and other information" you have the complaints received by HMRC which show overall quite a modestly significant rise between 2007–08 and 2008–09 and in quite a lot of key areas quite big rises. I know that complaints are only one measure of satisfaction but how do you reconcile that rise with the concept of improving customer satisfaction?

Ms Strathie: You are right to say it is one of a basket of measures but I cannot believe there is anyone in the Department keener to end customer complaints because they ultimately end up on my desk late in the evening every night and I am responding to many of them. One of the steps we have taken on the analysis of the numbers you are talking about is to address the manner in which we deal with people, because a very large chunk of those complaints have been about rudeness or tone or the way that we handled them rather than the subject matter in the first instance.

Q201 John Thurso: Is there a correlation between that and the poor call centre record, the fact that people are no longer dealing with their local human being but are now going through to a call centre which has a pretty poor track record?

Ms Strathie: Again, our contact centres have come on in leaps and bounds in this past year and we certainly answer a far greater proportion of the calls offered and we have a high satisfaction level on the quality of the conversation that our customers get when they go through, so I do not see that as the real relationship. Most of the complaints I see are about

² *Note by witness:* The HMRC Customer Survey is conducted quarterly, covering nationally representative samples of 2000 individuals, 2000 SMEs and 1750 agents. Latest results were in September 2009—The Benefits and Credits and SME business customer groups are currently at or above the 2011 target.

the time we took to handle, or something went wrong and we did not say sorry and deal with it, or people feel that they were routed from one arm of the system to another rather than us taking responsibility for solving the issue for the customer and getting back to them. We have moved on a lot but if you consider that on any one day we have 40 million customers there are always going to be those where something goes wrong.

Q202 John Thurso: Do you think answering 90% of all calls is actually a high enough figure as an aim? Your stated aim is to answer 90% of all calls.

Ms Strathie: That is the industry standard and we have quite a way to go before we hit that standard, but it is my standard and it is the industry standard. To be able to answer at least 90% of all calls offered and to answer 80% within 20 seconds is what we aspire to, and you do that by reducing the demand, not by increasing the supply. There is lots of evidence in the customer space to show that lots of these calls have no value to the organisation and no value to the customer, they are often generated by our own communications and a lot of them are customers who could handle things on our e-channels. We have a number of actions in hand to improve that.

Q203 Ms Keeble: I wanted to come in on this because I completely agree with your point that when you get through to your staff they are exceptionally helpful and friendly; there is an issue though about the phone answering, which is very important to people, because it says that your aim is 90%, your standard across the board is 57%, in off peak times you reach 75%. That suggests that at the peak point, when people are most concerned and agitated and up against deadlines, your responses must be very much lower than 57%; what are they?

Ms Strathie: When we were looking at this when we were in the 50s we broke this into the number of days we were open and tried to pick out where the peaks are occurring and where the service dips are.

Q204 Ms Keeble: We have got the figures here that show that you have got 57% across the board, 75% in all but three weeks outside of your peak period, so what is it in your peak period? It must be around 30% in your peaks, is that right?

Ms Strathie: The figures you are turning to, on some of those we have actually moved. We have moved the call answering up quite a bit since then, but that was very much the focus of our action plan to improve our call answering.

Q205 Ms Keeble: Is it the case that in the peak periods it is about 30%, because that is what your figures are suggesting?

Ms Strathie: I honestly do not know what it is as of today.

Q206 Ms Keeble: Does anyone else know?

Mr Bowles: We can say that we were over 70% in our most recent numbers against 52% a year previously so I think that is indicative of an improvement.

Q207 Ms Keeble: Perhaps you could have the figures clarified because if your average across the board is 57% and your average in the off peaks is 75%, your average in the peak periods must be very low indeed.

Ms Strathie: We would accept that.

Q208 Ms Keeble: It would be helpful to know so perhaps we could have those figures. Given that you know exactly when your peak periods are, because you have set them out very clearly, what are you doing to shift resources to make sure the phones get answered during the peak period?

Ms Strathie: As I say, the first thing we are doing is actually looking at the cause of all of the calls. Many of those calls come from what I suppose we would categorise as the “worried well”, so people ring up just to check we got X, or ring up just to check something—even when we write and tell people you do not need to take any action about this they do, so we have taken steps to try and manage that. On moving people around, our contact centres cover a lot of different services and lines of service so we prioritise in summertime tax credits renewal, we prioritise at other times on business support services.

Q209 Ms Keeble: If we could perhaps have the figures, I want to go on and ask about some other things³. One of your other targets is around fraud on tax credits and I wanted to ask some more about tax credits. You say that in the last year or when the assessment was done it was before you had done your new strategy and the central estimate for the level of fraud was 8.6%. I understand in fact that that is a slight increase on the previous year; can you say why then you are very confident that you will get down to 5%?

Ms Strathie: That is the combined fraud and error or the error figure. Richard, do you want to answer?

Mr Summersgill: The latest published statistic is 8.6% and the previous year was 7.8%; the statistic for 2008–09 will not be available until next summer. The error and fraud strategy formally really began in this financial year, 2009–10, and effectively the first phase runs for two years through to April 2011, so the very vast majority of our activities are taking place over the 24 months starting in April 2009. We calculate that those activities over that two-year period should get us down to 5%.

Q210 Ms Keeble: You also assess that the current take-up rate for working tax credit is only 57%; what do you think would be an acceptable take-up level and can you also as a second part to that say how that has been affected by the recession where quite a number of people, if they have had a reduction in hours and earnings, will be applying for tax credits, often for the first time?

Mr Summersgill: For child tax credit the take-up rates are around 80% and for child benefit it is 90% odd. For working tax credit it has always lagged behind and we do have a target to keep working on

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that. A particularly difficult area is within working tax credit only, it is the people who are only entitled to working tax credit.

Q211 Ms Keeble: That is for childless families and single people.

Mr Summersgill: Yes, people who do not have caring responsibilities for children any more. Within that there are two particular groups that we are trying to focus on: couples over 50 and young men over 25 which tend to be the groups in particular that are more resistant to taking up working tax credit. Quite a lot of our activity is focused at those groups.

Q212 Ms Keeble: What are your targets for those different areas?

Mr Summersgill: We have agreed with the Treasury a target for the working tax credit only sub-category which is to increase effectively the caseload by 100,000 by spring 2011.

Q213 Ms Keeble: What would it be in terms of the take-up rate roughly?

Mr Summersgill: Depending on how the statistics are crunched that will certainly get it into the 60s. One of the reasons we do do it in that way is because we can actually measure that almost in real time, whereas the percentage figures are based on entitlement and they lag.

Q214 Ms Keeble: Sure. How about the child care element which used to be the old child care tax credit which looks very generous on paper but for some reason the take-up rate had lagged way behind. What is happening about that?

Mr Summersgill: I do not think the child care take-up rate is lagging. I am not sure I have the actual detail but there is a very high take-up of child tax credit and the child care element amongst eligible families.

Q215 Ms Keeble: I particularly wanted to ask about that because we had asked about it previously and there were some issues around the fact that for some reason the take-up of that was not increasing in quite the way that was envisaged, and it was very difficult to find out exactly why that was.

Mr Summersgill: In fact it is not actually measured separately from take-up of child tax credit and working tax credit per se.

Q216 Ms Keeble: You do not look at the child care element.

Ms Strathie: We do not measure it, that is what Richard is saying.

Mr Summersgill: We do not measure it.

Q217 Ms Keeble: Are you sure about that because when it was a child care tax credit it was definitely separately measured and when it switched over to the child care element there was then some discussion about it because I was very keen at the time to see some improvements to it, to make it more effective. There were a number of answers that came forward which suggested that there were issues about it—

either the take-up was not going up or the take-up was not increasing. There were some issues about the take-up of it.

Mr Summersgill: We cannot survey the number eligible so we do not have the divisor to calculate the take-up percentage. It is possible we may be able to determine from the system the number of cases, I will look at that.

Q218 Ms Keeble: You should be able to determine the number of cases and that would be helpful. Would it be possible to have that and to have some tracking of it so we can see what is happening to it over time and whether there is an increase in the take-up?⁴

Mr Summersgill: I will see what we can pull out on that.

Q219 Ms Keeble: Thank you. I wanted to ask also about the errors, the overpayments and underpayments. Looking at your figures you had the big reductions in overpayments which look as if they came after the rule changes.

Mr Summersgill: It was the 2005 PBR changes.

Q220 Ms Keeble: How much of your improvement in the performance on overpayments do you attribute to the rule changes and how much do you attribute to your own administrative improvements?

Mr Summersgill: We said at the time it was going to be about a third reduction in the value of overpayments relating to the PBR 2005 change and that is broadly what the statistics do show. There have been further improvements besides.

Q221 Ms Keeble: What I am interested to know is what you have done in administrative terms to improve the position on overpayments. Underpayments have actually got worse but what have you done to improve your performance there over and above the rule changes? It was very sweeping and was always going to lead to improvements.

Mr Summersgill: A huge amount of the things we have done under the banner of the tax credit transformation programme have been entirely focused on helping customers avoid overpayment so many of the products we have rolled out like the service for households that are breaking down, where couples are splitting up and so on and we have given them fast track services, the in and out of work projects, assisted renewals—there have been about a dozen different offerings over the last couple of years which have helped people manage their overpayments. To some extent that has also helped customers manage themselves into an underpayment which is why underpayments and overpayments are now in broad equilibrium. An underpayment of course effectively means that at the end of the financial year that customer will get a cash payment.

Q222 Ms Keeble: Looking at your tax credits debt for recovery, which is in your report at our page 39, you have got a very sharp increase in total debt for direct

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recovery and a very gentle increase and then a plateauing off of direct recoveries in a year. How do you explain those figures?

Mr Summersgill: Over time the ideal is that we try to recover debts from an ongoing award where we are taking a small amount from an ongoing payment. When that ongoing award ceases, either because the family lose entitlement or because the household breaks up and new households are formed then the debt goes into our direct recovery. All of the evidence shows that once we do put debts into debt recovery it becomes increasingly difficult over time to collect them.

Q223 Ms Keeble: I just wanted to ask one final thing which was that in some research that I did in my constituency over the impact of the recession it showed that just under 50% of the families who took part in the work I did actually received tax credits, so it is an astonishing number in an area where people work but they have been impacted by loss of hours, loss of overtime, one person earning and so on. What is your estimate nationally of the impact that the recession is going to have and what are you doing to meet those challenges because the tax credits have been incredibly important and, personally, I would like to see lots more benefits pulled into them, but it does rely on your being able to run the system in a very robust fashion and that means having some proper projections as to what is going to happen.

Mr Summersgill: I do not think we have an estimate of how the recession has affected the increase;⁵ there undoubtedly has been an increase with people's hours reducing and so their entitlement to tax credits has increased. We have also done quite a lot of work in terms of helping people, both through the work we were talking about a little earlier in terms of encouraging the take-up of working tax credit, also the joint working we are doing with the DWP and local authorities on in and out of work so that as people move from tax credits or benefits or vice versa we have devised fast track procedures to help them get into tax credits or benefits more quickly. There is more work to be done though.

Q224 Mr Todd: I want to look at IT in HMRC. Firstly you were urging people to use the online self assessment system; is it working?

Ms Strathie: The online system is indeed working.

Q225 Mr Todd: There have been some reports of problems.

Ms Strathie: I saw that in the media today and we update on the system explaining what any issues are. We have probably about 7,000 people affected with some of the HMRC software rather than agents or anybody else who are using it differently and we will have it fixed pretty quickly now that we have got to the bottom of the problem.

Q226 Mr Todd: You have identified the problem and can fix it.

Ms Strathie: Yes, we are absolutely confident of that.

Q227 Mr Todd: You are obviously aware that confidence in that system is absolutely critical to its use.

Ms Strathie: Absolutely.

Q228 Mr Todd: If your reports become more prolific you will have difficulty getting people to use it.

Ms Strathie: Given that at the 31 January deadline we had 69% of people who filed online while this year, year-on-year, we are already ahead at this time—the take-up is huge so we monitor it daily.

Q229 Mr Todd: We have made some recommendations in the recent past over IT and HMRC and I want to pick out one or two and find out what has happened. We noted the proportion of cases that you have in open case where they are clerically handled; the data that we had at the time we looked, which was at the very end of last year, was that you had 16.2 million open tax cases and we suggested that there should be performance targets monitoring your ability to bring that number down. We have not seen any data suggesting that there has been an improvement, has there been?

Ms Strathie: This is a start which might not sound very good news but moves the conversation on. The constant growth in open cases would only be reversed when HMRC implemented the modernisation of the PAYE system and the release 3 which then merged 12 databases into one, very high risk and very successful. That does not cure the open cases but it stops the creation of the majority of all open cases. Those cases rose to around 30 million and we managed that back to 17 million in preparation to release MPPC3, bearing in mind this had been deferred and had not delivered on time.

Q230 Mr Todd: And we very kindly did not criticise you for that deferral; I remember amending the recommendations so that we did not.

Ms Strathie: I take responsibility for everything in HMRC but I arrived last November after this programme was running late. An enormous amount of work went into the entire business, not just the programme, to give a clear runway and we did. We are now working with the National Audit Office on those cases because release 4 comes on 24 November and we have release 5 in April; once we get to April we have then got the facility to start working the rest of the open cases. We are frozen in time now as we close down the old system. Some of those cases will be written off, I am pretty confident, but we are determined that we will clear them all.

Q231 Mr Todd: Can I gently criticise your lack of candour?

Ms Strathie: Please do.

⁵ *Note by witness:* HMRC is currently forecasting that as a result of the recession an additional net spend on tax credits of up to £500 million annually. HMRC does not have an estimate of the impact on take-up rates.

Q232 Mr Todd: We have in this report a reference to your achievements in IT.

Ms Strathie: Yes.

Q233 Mr Todd: I do not think any of what you have just told us features in your annual report; that gives a wholly unbalanced picture of what has been happening in a critical part of your business. Let me just read the point that is in here: "HMRC has been hailed as a shining example of how to use technology to take government services to a new level for its self assessment online." You do target it at one particular thing but one might get the impression that this was the general picture of IT performance within HMRC and it would be fair to say that would be a very partial picture, would it not?

Ms Strathie: Absolutely, but if I can just push back a little on that.

Q234 Mr Todd: Go on.

Ms Strathie: We did land MPPC3 at the end of June so it was three months beyond the completion of the annual report. There probably is—but I will stand to be corrected—a record of open cases there. HMRC has got over 200 IT systems; we had a huge legacy from two very large departments and there is masses for us yet to do before all of our systems will have moved on from 1970s technology.

Q235 Mr Todd: Can I let you instead send us a note which actually gives a more accurate summary of what is happening in your IT resources in HMRC than the somewhat partial picture that one might get from the document that we have in front of us?

Ms Strathie: I shall give you a full update on that but I stand by every word of that in terms of what HMRC has achieved.⁶

Q236 Mr Todd: I am sure. Can I turn to something that is in your annual report?

Ms Strathie: Are you going to stay with IT?

Q237 Mr Todd: Yes, I am.

Ms Strathie: I would like to brief the Committee on our IT contract and a press release that we will be releasing tomorrow, so you might want to come back to that, Chairman. It is in terms of our relationship and our costs but we can cover it.

Q238 Mr Todd: We are aware that something may be imminent but you are presumably not able to tell us what your announcement will be.

Ms Strathie: I can tell you there will be a press release tomorrow stating what new agreement we have worked with our current contract, with our Aspire contract, and the suppliers that are part of that ecosystem, which will significantly reduce cost for the department over the coming years.

Q239 Mr Todd: Maybe it will cover the point that I was about to ask which is about disaster recovery, which is referred to in your annual report and where the risk profile remains high. What is being done to address that?

Ms Strathie: We are actually working very closely, taking this from a business continuity perspective, not just starting with disaster recovery, and reviewing all of our systems in terms of the cost versus the potential risk mitigation and satisfying ourselves of what we can ultimately afford and what we believe, based on what other organisations have done in reducing that. Our new chief information officer who joined us on 2 September is undertaking that work with our head of risk who was appointed a few months back in the entire business. There are systems identified that do not have an IT solution in disaster recovery but I would contend from all of my experience and for other companies that a vast amount of money spent on these will not give a vast amount of risk reduction and we need to look at the other mitigations.

Q240 Mr Todd: Could you summarise that position to us as well?

Ms Strathie: Yes, sure.⁷

Q241 Mr Todd: I agree with what you just said, incidentally, but I would welcome a bit more quantification as to how you are approaching that.

Ms Strathie: Yes, we will do that.

Q242 Mr Todd: The online PAYE system has been rescheduled, is that right? This is the change to the online PAYE service.

Ms Strathie: The modernisation of PAYE goes on. We have talked about release 3, 4 and 5 which will give our people a single view of their customer and enables them to answer the vast majority of questions. You may be talking about our next big wave of PAYE. At the moment we have been working our way through feasibility and a number of options for what we might recommend to Treasury.

Q243 Mr Todd: We are nowhere near to getting a particular picture of where we are.

Ms Strathie: No, we have not issued a consultation document or anything like that yet.

Q244 Mr Todd: Okay. Can I just turn to some efficiency questions as well? The website that covers value for money for HMRC has a variety of figures within it on operational savings but I was not entirely clear whether some of them overlapped each other, so it would be helpful to separate them out. If I pick out some of the ones where I puzzled in particular, there was the reference to reductions in administrative work related to greater accuracy as a result of direct data input. This is over self assessment, PAYE and encouraging online filing and that produces a saving of £50 million by March 2011. There is what I would take to be a separate amount

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relating to workforce changes and estate management of £70 million by 2011 and then there is another one which relates to £60 million worth of savings through the delivery of the OEP back office programme. Some of these appear to be shooting at similar targets so it is not quite clear whether they are all added together, they overlap to some extent, what?

Mr Bowles: The answer to that is you can add those together and I would be very happy to give you a note showing how those relate to each other.

Q245 Mr Todd: They are all separate and there is no overlap saying part of that includes a property saving and that is in this figure as well.

Ms Strathie: No, we manage this as a portfolio, as one programme, and indeed it is internally audited and open for NAO to validate our figures, so we are clear on that.

Q246 Mr Todd: With efficiency programmes of this kind, and you have had plenty of experience of this already, we have discussed staff morale implications—that is one thing that certainly arises—the other implication can often be a decline in customer service. How are you monitoring the quality output when you deliver a change programme that delivers a saving of this scale?

Ms Strathie: Could I use the example of MPPC3 that we have talked about? We recognise that this is a huge change for our people and a huge change in the use of the IT and the information, and in line with best practice we put in 1,500 floor walkers, skilled up and ready, who supported their colleagues from day one go live and also all of our coaches and quality managers captured all the immediate learning because you could not practice on the system, it was a release and a no regression basis. We captured that straight into the central programme, constantly (it is almost on a daily basis) with our suppliers, deciding, “Is this an IT tweak we need here, or is it actually a process change, or is it a quality learning issue?” I think the success that we have had and the rate that our people are getting up their learning curve means our customers are getting a much better service. It will not be perfect until we have had the next two releases.

Q247 Mr Todd: This is your floor walkers telling you this. Is there an external reference?

Ms Strathie: Across the different products and services that HMRC delivers, we have accuracy measures and we have quality managers. I would not pretend that we do everything perfectly everywhere, but we do have to look through our problem-solving techniques and lean processes to collect that information and put it back into the system in terms of how we train and develop our staff.

Q248 Mr Todd: The answer to my question directly: there is not a formal external reference point to test your quality, other than direct complaints of some kind?

Ms Strathie: The NAO audit us, we have a number of people who take a very strong view of different parts of our service, and whilst our customer unit is still internal to HMRC, we do operate it in a way that it is a challenge to the business.

Q249 Mr Todd: I think when I asked you about your relationship to Mapeley before, I was surprised to find that you had a very flexible arrangement in which you could, effectively, toss back office space to them to sort out without any penalties at all. Is that the case?

Mr Bowles: Can I come in on that? I think it was not quite as rosy a picture as you described. We do have a lot of flexibility and over the contract (which, as you recall, runs for 20 years from 2001) we can hand over 60%.

Q250 Mr Todd: So you can hand over any 60% of your property without penalty to them.

Mr Bowles: Yes, and over a period of time. It is not something that we can do immediately.

Ms Strathie: It is 12 months' notice we need to give, minimum.

Q251 Mr Todd: Sure, the normal penalties one might expect of unfulfilled leases do not apply.

Mr Bowles: They have essentially taken on that portfolio.

Q252 Mr Todd: They take that risk.

Mr Bowles: Yes.

Q253 Mr Todd: It would be useful to have a little note summarising that. If you are going through a programme of significant office reduction, which you are, it would be useful to know what the constraints are.⁸ I must admit, I admire the person who negotiated that, if that is indeed what it is.

Ms Strathie: At the end of the day, this is one of my largest contracts, the other being Aspire, and you get the best by working in alliance; so we work very closely in how we do that.

Q254 Mr Todd: Nevertheless, they have got a chunk of risk.

Ms Strathie: Yes.

Q255 Nick Ainger: Can we go back to the staff morale issue and the changes that have happened over the 12 months to 31 March 2009? What impact have those closures had on morale and performance, and how do you measure performance?

Ms Strathie: We always assess measures depending on which area of the business we are involved in. If I go back to the morale issue, we are very clear about what the survey tells us, and that is why we are very eager that we encourage everybody to fill in the new survey and we deal with the findings. We are committed to doing things about it, but the morale issue for many is that they have been in a position for quite a long time knowing the building they work in is not a strategic site for the job that they do, or that

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the job that they do is now done in another way, on a self-serve basis or online, and that we have not been able to find a new job for them—they have not been able to move to where the work has moved or another opportunity—and for people who have, in many cases, quite long service, the only certainty we might bring is that there is no future for them or we cannot place them in another government department. That is at the core of our issue. I also think in our tax profession, which is about 17,000 of our workforce, we have recognised a need to build that profession and deal with some of the gaps we would foresee in future years and upskill and accredit our people. So we have taken an enormous amount of action and what it tells us. I am not going to say I will come back here in six months' time and there will be a step-change in the survey of sorts in morale, but that does not mean that we are not doing an enormous amount on this.

Q256 Nick Ainger: I hear what you say, but it seems to me that what you are saying is you need to tackle some issues relating to individual members of staff, training, and so on. If you actually look at the survey published in February 2009, the most severe criticism is aimed at management and, in particular, senior management. I will just quote, for the record, some of the results: "When changes are made they are usually for the better". Sixty-seven per cent said, no, they are not, and only 9% agreed that they were. "HMRC as a whole is well managed." Sixty-four per cent said, "Oh, no, it is not", and only 11% said it is. "And overall I have confidence in senior civil servants in HMRC." Sixty per cent said, "No, I do not", and only 11% said, "Yes, I do." Does that not give you an indication that perhaps this morale problem is actually not about staff performance but about senior civil servants' performance?

Ms Strathie: Yes, I absolutely accept that. The point I made earlier in the work that we have done (bearing in mind we have an awful lot of managers and leaders in HMRC), despite all of that, many of our managers do not believe they need to change, and clearly we all need to change. The best performance will be delivered at the end of the day with a skilled, motivated, engaged workforce that is proud to work for the department. I do not defend those results in any way at all.

Q257 Nick Ainger: In the report it is rather difficult to establish exactly how many people left HMRC in the year from March to April 2009, because the report quotes various categories of how they left. It is on page 40. Is that the total number that left in the 12 months to April 2009, or were there more people leaving because, basically, they were on maybe short-term contracts, they had moved on because they got an alternative and they were not engaged in any severance scheme? I am just wondering about the actual numbers, because earlier in the same paragraph it says that the numbers have been reduced from 105,000 to less than 89,000; it does not actually give the dates for those.

Ms Strathie: The 105,000 is when the department was created in 2005, and the 89,000, and they are both people figures, they are not head count, so they are not full-time equivalent. We have about 25% of people who work part-time. So they are people numbers.

Q258 Nick Ainger: I added all those categories up and it came to 2,061 members of staff. I do not know if that is full-time equivalent.

Ms Strathie: Our staff in post figure on 1 April 2008 was 83,828. So by that time there was a reduction of 13,927; 1 April 2009, 81,160; 1 October 2009, 78,424. In between all of that we also transferred a small number of people to SOCA, when it was created, and we transferred 4,500 to UKBA.

Q259 Nick Ainger: Have you got a figure of the number of people that left HMRC in the 12 months to April 2009?

Mr Bowles: It should be 2,700⁹ approximately. I am just taking the difference between the two numbers that Lesley quoted.

Ms Strathie: But you get a snapshot at the start and you get a snapshot at the end. Clearly, people enter the organisation and people leave the organisation during that time.

Q260 Nick Ainger: Coming back to the point I was making and that you seemed to be agreeing with me about the problems of your management, in that same period only seven posts in the senior Civil Service category were removed. I do not know what has happened before that, but we have seen literally tens of thousands of people in the past four or five years lose their jobs in HMRC. I just wondered how many of these, quite frankly, according to this survey and your admission, very poor management have actually lost their jobs or had their posts removed, combined, altered in some way.

Ms Strathie: There are several points in that. First, the Senior Civil Service in HMRC, which is the largest in the Civil Service, has a very different shape to the Senior Civil Service in most departments, even DWP, my previous department—that is the only other big comparator in terms of a big deliverer—and that is because a very large chunk of ours are senior tax professionals who are in that category, who do not have large commands at all. Most of our management and leadership is actually in the two feeder grades below the SCS, what we would traditionally know as grade six and grade seven, but there are obviously a number of SCS. I would be very happy to provide the figures on what the pattern has been on the three different levels within the SCS and over the period of time, but I would also say that most of the modernisation has eradicated lower level work. The leaning and eradication of waste in process, the move for customers who want to serve themselves online or through telephony, the way that we do the job, means that huge numbers of lower level jobs disappear, and that, as I have said, is the

⁹ Note by witness: The net leavers figure for 2008–09 was 2667 FTEs.

current challenge for the department. It has been the challenge for a long time and it will continue to be a challenge for us.

Q261 Nick Ainger: We have heard criticism in the past that the number of business sectors which exist in HMRC actually leads to a top-heavy management structure. Have you reviewed that? Are there 37, something like that, separate business sectors?

Ms Strathie: The original creation of the department had 36 different business units. The organisation was reshaped into lines of business (personal tax, business tax, benefits and credits and compliance and enforcement) in February 2008, I believe, and since I arrived last November, along with other changes, we have been building the new Executive Committee and the new Board and we have been developing a unified approach to HMRC in terms of our strategy and then what that means for the organisation design, the management structures, and so on, that we need for that. So the 36 business units would not be recognised in quite the same way as they were then and we will all be subject to shaping ourselves fit for the future.

Q262 Nick Ainger: Will that lead to savings in management?

Ms Strathie: The efficiency challenge we face means that we have to look at every cost burner in the organisation, and good organisation design is always a central plank in any efficiency programme.

Q263 Nick Ainger: The year 2007–08, the year before (and admittedly you were not there then) saw the biggest reduction, I think, year-on-year of staff. It also coincided with a 38% increase in overtime. Is that poor planning? In other words, you were making too many people redundant and you ended up having to pay some substantial amounts of overtime.

Ms Strathie: Overtime is something I would have looked very hard at myself, because it is always an indicator. I personally believe that we should manage the business in a way that we only use overtime on two occasions: one where we have “out of hours” type work, of course, very much in the Customs space and some others, and in the enforcement and compliance space we need that—we have to do the work when the work needs to be done—and the other is when we have large peaks of work to be done, like when you are preparing to land a big programme. You are not going to take on an army of permanent staff and the cost of training all those goes up, but you will ask for staff to voluntarily work additional hours for that period. I am quite sure Simon has a view too on how we are managing the whole of those finances.

Chairman: We are running into our last 15 minutes, so we have got to keep the answers as brief as we can.

Q264 Nick Ainger: Can I move on to a different issue, and that is litigation and the policy that is followed by HMRC in terms of bankruptcy petitions? Have you any idea—I cannot find any

numbers in the annual report—of the number of bankruptcy petitions that you have sought against businesses? The reason I ask the question is that I have had a number of companies in my constituency come to me, basically, extremely concerned at the attitude that is being followed by HMRC, in that they are following a rigid structure rather than taking each case on its merits. For example, if an IVA has failed, then HMRC will not consider a second IVA, despite the viability of the company and, as a result of that, people are being pursued through the courts. Could you, first of all, give the committee numbers (previous years and current) of the number of bankruptcies sought, and, secondly, whether you are keeping under review the policies which are being followed which seem to me to be too rigid and may well be putting viable companies actually into bankruptcy, resulting in further unemployment in the recession?

Ms Strathie: Firstly, I believe we have had a PQ and answered on this, so I shall take it away and confirm. I go back to our business payment support service. We are not a preferred creditor. Insolvency produces a very poor return for the Exchequer. We have worked very, very hard with companies, if we believe they are otherwise viable, to avoid that—I am very clear—but in terms of numbers we will take that away.¹⁰

Q265 Ms Keeble: According to this survey, you have only 12% of people who think that they are energised to go the extra mile and 71% who intend to still be working for you in 12 months.

Ms Strathie: I know.

Q266 Ms Keeble: That means you have a poorly motivated workforce but one that intends to stay with you, and that is a big challenge given what you have to do. How do you intend to energise them?

Ms Strathie: We have done a lot of work. In fact, one of my members of the Executive Committee on our General Council is leading this, with the rest of the Executive Committee, in having champions in place, following through with conversations with our people, and we have the new survey and the amount we are putting into it, but I do feel very strongly. I have never seen a set of results quite this shape in my very long career where we have twice as many people who would want to be with us, in fact three times as many people who want to be with us and stay in the organisation, but are not proud to work there and would not recommend to it anybody else. That in itself tells a story, and I do not think it is just the economic conditions that prevail that make them want to stay. I think it tells me that people do want to stay but they want HMRC to be different.

Q267 Mr Breed: In my experience, low morale often goes together with high sickness.

Ms Strathie: Yes.

Q268 Mr Breed: That seems to be the case in yours, so what are you going to do about it?

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Ms Strathie: Our current attendance figures are above ten days—that is global—in terms of average working days lost per person. That is about 8,000 days per year.

Q269 Mr Breed: What are you going to do?

Ms Strathie: We are doing quite a lot of things, and in many pockets of the business we have significantly reduced the numbers. We have a number of strands of work but it starts with best practice and making sure it is applied. All of our policies in this area are as good as anybody else's, but it is the quality of the intervention, making sure that everybody has a back-to-work interview when they come back and that that back-to-work interview is very clear about what the impact of their absence was and what is expected. We have recently piloted and are now introducing nursing support, where people need to report in.

Q270 Mr Breed: When you come back next year, what do you think the average absence will be?

Ms Strathie: I think, if we look right across Whitehall, bearing in mind we now do all measure this the same way—we do not measure it the same as the private sector; we are pretty tough on ourselves; we do not discount anything—the target that we are working towards is eight days. Do I think that that is good enough? No, I do not, but it will be a struggle to get there.

Q271 Mr Breed: Eight days in a year's time?

Ms Strathie: Yes.

Q272 Mr Breed: You acknowledged in your account a serious weakness in the management of health and safety. Why is it, briefly, and to what extent is health and safety a matter for your PFI contractor, Mapeley, to address?

Ms Strathie: I think, with a workforce the size I have and an estate network the size I have, health and safety has just got to be up there as a priority, and we believe, for an organisation going through the amount of change we are, especially the change to our network and estates, we need to be clear that all of our managers are equipped to discharge their duty of care.

Q273 Mr Breed: Who is the serious weakness: HMRC or Mapeley?

Ms Strathie: I do not think that I can say it falls neatly, bearing in mind this a PFI and we are talking about what happens inside the organisation as well as the buildings. It is a shared responsibility, but, ultimately, we are the employer. Every manager in every site carries that duty of care.

Q274 John Thurso: Can I ask you about your remuneration policy, first, on the non-executive directors? You seem to have two bands the 30/35 and another band at 20/25. Is it an accident that all the women are on the lower band?

Ms Strathie: I suppose I prefer to celebrate the fact that there are women there. I think the figures that we are referring to are probably the change-over in

terms of those who came in part way through the year and left and those who were appointed in January. I can say that all of my non-execs are on the same,¹¹ those who were all confirmed in January after we went through an open process. So that is six of them, plus the Chair.

Q275 John Thurso: So if I look at his table for 2009–10, this time next year, I will see that they are all on the same: all the non-execs, bar the chairman, are on the same.

Ms Strathie: Yes.

Q276 John Thurso: Turning to the executive remuneration, why is the chief financial officer on 15K more than the chief executive officer?

Ms Strathie: Why is that! Simon?

Mr Bowles: I guess I was recruited from the private sector and I assume that the remuneration was targeted to reflect a private sector salary.

Q277 John Thurso: Just as a matter of interest, you have got half the remuneration reported in the remuneration report but the table on bonuses is actually in the other document. Would it not be helpful, in one of these documents, to have a complete remuneration report, as you might find in a plc set of accounts?

Ms Strathie: Yes.

Q278 John Thurso: Would it not also be helpful, instead of having lots of funny little 5K bands with any one person, to actually just make a straight statement as to what is earned and each component of remuneration? If you are going down the plc route, why do you not just follow the model code?

Ms Strathie: I take your point about transparency and making it very clear. I have covered this in several departments and over several years, and I would prefer just a stark statement of exactly what everybody gets, but I do know of colleagues in other departments who were targeted because they did not get a performance bonus. Therefore, they are identified and targeted as that somehow makes you a poor performer when, actually, we did not have any bonuses this year, and we tried very much to do it in line with the rest of Whitehall in how we protected some people from being identified or attacked wrongly in that way.

Q279 John Thurso: In the table on bonuses, Steve Lammy is 30 to 35; everybody else is either five to ten or ten to 15. Was he spectacularly better than anybody else or were the rest spectacularly worse than he was?

Ms Strathie: I think it is fair to say that there are a number of different contracts and remuneration packages in play, particularly if you were on a fixed-term contract with a particular set of objectives and a reward system that went around that, rather than if, like me, you were a permanent civil servant who

¹¹ *Note by witness:* The amounts reported reflect the various periods of appointment during the year. Two of our Non-Executive Directors receive an additional payment for chairing committees.

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accepted a salary. So we are where we are with the contracts that people have and I think it is important in any of these to say that contracts will be shaped, in any case, without talking about anybody personally as “eligible for a bonus up to, or a non-consolidated award up to”, and, as you will see next year, they are very much reduced.

Q280 John Thurso: Just a final comment, if I may, Chairman. In this new age of utter transparency, it would be helpful at board level in public organisations if one had exactly the same level of detail and transparency as you would find in a plc—I think that is a standard that we should accept—and, as you are one of the first to have a private sector, non-executive chairman, you and he might like to consider that and think about leading the way?

Ms Strathie: We certainly take that on board, but this is not Lesley Strathie Plc, it is HMRC, a department of government, and, equally, we try to operate in a way that makes it easy to look right across Whitehall.

Mr Bowles: Perhaps I can add to that, we operate and we report within a standard model set by the Treasury, so we are not fully our own masters in that matter.

Q281 Chairman: That is something we can pursue with Treasury ministers, but you might like to reflect on the point that has been made.

Ms Strathie: Yes, we absolutely will do.

Q282 Chairman: A couple of points before we finish. You have served the nationwide network of Inland Detection Teams to complement what is being done by the Border Agency. How clear is that division of responsibility between yourselves and the Border Agency?

Ms Strathie: I think it is incredibly clear, because we had about 18 months of shadow working and preparing. I am very clear that I still have policy ownership, and it is for me to set the service levels and the targets, commissioning the physical

detection service at the border for the UKBA. So I still have the enforcement and compliance and the intelligence to stop contraband getting to the border from the other side of the UK border and then I have the inland teams if things manage to get through the border. So the bit that the UK Border Agency is very focused on is that physical detection at the border.

Q283 Chairman: In that respect they are your agency?

Ms Strathie: Yes, they are a delivery partner. They are an agency of the Home Office, but I commission them, as opposed to commissioning anybody else, to deliver that.

Q284 Chairman: But you are not winning on excise fraud, are you? The number of seizures is actually down.

Ms Strathie: I think that is a success. In fact, if you look at what was the biggest cigarette seizure ever in Irish waters this week, you will see that the amount of seizure the other side of the border is in itself a success. We will be publishing figures at PBR which will demonstrate the impact of our strategy in this space.

Q285 Chairman: We are going to leave it there. You have promised us a great number of notes and information. Because we are going to take these points further with ministers, we will need that by 13 November, if you can do that.

Ms Strathie: Could I add one point, before you go, to the committee member who asked me about avoidance. The last public figures we had on this that were robust would demonstrate that we believe around £12 billion has been saved,¹² but we only publish figures when we feel that they are robust.

Chairman: We are going to have to leave it there. Thank you very much.

¹² *Note by witness:* The £12bn referred to relates to the Disclosure of Tax Avoidance Schemes (DOTAS) regime, which was introduced in 2004. HMRC has used information from these disclosures to prevent over £12 billion of avoidance opportunities. Whilst the £12bn figure is frequently referred to, it is not actually published.

Wednesday 11 November 2009

Members present

Mr Michael Fallon, in the Chair

Nick Ainger
Mr Colin Breed
Jim Cousins
Ms Sally Keeble
Mr Andrew Love

John McFall
Mr James Plaskitt
John Thurso
Mr Mark Todd
Sir Peter Viggers

Witnesses: **Sir Nicholas Macpherson**, Permanent Secretary, and **Ms Louise Tulett**, Group Director of Finance and Procurement, HM Treasury, gave evidence.

Q286 Chairman: Sir Nicholas, I welcome you back to the Sub-Committee. Perhaps you would briefly introduce yourself and your colleague for the shorthand writer.

Sir Nicholas Macpherson: I am Nicholas Macpherson, permanent secretary to the Treasury. On my left and your right is Louise Tulett, finance director of HM Treasury.

Q287 Chairman: Today we are to cover the 2008–09 year which is probably one of the toughest that the Treasury has had. Is that right?

Sir Nicholas Macpherson: It is certainly the toughest year in my working life.

Q288 Chairman: You appear to have paid yourself and your seven senior staff bonuses totalling £115,000 for that year.

Sir Nicholas Macpherson: No. Those bonuses were paid in respect of 2007–08. The bonuses in respect of 2008–09 will be published in the next departmental report. In case you are interested, I chose to waive my bonus so my wages will be lower in respect of that year.

Q289 Chairman: Is the position, therefore, that the 2008–09 bonuses have been decided but not yet published?

Sir Nicholas Macpherson: That is correct.

Q290 Chairman: But you expect them generally to be lower than in 2007–08?

Sir Nicholas Macpherson: We have to take into account two things: first, the current pay environment; second, there are people in the Treasury who have given an extraordinary amount of their time in the past year. A number of people have worked almost day in and day out over many weekends. It can be argued that one should look at the outcomes. We have ended up having to bail out banks and GDP is falling. But one has to balance performance against objectives, against commitment and sheer effort.

Q291 Chairman: You have a huge number of measures to stabilise the financial system. Are you able to give the Sub-Committee the total overall cost to the taxpayer of all the financial stability interventions?

Sir Nicholas Macpherson: We can do two things. First, at Budget time we made a fiscal provision of £20 billion to £50 billion. Second, both in these accounts and whenever we have an update in either the spring estimates or main estimates we set out both contingent liabilities, ie a running commentary on the loss on our shareholdings—so far it has been a loss—but also provisions for interventions like the asset protection scheme. Needless to say these numbers will continue to move around a lot. The Treasury is committed to as much transparency as possible on these issues and will continue to report both at PBR but also in future accounts.

Q292 Chairman: Do you expect to recover the sum set aside for these financial stability measures or make a profit from any of them?

Sir Nicholas Macpherson: There must be a good chance. Today I tried to work out the running loss on our shareholdings. I believe that the trough was in January when we made a loss on our shareholdings of £26 billion. By the time of these accounts that number had come down to £17 billion. As of close last night it had reduced to about £9 billion. Indeed, a couple of months ago there was a brief period when we were in profit. I am reasonably confident that we will get a decent return for the taxpayer. The shareholdings are one of a series of interventions, some of which received quite decent fees such as those under the credit guarantee scheme. If those guarantees are not called we shall make quite a nice turn on that intervention. Similarly, RBS is paying reasonable fees for its access to the asset protection scheme. There is huge uncertainty around it. Obviously, if the economy suddenly turned down and there was a double-dip recession things could look quite different, but currently I am cautiously optimistic.

Q293 Chairman: If any of these liabilities are called in—you spoke of the £50 billion—how will they be funded by the Treasury?

Sir Nicholas Macpherson: It would depend on what form they took, but if we suddenly had to indemnify a lender where we had given a guarantee obviously we would have to fund it through conventional borrowing. I am aware that a few weeks ago Robert Steeman of the Debt Management Office was before you. The DMO has been remarkably successful at funding sudden needs.

Q294 Chairman: The simple answer is that you would issue gilts?

Sir Nicholas Macpherson: Yes.

Q295 Mr Plaskitt: I turn to chapter 1 of your report where paragraph 1.5 says that the government has set out plans to deliver a sustained fiscal consolidation once the economy emerges from the downturn. Table 1A shows the impact of those plans which is to halve the PSNB between 2010–11 and 2013–14, yet the only money figure I can see in the report to contribute to that is the £26.5 billion reduction in borrowing mentioned in paragraph 1.13. The reduction of £26.5 billion comes nowhere near amounting to a halving of the PSNB, so which bits are missing?

Sir Nicholas Macpherson: That is a good question. The £26 billion to which you refer represents measures that reduce the deficit and they are primarily but not wholly tax. One reason the deficit will reduce over the period is that the economy is set to recover and revenues will begin to grow and for a given level of public spending that growth slowly reduces the level of borrowing. The reason the government has had to take measures is that it cannot rely totally on a normal cycle to close the gap. That is why measures were set out in the Budget both on the tax side but also in terms of setting quite tight spending plans in future.

Q296 Mr Plaskitt: Referring to table 1A which shows PSNB falling from 11.9% to 5.5% of GDP, is that heavily contingent on hitting the projected GDP growth figures for the economy? You seem to be saying that a return to growth is the biggest contribution to delivering the corrections to the fiscal balances.

Sir Nicholas Macpherson: At Budget time this year borrowing was set to be 12.4% of GDP; it falls to 5.5% in 2013–14. That is a reduction in the deficit of £78 billion from £175 billion to £97 billion. The economic growth element is only a component of that; it could be about one half. I would need to come back to you to confirm the assumption on that, but my view is that broadly you can rely on recovery to get you about half way and measures for the rest of it.¹

Q297 Mr Plaskitt: You have acknowledged that the forecast is uncertain because in response to the Chairman's question you entertained the possibility of a double-dip recession?

Sir Nicholas Macpherson: Just as you can have very rapid growth. I believe today's forecast by the Bank of England points to reasonably rapid growth, but clearly it is a factor.

Q298 Mr Plaskitt: Are you saying that if you hit 5.5% of GDP for net borrowing in 2013–14 that is a condition you would describe as sustainable fiscal consolidation?

Sir Nicholas Macpherson: I think it is a good start at a reasonably rapid pace, but no one is in any doubt that further consolidation is needed if we want to get borrowing down to a level that past governments of whatever persuasion have regarded as prudent.

Q299 Mr Todd: I want to ask about two different areas. First, can you outline how your relationship with UKFI operates? You will be aware that recently it appeared before us. The impression one had was that a strategic direction had been given by the Treasury with tactical day-to-day relationships with the banks being carried out by them. Do you want to expand on how you see this working?

Sir Nicholas Macpherson: My colleague can put me right because she is on the board of UKFI. UKFI works at arm's length from the Treasury, but there are a number of instruments designed to ensure that it has a very clear framework. It has to agree an investment mandate and business plan with the Treasury. If it is to do anything serious like selling shares in the two major banks that must be cleared with the Chancellor of the Exchequer. I have just been involved in appointing the new chief executive. I was only one member of the panel which was chaired by David Cooksey. Appointments to the board must be approved by the Treasury.

Q300 Mr Todd: I want to illustrate it by putting a question that I put to them. There has been a substantial exercise to look at the balance sheets of the two institutions we now largely control and is based on the insurance schemes we have devised for them, one of which has been taken up and the other not. I wondered what level of information had been provided to UKFI and what had been found and I was told none at all. First, is that right? Obviously, in part it is not right if Ms Tulett is on the board and presumably has been party to some extent to the knowledge that has been gained.

Sir Nicholas Macpherson: UKFI operates within the terms of its mandate. The asset protection scheme is something that the Treasury took forward on the basis of substantial professional advice from various sources and it also consulted UKFI on some of the implications for shareholders. We have a regular dialogue with UKFI.

Ms Tulett: The level of detail that I see coming forward to the UKFI board would not indicate a high level of information or cross-over. Everybody is conscious of the controls to protect information to allow only legitimate shareholder information to be known by UKFI and with the asset protection scheme, which is now to be administered by an arm's length body in the opposite direction, there is clear water between the two. In these early days it is quite difficult to get the demarcation right, but I think we are getting there.

Q301 Mr Todd: And also to define the principles of that demarcation?

Ms Tulett: Yes.

¹ Ev 105

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Q302 Mr Todd: To give a concrete example, most major shareholders would want to know quite a lot of what had been discovered about the asset base of a company where a very substantial part of it was being valued down. Where do you draw a line of principle in that regard?

Ms Tulett: I do not quite know how we have articulated that line of principle being drawn, but I think the professionals who manage the data and knowledge around the asset protection scheme and the legitimate things that UKFI should know if it is to execute the responsibilities of its shareholding are things that professionals are used to doing.

Q303 Mr Todd: It comes across as being well intentioned but vague.

Sir Nicholas Macpherson: I give a concrete example. I was heavily involved in the recent announcements. You will recall that originally Lloyds signed up to the asset protection scheme and in the course of the summer its management began to take the view that there might be a different way forward. We consulted UKFI from the shareholders' perspective on whether to continue in the asset protection scheme or to get out of it would be better for the share price. In doing that UKFI had to have a very strong understanding about the implications for Lloyds. They gave us advice which was consistent—without giving away confidences—with the eventual outcome. The Treasury has a very strong shareholder interest but it is not simply that; we have an interest in financial stability.

Q304 Mr Todd: That is why in concrete terms with a due diligence exercise over RBS which has been conducted I am slightly surprised to find that no knowledge has been exchanged between UKFI and the Treasury; indeed, I am not entirely clear how the Treasury has used the information that has been forthcoming.

Sir Nicholas Macpherson: I would be happy to provide a note on precisely the way we have interacted with UKFI on this.² I have spoken regularly to John Kingman over the past few months. There are mechanisms whereby we consult. The critical thing on these big interventions is that decisions need to be taken not just from a fiscal perspective but from the perspective of financial stability and only the Treasury can do that.

Q305 Mr Todd: I was interested in your Objective 1. I turn to pages 41 and 42 where you talk of the professionalisation of the procurement function in government. Have you examined research—I have in mind particularly the procurement of ICT projects which tends to dominate at least the political horizon—which shows that we do rather worse in this than, say, the Netherlands which is held up as an example of a rather smarter procurement process?

Sir Nicholas Macpherson: Clearly, on procurement we can learn from other countries; we can learn from the private sector, although the latter also has

problems with procuring ICT. The critical point is that the OGC under the leadership of Nigel Smith, who has real and deep experience in this area, is committed to driving further improvements. If the adoption of the Dutch approach is the right way forward I am quite certain that they will consider that.

Mr Todd: To be really concrete, I did not spot in the document—it may be due to my speed reading—a benchmarking process in which you examined procurement practice against best practice elsewhere. Can I commend that to you? This looked like a rather internalised way to manage improvements in procurement, if I may say so.

Chairman: We give you 10 minutes to come up with an answer to that question. We shall suspend the hearing.

The Committee suspended from 4.35 pm to 4.45 pm for a division in the House

Q306 Chairman: And you may answer.

Sir Nicholas Macpherson: I have just managed to speak to the chief executive who was getting off a train at Euston. We do not do any formal benchmarking against other countries. Obviously, we have quite a strong dialogue with other procurement authorities and seek to learn from one another. Occasionally, they learn from us. For example, 28 countries have adopted our approach to the gateway process. Your point is a good one and we may want to follow it up.³

Q307 Chairman: What hard evidence does the Treasury have that quantitative easing is working?

Sir Nicholas Macpherson: It has some evidence. This is a very difficult issue to assess because one is assessing against a counterfactual that none of us knows. All one can do is look at things like asset prices, the gilts market and long-term yields and whether lending is increasing. We can also look at the wider corporate bond market. There is evidence. The governor will be far more eloquent on this than I am, but quantitative easing is a journey into the unknown. We do not understand every aspect of it. I am sure that it will keep academics busy for many years to come.

Q308 Chairman: In box 2B of your report you say that the chancellor authorised up to £150 billion of purchases of which £50 billion should be used to purchase private sector assets, but according to the Bank of England website the actual amount of such assets is only about £2 billion. Can you elucidate?

Sir Nicholas Macpherson: How the bank operationalise quantitative easing is a matter for the executive of the Bank of England. The bank would argue that its interventions in the corporate market have been successful and that the corporate bond market is now functioning much better—that is down in part to QE but also wider developments—

² Ev 104

³ Ev 109

and that therefore further purchases in that area are unnecessary. I do not want to put words into their mouth.

Q309 Chairman: Let us hear it from the mouth of the Treasury. The chancellor has authorised this total of purchases and it says clearly on page 57 that up to £50 billion should be used to purchase private sector assets but only £2 billion worth of assets have been bought, so is it not right that they are adopting a very different portfolio profile from the one the chancellor wanted?

Sir Nicholas Macpherson: I think we wanted to enable them to buy private sector assets if they wanted to. Our view at that time certainly based on the experience of other countries like the United States was that this could be a fruitful line of intervention.

Q310 Chairman: So, is this sentence “up to £50 billion should be used to purchase private sector assets” just a suggestion?

Sir Nicholas Macpherson: It was a suggestion and it also pre-dates the pure quantitative easing process. There was an intermediate phase at the beginning of the year in which we authorised the bank to buy private assets funded through the issue of Treasury bills rather than central bank money.

Q311 Chairman: Is it right that it is no longer quite as operative as it was?

Sir Nicholas Macpherson: I think you should ask the Bank of England about it.

Q312 Chairman: But it is your policy.

Sir Nicholas Macpherson: The Bank of England is independent in the conduct of monetary policy and this is now a monetary policy issue; at the turn of the year it was not because it was not being funded in the same way.

Q313 John Thurso: I should like to look at the outcomes in DSO 1. Referring to indicator outcome 1(a) which is about meeting the fiscal rules, during the course of the year you changed that to a new statement which seems to me to be rather full of motherhood and apple pie but not a lot of meaning. Was there any real point in having it?

Sir Nicholas Macpherson: It is always very important to have some sort of objective or rule to guide fiscal policy. I can remember that under successive governments the objective has changed from time to time, but in terms of credibility one needs something that guides policy. Given the events of last year I would not attach so much importance to the rule as to the actions of the government. There comes a point when you can announce whatever rule you like. What gives you credibility fiscally is what you do.

Q314 John Thurso: That is the point I am getting at. Would it not be worth saying in the current circumstance that rules are pointless and we should watch your actions?

Sir Nicholas Macpherson: There was a debate about whether we should just suspend the rules. Our view and that of the government as a whole was that to suspend the rules would create more uncertainty than if at least we made clear that there was some objective that informed policy and then we would set policy consistent with that objective. I do not believe this rule will be a permanent one.

Q315 John Thurso: It is not really a rule but a statement of hope?

Sir Nicholas Macpherson: It is a statement.

Q316 John Thurso: It is a mission statement.

Sir Nicholas Macpherson: What matters is the policy but since then the government has announced it will legislate the decision to halve the deficit over four years and I suppose that at that point it becomes a rather harder rule.

Q317 John Thurso: Will this be replaced in the near future by a rule against which measurement can be made? You cannot measure anything in that other than, “We are doing better”?

Sir Nicholas Macpherson: I think you can, but if the government is to legislate a hard budget constraint, which is my understanding of the announcements in September and October, that will provide a harder edge and an opportunity for both the public and parliament to hold the government to account on whether it is hitting the target.

Q318 John Thurso: I turn to outcome 1(b) which is to ensure that the tax yield is sustainable and the risks managed. What are you doing to sustain the tax yield?

Sir Nicholas Macpherson: Two things. First, Revenue and Customs are working very hard to focus all their activity to maximise the tax yield for a given set of policies, but especially in the current environment we also must look across the tax policy spectrum to see where the system needs to be improved to maximise revenue.

Q319 John Thurso: What are the risks that you are managing?

Sir Nicholas Macpherson: The immediate risks arise from the downturn which has hit revenues very badly, perhaps even more than expected. With the benefit of hindsight, some taxes are more geared to both the financial service sector and housing and therefore revenues have fallen far more than GDP. That will provide important lessons for the future.

Q320 John Thurso: So, one of the risks you are managing for the future is not to rely on the financial sector or the housing market and to look for other things to tax?

Sir Nicholas Macpherson: The history of tax collecting is that one must always keep an eye on new sources of revenue. If one goes back over the past 300 or 400 years some taxes last a long time like income tax and some excise duties but an awful lot of other taxes come and go. One must get tax where one can find it.

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Q321 Sir Peter Viggers: Looking at departmental strategic objective 1 d(i), which is professionalising and modernising the finance function in government, you claim strong progress, but I see that on page 39 of your report that only 22% of all bodies regularly met all agreed standards for timeliness and accuracy. Are the targets wrong? How can you claim strong progress when only 22% meet the standard?

Sir Nicholas Macpherson: These targets are very new and are part of raising the bar in terms of departmental performance. This is particularly about the quality of monthly reporting of spending to the Treasury. All departments are on an upward trajectory, but what that statistic reveals is that there is a lot more to be done.

Q322 Sir Peter Viggers: What can you do to improve their performance?

Sir Nicholas Macpherson: You can do quite a lot. Part of it is moral suasion. There is a group of finance directors, of which no doubt Louise is a member. People do not like league tables or being named and shamed, especially by their colleagues, so one can create quite a lot of peer pressure. There are also more direct mechanisms whereby if a finance function in a department is weak both through the Cabinet Office's capability review programme but also in terms of my relationship with permanent secretaries one can draw attention to that weakness and that something needs to be done about it pronto.

Q323 Sir Peter Viggers: It sounds a little compellable. Does it really matter and, if so, can you not simply tell them?

Sir Nicholas Macpherson: I think people are receptive to messages on this point. There has been a big step forward on professionalisation. Only six years ago when I used to appear before this Sub-Committee the finance director sitting next to me was not a professional. We have professionals in place. The quality of accounts and financial management and data is improving, but in some areas it starts from a low base. For example, the relationship between resources and outputs and outcomes has tended to lag behind the private sector partly because getting a measure on somebody's objectives is quite difficult. But John Thompson, head of profession, myself and Andrew Hudson who runs the directorate in the Treasury are seriously committed to making progress.

Q324 Sir Peter Viggers: Would you get a better idea of government reporting performance if you expanded your measure of timeliness and quality of resource accounts to include arm's length bodies such as the Royal Mint?

Sir Nicholas Macpherson: Getting arm's length bodies more closely involved in the process is critical. One comes back to the clear line of sight point and what determines the departmental boundary. I think this is a real priority.

Q325 Sir Peter Viggers: Turning to DSO outcome 2(a), supporting low inflation, your overall outcome assessment is met ongoing and the target is 2% with a margin of 1% but average CPI was consistently above 3% during 2008–09, peaking at 4.8% in the fourth quarter of 2008. How can you claim that the target was met ongoing?

Sir Nicholas Macpherson: Because inflation came back rapidly to within the range. Looking over any reasonable length of time inflation out-turns have been very close to target. There will always be times when it goes over the top of the limit and possibly beneath it, but I do not think that failing to hit the target for a few months means one is not meeting one's objectives. What matters is what the average inflation rate is over a long period and it is very close to the 2% target; indeed, it is threatening to go out at the bottom, but I think that inflation will be rising again soon with the VAT increase coming up. I am reasonably confident that the bank will continue to hit the target.

Q326 Jim Cousins: Referring to child poverty, do you think you will meet the targets?

Sir Nicholas Macpherson: It will be very hard work. Over the past two years of published data we have not made as much progress as we would have liked. A lot of resources have been put into tax and benefits to support poor families but progress does not seem to have been reflected in the statistics. It does not mean you give up; if anything, you need to redouble your efforts, but we shall be hard pressed to halve child poverty by 2010 given the recent trajectory.

Q327 Jim Cousins: Can you supply the Committee with the current take-up rates as you see them for the child tax credit and working tax credit? Can you also supply the Committee with information because there appears to have been a growth of casual and part-time jobs and that does not necessarily trigger ineligibility for working tax credit given the rules that apply? It would be quite worrying if sections of the labour market which are expanding at the present time, particularly for women, did not qualify people for the working tax credit.

Sir Nicholas Macpherson: I am aware that HMRC publishes data in its annual report, but I would be happy to provide the Sub-Committee with a note.⁴

Q328 Jim Cousins: What was announced in the Budget in 2007 was that another half a million children would be taken out of poverty. Are you now uncertain about whether you will meet that target?

Sir Nicholas Macpherson: The measures we have taken in recent Budgets will ensure that child poverty is 500,000 lower than it would otherwise have been. The worry is that there are trends at work in the economy which mean one is running quite hard sometimes to stand still. I am optimistic that those measures will have a positive impact on people's lives. What I am less confident about is that they will translate on a one-to-one basis in the child poverty statistics.

⁴ Ev 106

Q329 Jim Cousins: You have reminded us of the important gloss that the target is relative; it is half a million less not of the fixed figure but where it would have been. It would be interesting to measure it and obtain your analysis of where the figure would have been and why; that is, the moving target which is the basis of your comparison.

Sir Nicholas Macpherson: This is a very complex area and analysing it is difficult, but I would be very happy for the Treasury to give you a note on it.

Q330 Jim Cousins: It is a little disappointing that pensioners are not mentioned at all under outcome 2(c). Perhaps I need to place on record that although I am of pensionable age I do not claim the state pension. Therefore, I am not asking about something of which I am a direct, personal beneficiary at the present time. I was quite disturbed to see recently that amongst the over 65s there are three million pensioners who do not claim the enhanced tax relief who could so and 2.5 million pensioners pay tax on their savings, because tax is deducted at source—it is a withholding tax on savings—when they should be receiving those savings tax free. What are the government doing to ensure that pensioners claim the much larger tax relief to which the over 65s are entitled?

Sir Nicholas Macpherson: First, I am sorry that this section does not contain a reference to pensioners. We will endeavour to do better next year. Second, I am aware of the problems of take up in all sorts of areas relating to old people. I do not have before me information about what HMRC is doing. I am pretty sure that it has run campaigns to ensure that old people who do not pay tax reclaim what they are entitled to. Again, I would be happy to come back to you on that.

Q331 Jim Cousins: There is a growing body of evidence to suggest that pensioners who do not take up the enhanced tax relief and get their savings tax free as they should are very often women who live on their own. The Leader of the House may be reassured to know that sometimes the old boys care very strongly about the old girls. I am concerned that it is particularly women who lose out by not claiming their entitlements. What measure are you taking in that regard?

Sir Nicholas Macpherson: I agree with you on that. Historically, it is that group which is most likely to be living in poverty. I am aware that the Department for Work and Pensions has done a lot of work to promote the take up of pension credits.

Q332 Jim Cousins: I am talking here about tax which is your direct responsibility.

Sir Nicholas Macpherson: Tax policy is indeed my responsibility. I am not trying to get out of responsibility for this in any way. The implementation of that policy is a matter for Revenue and Customs, but I shall find out where HMRC is on this. Tomorrow I am to see its Chief Executive, Lesley Strathie, and I will come back to you.

Q333 Ms Keeble: Dealing with child poverty, one of the key measures has just come in, namely the changing rule about housing benefit.

Sir Nicholas Macpherson: Yes.

Q334 Ms Keeble: Do you know how that is progressing? There were real issues about whether local authorities would be able to implement it.

Sir Nicholas Macpherson: To the best of my knowledge, the implementation is working, but again I shall be happy to give you a note on that. I am sorry that I am promising to send in so many notes.⁵

Q335 Ms Keeble: How do you know it is progressing properly? Do you liaise with DCLG on it?

Sir Nicholas Macpherson: We have a mechanism for ensuring that the Treasury, Work and Pensions, CLG and the Department for Children work closely together. There is a structure which supports the PSA process. I assume that if there was a serious problem with it I would be aware of it.

Q336 Ms Keeble: One impact is that you give more money to families on housing benefit; the other is that you take money away from those who are on rent allowance. Have you seen what the impact will be of taking money away from people on rent allowance at the same time that you give money to people on housing benefit?

Sir Nicholas Macpherson: We try to model these things to get a decent distributional analysis to inform policy, so those sorts of calculations will be done.

Q337 Ms Keeble: These are exactly the same families; it is just that some are in council and some are in private tenancies. The former get more help with their rent and the latter have money taken away from them.

Sir Nicholas Macpherson: Certainly, the impact of some of these policies can be consistent with what you say. One of the problems is that historically rent allowances in particular have supported rents which are far higher than in the local authority sector. People have always tried to reform housing benefit which is a very difficult matter.

Q338 Ms Keeble: I am not asking questions about the reform of housing benefit but the amount of disposable income that families have after housing costs. With housing benefit it will be more because they can keep more but with rent allowance it is taken away because any money that is left over is removed from them. I want to know about the income of poor households after housing costs. Are you measuring it and, if so, how?

Sir Nicholas Macpherson: This would be measured both at the time the policy is being modelled but also when you get the child poverty statistics. The child poverty statistics are done both before and after housing costs.

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Q339 Ms Keeble: Can we have the figures from your modelling about how many families got how much money through the changes in housing benefit and how many families with children lost how much money as a result of the rent allowance claim and compare them with the results, presumably after three months, so we know what has happened to household incomes?

Sir Nicholas Macpherson: I can give you that information assuming we have it. It is the Department for Work and Pensions that is responsible for housing benefit.

Q340 Ms Keeble: But you have the lead on child poverty.

Sir Nicholas Macpherson: Of course we do and I do not seek to duck responsibility for that.

Q341 Ms Keeble: You are responsible for the 21 measures dealing with material deprivation. Have you costed them? Do you have any legislative measures in place to enforce the standards in the material deprivation indicators?

Sir Nicholas Macpherson: Our estimates of material deprivation do not hinge on what is in the legislation but on the real life experience of individuals.

Q342 Ms Keeble: But do you have any measures to get families out of material deprivation?

Sir Nicholas Macpherson: Yes. Clearly, the government seeks to intervene on quite a wide front.

Q343 Ms Keeble: Can we take one of them: the bedroom standard? That is the only indicator that deals specifically with housing. What bit of legislation do you have in place, or what intervention has the government made, to enforce a bedroom standard?

Sir Nicholas Macpherson: I do not know the answer to that question. There will be people who do; it is just that there are limits to how much the Treasury can do in that regard.

Q344 Ms Keeble: I am a former housing minister. The bedroom standard is that each child over 10 can share a bedroom only with another child of the same gender. The legal standard is quite different from that; it is that all rooms over a certain size in the house count as bedrooms and there is no issue about gender. For children under 10 there can be four to a room. Why have you not aligned your indicators for material deprivation with the reality of what the government is prepared to fund?

Sir Nicholas Macpherson: No doubt that was an issue which your department would consider.

Q345 Ms Keeble: The material deprivation indicators are the ones for which your department is responsible; you have the lead responsibility for it, not any other department.

Sir Nicholas Macpherson: We do have the lead responsibility for reporting on this and we chair the interdepartmental group which takes it forward and we take responsibility for it. Equally, responsibility for individual sub-components of what you

acknowledge is an extremely complex basket of indicators would be taken forward by relevant departments.

Q346 Ms Keeble: Referring to child care, I think it is acknowledged that a key way out of poverty is work. I do not believe we have yet had information about the take-up of the child care element of working tax credit. Can you say what is happening there?

Sir Nicholas Macpherson: I do not have in front of me the current figures for take up. The trend has been a rising one. I was responsible for this policy area in the late 1990s. I believe that in those days about 15,000 families took up the child care element within family credit and now the figure is several hundred thousand, so there has been substantive progress.

Q347 Ms Keeble: Can we have the figures? The information we had at one stage was that it had stalled. Since it is topical can you say how much you will save by taking away the tax relief on child care vouchers?

Sir Nicholas Macpherson: I do not know the answer to that question.

Q348 Ms Keeble: What will the net saving be if they switch to the child care element of the tax credit?

Sir Nicholas Macpherson: I will have to add that to the ever-increasing list of additional information.

Q349 Ms Keeble: How can you deliver on child poverty if you do not have the tools to measure some of the key factors?

Sir Nicholas Macpherson: Having information is critical. I believe we do have information in relation to a number of these indicators. You have also drawn attention to issues like relevant legal standards. This is a very complex area. We have at our disposal quite a lot of instruments but there is a whole series of other areas where progress is more difficult.

Q350 Chairman: You are to examine Ms Keeble's questions in more detail and come back to us with all the information you have that may enable you to answer them?

Sir Nicholas Macpherson: Yes.⁶

Q351 John McFall: What is the present shortfall in the government's target to halve child poverty by 2010?

Sir Nicholas Macpherson: All I can tell you is that in the past couple of years the child poverty figures have remained unchanged.

Q352 John McFall: It is still 3.4 billion?

Sir Nicholas Macpherson: It is on page 79 of the document.

Q353 Mr Love: In the context of the comment you made right at the beginning that in your time at the Treasury this was the hardest year you could

⁶ Ev 106

remember are you still confident you can deliver the £35 million of efficiency savings outlined in your annual report?

Sir Nicholas Macpherson: Yes.

Q354 Mr Love: Even in the context where it appears that very little of it will be delivered by reductions in staff?

Sir Nicholas Macpherson: That is correct. Louise may want to explain how we are to deliver it.

Q355 Mr Love: Before she does so, I read through the Treasury document which says that for the core Treasury you will deliver the savings by “rationalising its organisational structure to exploit synergies across business areas”. I do not understand that, but can you tell me how that can deliver the savings you outline?

Ms Tulett: Obviously, the efficiency is not just about making the savings; it is also about either maintaining outputs or improving outputs for the same inputs. The reason we can achieve efficiency by redeploying staff is that provided we can improve outputs by redistributing the same staff to a higher level of productivity that is an efficiency gain, even though the expenditure stays static, so it is important to understand the relationship between them. The paragraph to which you have just referred is part of the description we have given in our VfM Delivery Agreement published on our website in July about how we are to achieve savings. We have already rationalised some areas. We are trying to maintain a very lean governance structure and are currently going through a governance review to make sure we are effective in not allowing overheads to creep up. We are quite diligent when vacancies arise to assess whether we need to replace somebody or remove that post. Having removed the post we may wish to redeploy the resources to create another post somewhere elsewhere. You will note that under financial services stability we moved quite a lot of people into international finance.

Q356 Mr Love: All of that sounds fine but you are talking about increasing productivity at a time when according to all outside opinion your workload has gone up substantially.

Ms Tulett: Yes.

Q357 Mr Love: As I understand it, all of this must be a net cash saving. That is a major task, is it not?

Ms Tulett: It is.

Q358 Mr Love: To do it without the increased workload would be a major task. I question whether you can gain that productivity improvement against the backdrop of an enormous workload. Is it seriously considered that you can deliver this?

Ms Tulett: It is a major task and it is one that we are on track to deliver. The second half of the programme to deliver will clearly be harder than the first half because one picks the low-hanging fruit first. Our Autumn Performance report should

be published before recess in December and the figure that we put into it will be audited to ensure we deliver sustainable savings and efficiency gains. I do not belittle the size of the task, but in another way in an organisation that has quite a lot of innovation and new areas of work it makes us examine what is lower priority and what one can stop doing. An organisation that goes through the massive change that the Treasury has experienced sometimes sets the right culture to be exploratory in how it can do this.

Q359 Mr Love: Sir Nicholas, have you had any conversations with the Chancellor along the lines that this is a relatively small amount of money in terms of the overall efficiency savings being demanded across government and to continue this may impair the ability of Treasury staff to respond to the many demands that the Chancellor places upon them?

Sir Nicholas Macpherson: The Chancellor and I have had a number of conversations about how we resource ourselves through the crisis and the Committee was quite helpful and supportive in suggesting that we needed more resources. We have taken in more resources and on the financial stability side in particular the Treasury is much bigger; it has grown in size during this period. All I would say is that it has been helpful to us to have the resources to deal with what we have had to do, but it should not mean that we give up on the efficiency agenda. Things like getting better use of our accommodation, rationalising our estate and thinking through how our corporate services work remain really important. In a crisis one needs to bring in more resources. The Treasury has had to operate on a far wider front and what it has done over the past year in that respect has been very sensible.

Q360 Mr Love: Whilst I accept that you can continue to look to make efficiency savings from the areas you have talked about—the estate and other functions—the obvious question that arises from it is: is it not important for you, the government and country that you do nothing to impair the ability to continue to respond to what clearly everyone thinks is a continuing major economic dislocation? Therefore, sitting here before the Sub-Committee today are you confident that the Treasury can continue to do the job it has been doing for the past year even with its efficiency programme?

Sir Nicholas Macpherson: I am confident that £35 million is deliverable. Ultimately, the question is that if you keep seeking to impose very demanding efficiency targets there are risks. My personal view is that there is a certain level of Treasury staffing below which you may have a problem. You need a certain number of people to run a decent, functioning finance ministry. In my time at the Treasury the number of people within it has tended to vary between about 900 and 1,300. I would become quite worried if we ended up at, say, 750.

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Q361 Mr Love: But a lot of the reductions were made in recent years. You started out top heavy and you have made reductions. You are now being asked to continue to make those reductions against the present backdrop. Does that not raise some concerns about whether you can continue?

Sir Nicholas Macpherson: We have to manage the risks. We have expanded recently to deal with specific challenges, but with the end of the negotiations with RBS over the asset protection scheme at a stroke quite a lot of resources will be released. What I am keen to avoid is the Treasury becoming a flabby organisation. The Treasury is at its best when it is quite small and focused, but clearly on the financial stability side for a few years yet we will need a lot more people than we had five years ago.

Q362 Nick Ainger: I find it difficult to resolve two positions. I refer to the figures on pages 87 and 88 which show a significant increase in staffing. You go on to say that in key positions you have recruited a second permanent secretary, a new managing director, two additional directors working on financial stability and a new director of corporate services. In addition the department has recruited a new position of director of communications strategy supported by a new economic briefing unit. An awful lot of staff at senior level are being appointed. I do not suggest they are not needed, but overall my calculation is that this year an extra 250 staff are being recruited, both permanent and casual, and your predictions are that these levels of staffing will continue right the way through to March 2011. As staffing is presumably your main expenditure how on earth can you say that you will meet the cash-releasing efficiency saving of £35 million?

Sir Nicholas Macpherson: The savings are cash-releasing but some of them will have to be reallocated within the organisation.

Ms Tulett: We had a baseline in our CSR settlement with which the Sub-Committee will be familiar. Sir Nicholas and the spending team had discussions with the Chancellor. We have temporarily had access to an extra £20 million EYF to fund those areas that required it, so the £35 million efficiency comes from the core Treasury which we have bedded into the CSR 2007 settlement. The additional £20 million is what finances some of the increase that you see now, but because we hope it is not something that we have to sustain long term we are currently accessing it from the EYF and when we have the next spending review clearly we shall have to look at the baseline.

Q363 Nick Ainger: But the figures on page 87 indicate that from March 2008 to March 2011 in virtually all the departments, but certainly in the core Treasury group, there are very significant increases in staffing. That occurs in exactly the same period when you are supposed to be delivering the £35 million cash-releasing efficiency programme. It just does not add up.

Ms Tulett: The 107 kick-up from 1,136 to 1,243 was the result of our having to fill vacancies that I believe we discussed with the Sub-Committee last time. Vacancies do not score towards our efficiency, so that was money already in our baseline. When we had to re-deploy people rapidly to the front line to deal with the financial services we then in slower time backfilled them. Therefore, the net increase that represents the marginal effect which would be funded from the additional £20 million EYF is the second year figure of 143. The first year kick-up of 107 got us back to the 31 March 2007 level. I know that in previous hearings we had a discussion about the fact we had dipped and were running with a high vacancy rate.

Q364 Nick Ainger: Quite frankly, I still do not see how the numbers add up. Given the number of people and the grades at which you are recruiting I do not see how the £35 million can be delivered. I understand why perhaps it should not be delivered, which was the point Mr Love made, but you are still pursuing it and things have moved on. Your department has come under enormous pressure and has responded extremely well. Surely, you should be saying that you cannot do this; it is not deliverable?

Sir Nicholas Macpherson: I distinguish how much money the Treasury will spend from the number employed over this period. Clearly, we are spending more and are employing more people. Cash-releasing efficiency saving reflects things like how we exploit the building and much of it will help fund the Treasury rather than go back to the Exchequer. It is really a cash-releasing efficiency saving that supports the level of activity in which the Treasury is engaged rather than one that just represents a cut in our budget.

Q365 Nick Ainger: We shall see what happens in the next annual report. To move on, the staff surveys within the Treasury indicate some very positive things and I am sure that in part that is to do with all the recruitment that is going on rather than the shedding of staff. As you are probably aware, a couple of weeks ago we had before us HMRC where it is not the same picture. I do not know whether you have read the transcript or seen the staff survey within HMRC. When asked whether staff felt that change was well managed within HMRC 11% were positive and 70% were negative; when asked whether when changes were made they were usually for the better 9% agreed and 67% disagreed; when asked whether on the whole HMRC was well managed 11% agreed and 64% disagreed; and when asked whether overall people had confidence in senior civil servants and senior management 11% agreed and 60% disagreed. Lesley Strathie recognises the very serious position she has inherited. HMRC is, if you like, your military wing; you need them to act effectively particularly now in ensuring that you get in every bit of tax to which the Treasury is entitled. What will you do? How can you, who appear to be able

to deliver good staff morale within your core departments, translate that into a massive improvement in HMRC?

Sir Nicholas Macpherson: The Treasury and HMRC are very different organisations. I wish I could say that morale is high in the Treasury because of something I am doing. I think it reflects a far wider range of factors. We are small and are in one location. We have a relatively senior staff balance in our organisation, whereas HMRC is 80 times bigger than the Treasury and has far more junior grades. The Treasury has very high staff turnover; HMRC has extraordinary low staff turnover. It has had quite ambitious efficiency savings which genuinely have been driven out. It is important that the Treasury understands HMRC; it has a huge responsibility in ensuring that it is adequately resourced to do the job. There is now a greater dialogue between the Treasury's board and that of HMRC. We met each other only the other day. We have big obligations in terms of the policy design of a tax system which is manageable from their point of view. They start from a very low base. I have been very impressed by Lesley Strathie's approach to the organisation. I have met people who work in HMRC who are pleased that they have someone running it who really understands what it is like to work in a large organisation, because she worked her way up from the bottom in the employment service. We want to support HMRC and I hope it will get better results.

Q366 Nick Ainger: Members of the PCS trade union have told me that at this difficult time they would like to see the same level of investment going into their organisation as has gone into the Treasury's, but clearly the reverse has happened. We want to drive efficiencies at this time but they believe that it may affect their tax take. Have you looked at that in any way?

Sir Nicholas Macpherson: We have continuing close dialogue with HMRC about this because it is important that it is resourced to do the job. The Treasury has had a bit more resource, but in the general run of things that would not make a huge amount of difference to HMRC because it is just a far bigger organisation. Grade for grade, those who work in HMRC are paid more than people who work in the Treasury and it is of interest that that does not seem to impact on the morale of the two organisations.

Q367 John Thurso: You asked all government departments to restate their 2008–09 accounts on an IFRS basis including the opening balance sheet by 10 December 2009. How many made it?

Ms Tulett: Forty-one out of 43.

Q368 John Thurso: What about the Treasury itself? What is the impact of IFRS on your own resource accounts?

Ms Tulett: Quite considerable, but most of that came about through FRS which was something we had to implement in the set of accounts that you have in front of you. The step change between

IFRS and FRS is not a major one for us. We have submitted our return which is currently being audited by the NAO.

Q369 John Thurso: Does the move to IFRS mean that more PFIs will appear on the balance sheet? If so, what will that do to the net debt figure?

Ms Tulett: I do not know the answer across the whole of government, but for the Treasury the answer is that it will not because our existing PFI deal has been on our balance sheet since the day it went operational. I am afraid I do not have available the information across government.

Sir Nicholas Macpherson: My recollection is that inevitably it will result in more PFI deals being on the balance sheet, but increasingly large amounts of them are on the balance sheet anyway.

Q370 John Thurso: Do you still intend to publish whole government accounts for 2009–10?

Sir Nicholas Macpherson: Yes, we do.

Q371 John Thurso: Do you intend to include in those accounts the investments in the part-nationalised banks?

Ms Tulett: No, we do not. We have taken the policy decision not to do that, in the same way we do not consolidate them within the annual report and accounts.

Q372 John Thurso: They will remain off-balance sheet items?

Ms Tulett: They will remain out of WGA but obviously they will continue to produce their own reports.

Q373 John Thurso: It will be the whole of government accounts less the banks' accounts?

Ms Tulett: We are not consolidating them.

Q374 John Thurso: How do you account for the money that you have put into them? If you were doing this in a normal institution you would either have it as an historic cost or would mark it to market or whatever. Will you show it in your balance sheet?

Ms Tulett: Yes.

Q375 John Thurso: Therefore, you will show it as a separate entity at cost?

Ms Tulett: No; we show it as mark to market.

Q376 John Thurso: You record the loss at the balance sheet date?

Ms Tulett: Yes.

Q377 Chairman: Page 100 shows that last year the number of MPs' letters answered in 15 days fell quite dramatically below your 80% target to 60%. At the same time you have set up a Treasury twitter channel. Do you have your priorities right? Why are you not answering our letters?

Sir Nicholas Macpherson: Earlier this year we were inundated with letters and I think that by March we had a backlog of about 5,000 letters. We

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recognised there was a problem and put a huge amount of resource into dealing with letters over the summer. I think we now have a backlog of about 100. I have sent a letter to a number of MPs to apologise for the delay; I apologise once again, but in the absence of a further crisis in the banks I am confident that we shall be back on track. Even if we answered every letter on time for the rest of this year we will still end up with something like 55% or 60% of letters being replied to within target but I am very confident that we shall do better next year.

Q378 Ms Keeble: I was dismayed by the lack of information about what is happening on child poverty and the lack of measures. I question the seriousness of the Treasury in tackling child poverty.

Sir Nicholas Macpherson: I should like to reassure you that we take it very seriously. The annual report at 260-odd pages is already very long. There is a publication every year by the DWP that goes into huge detail.

Q379 Ms Keeble: But you are responsible for the delivery.

Sir Nicholas Macpherson: We are responsible for reporting against the target and we chair the interdepartmental group which takes work forward on this. I take it very seriously, which is one reason why recently I announced I would move someone at very senior level, Mark Neale, to work full time on the child poverty agenda over the next few months. We need to look at child poverty not just from the point of view of income but in order to re-energise our approach to public services and how we work with different tiers of government, in particular local authorities, to promote the child poverty agenda.

Q380 Ms Keeble: If you look at the numbers they have remained static. You cannot give an answer for the progress on the most recent measures around housing benefit which were supposed to lift children out of poverty; you cannot comment on the measures that have been taken that would tend to increase child poverty, for example rent allowances; you do not know about the child care vouchers; and you have not told us about any ways in which you are to tackle material deprivation. If you look at the number of children in combined low income and material deprivation it is 2.2 million and that number has remained static since 2004-05. Why are you not dealing with those means of measurement and delivering?

Sir Nicholas Macpherson: I regret that I have not been able to answer your questions in as detailed a way as you would like.

Q381 Ms Keeble: They are not very detailed.

Sir Nicholas Macpherson: There are still a good number of people in the Treasury working on this agenda. Inevitably, from a personal perspective I have had less time to devote to the details of this agenda as in previous years because I have had to

spend much of the year dealing with the banks and the implications of the recession in terms of monetary and fiscal policy. It does not mean that it is not important; it is.

Q382 Ms Keeble: The recession would tend to make it worse.

Sir Nicholas Macpherson: All I can tell you is that in terms of my personal time I must prioritise; otherwise, I would never get any sleep at all.

Q383 John McFall: You will be aware that the Sub-Committee has focused on child poverty for a number of years and tried to move it up the agenda. I asked you a question about the shortfall. In the intervening half-hour did you get any whispers from behind?

Sir Nicholas Macpherson: No.

Q384 John McFall: Is your department mute?

Sir Nicholas Macpherson: It is mute as of this minute. All I know is that in the past two years we have made no progress in terms of the child poverty numbers. As I believe I replied to Jim Cousins earlier, we have taken a lot of measures designed to reduce child poverty. All of those will come through in the data for 2008-09 and so on which are yet to be published, but I am slightly suspicious, in part because of experience over the past few years, that they may not fully feed through to the statistics. I can remember saying in previous years that measures would have such an effect and yet after quite a good period in the early part of the decade we find it far more difficult to make progress.

Q385 John McFall: What I gather from page 79 is that you have taken about 2.7 million children out of poverty, whether that is absolute low income households, relative low income households or relative low income households and material deprivation. Taking the first two categories in particular, you have taken out 2.7 million but given it is a flagship policy to halve the number of children in poverty by 2010-11 it is important that we get a precise measure of the shortfall. We went through this before when Mr Mudie was on the Committee; we chipped away at this issue and obtained different figures. I understand the stress that the Treasury has experienced over the past year, but if it can provide us with a memo it will give us a handle on it.

Sir Nicholas Macpherson: I am very happy to do that. I do not want you to go away from this meeting thinking that we have either given up on child poverty or do not take it seriously.⁷

Q386 John McFall: In the past two years it has been difficult for what reason? Is it due to increased unemployment among parents and different things?

Sir Nicholas Macpherson: I think so. Some of this is due to the effect of globalisation. There are huge forces at work in our society that tend to stretch

⁷ Ev 106

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the income distribution. Relative measures of poverty are based on median incomes. If you look at what has happened, despite the minimum wage and other interventions at the lower end of the income distribution wages do not appear to have been rising, certainly not in real terms. You can put more government money into it, but if the labour market is moving against you you just do not make progress. I believe that is the fundamental challenge in our economy.

Q387 Chairman: We shall leave it there. You have promised us a great deal of information. We must have it in good time before the minister appears so we need it by 30 November, if that is possible. Can you also include in it an update on the line of sight programme about which we have not heard for a while?

Sir Nicholas Macpherson: Certainly.

Chairman: In the mean time, thank you very much for your attendance.

Tuesday 8 December 2009

Members present

Michael Fallon, in the Chair

Nick Ainger
Mr Graham Brady
Jim Cousins
Ms Sally Keeble
John McFall
John Mann

Mr James Plaskitt
John Thurso
Mr Mark Todd
Mr Andrew Tyrie
Sir Peter Viggers

Witnesses: **Rt Hon Stephen Timms MP**, Financial Secretary, **Sarah McCarthy-Fry MP**, Exchequer Secretary, HM Treasury, gave evidence.

Q388 Chairman: Ministers, welcome back to the Sub-Committee. Would you identify yourself formally for the shorthand writer, please.

Sarah McCarthy-Fry: Sarah McCarthy-Fry, Exchequer Secretary to the Treasury.

Mr Timms: Stephen Timms, Financial Secretary.

Q388 Chairman: We have had an extraordinary year in the Treasury, with the issues of financial stability. Have you in fact had to divert resources from other projects to deal with those challenges?

Sarah McCarthy-Fry: There is always going to be a balance. Obviously we have had to prioritise our resources, and there has inevitably been a priority, a focus, on stabilising the banking system, but we have tried not to let the bread-and-butter issues go. We are keeping them on track, but inevitably there has been a prioritisation on the banking stability side.

Q389 Chairman: Would you be able to reassure us that you have not in fact stopped any of your lower priority activities? Or have some simply had to be put in abeyance?

Sarah McCarthy-Fry: We are trying to keep them ticking over. Obviously we are trying to balance the whole thing, but, as I said, inevitably we have had to prioritise.

Q390 Chairman: The Permanent Secretary, for example, told us that he personally had had less time to devote to the child poverty agenda because of the time he had had to spend on financial stability. Has that applied to ministers as well?

Mr Timms: I do not think it applies to me, no. I have spent quite a lot of time dealing with child poverty, not least, of course, on the Bill, which has recently completed its committee stage. In terms of ministerial commitment, I would not have been able to identify a negative impact from the difficulties that we have seen.

Q391 Chairman: Which of the associated bodies that report to you do you think will have most call on your time in the year ahead?

Sarah McCarthy-Fry: What do you mean by associated bodies?

Q392 Chairman: I mean the bodies that we look at, like the Royal Mint, OGC, GAD, DMO and so on.

Sarah McCarthy-Fry: Which ones will have most call on ministerial time?

Q393 Chairman: For you, yes.

Sarah McCarthy-Fry: For me personally?

Q394 Chairman: Yes, for you personally.

Sarah McCarthy-Fry: For me personally, probably OGC, I would think, and the Royal Mint as we go through the vesting process and see that through.

Q395 Chairman: Those would be the two that would take most of your time.

Sarah McCarthy-Fry: I would think so, yes.

Q396 Chairman: Mr Timms?

Mr Timms: For me, inevitably it will be Her Majesty's Revenue and Customs, which at any time takes up a large proportion of the Financial Secretary's time. That is much the biggest.

Chairman: Good. Thank you.

Q397 Sir Peter Viggers: When the Permanent Secretary to the Treasury appeared before this Committee on 11 November, Members of the Committee probed about the relationship between the Treasury and UKFI, and the Permanent Secretary said he would write a note to us to explain precisely the way in which we had interacted with UKFI. In fact, the note is very sophisticated but it does the opposite of explaining exactly how the relationship works. Can you please explain the extent to which you are able to control the activities of the banks in which you have majority shareholdings?

Sarah McCarthy-Fry: I will probably say that it is not our role to control the banks' activities. That is what we have passed to UKFI. We obviously have agreed objectives with UKFI. We have established a corporate governance structure for them; we have agreed a business plan; and we have agreed the reporting mechanisms. There are quarterly shareholder meetings held between the CEO of UKFI and senior Treasury officials, and those are forward-looking, risk-based analyses of progress against business plan and investment mandate. A performance monitoring framework is under development and that will be coming forward. As you know, UKFI produces audited financial

statements annually. The first one was produced up to the end of March 2009, and it was laid before Parliament in July, I believe.

Q398 Sir Peter Viggers: To take a specific example and an obvious one, how does the dialogue go about bonuses?

Sarah McCarthy-Fry: Those are discussions that are held as part of the quarterly shareholder meetings.

Q399 Sir Peter Viggers: To what extent are UKFI and the Treasury constrained in their ability to share advice and information?

Sarah McCarthy-Fry: They are both very aware of their legal obligations and having to take that separation, but where information can be shared it definitely is.

Q400 Sir Peter Viggers: At the end of the day I assume the directors of a company are bound by their Companies Act obligations.

Sarah McCarthy-Fry: Yes.

Q401 Mr Tyrie: In these meetings there are also the interests of large minority shareholders to consider. Do they attend the quarterly meetings?

Sarah McCarthy-Fry: I will need to come back to you on that one. I will let you know.

Q402 Mr Tyrie: Goodness me! I am surprised you do not know the answer to that. That would seem to be pretty fundamental. We are talking about people's pensions which are tied up in these. We have no idea whether the minority shareholders have had an opportunity to comment on the bonus policy and the effect that would have on long-term value of the firms.

Sarah McCarthy-Fry: That would be between UKFI and the minority shareholders. I am talking about the relationship that we have as majority shareholders with UKFI. I will need to come back to you on that.

Mr Tyrie: Will you come back to us and let us know? Thank you very much.¹

Q403 Mr Plaskitt: The Annual Report and Accounts from HM Treasury discussed the Asset Protection Scheme and mentioned the targets that were given to RBS and to Lloyds for additional lending. Who set those targets?

Sarah McCarthy-Fry: They were agreed between the Treasury and RBS and Lloyds. I do not know exactly who set them.

Q404 Mr Plaskitt: But someone came up with the numbers.

Sarah McCarthy-Fry: It was a number that was felt appropriate.

Q405 Mr Plaskitt: By whom?

Sarah McCarthy-Fry: I do not know who came up with them.

Q406 Mr Plaskitt: You do not know why it was those particular numbers: why £25 billion for RBS and why £14 billion for LBG? I just wanted to know the reasoning behind those particular numbers.

Sarah McCarthy-Fry: I am afraid I do not know the answer to that. We can get a note to you.² I do not know the reasoning or why those particular numbers came up. That is the numbers that were agreed between them.

Q407 Mr Plaskitt: Are numbers being devised for lending targets for those banks for 2010?

Sarah McCarthy-Fry: We are looking at similar lending commitments in respect of the 12 months up to 2010.

Q408 Mr Plaskitt: Is there a process working that will come up with a specific number again?

Sarah McCarthy-Fry: Yes.

Q409 Mr Plaskitt: Even though the report says it depends on market conditions and obviously we do not know in detail market conditions ahead of time.

Sarah McCarthy-Fry: Assuming a steady state, it will be a similar number. If the £14 billion and the £25 billion were the appropriate numbers within those market conditions that would be the proportion, and then depending on market conditions.

Q410 Mr Plaskitt: So it will not be the same numbers.

Sarah McCarthy-Fry: Not necessarily the same exact numbers.

Q411 Mr Plaskitt: Will there be any sanctions imposed if those numbers are not met?

Sarah McCarthy-Fry: Obviously we are hoping that we can get through those numbers. There is additional work being done to establish, if the conditions are not met, is it because the banks are not fulfilling their side of the bargain or is it because there is not sufficient demand? That would have to be gone through first. There is a sanction in the access to the Credit Guarantee Scheme. That is the only formal sanction there is but obviously we are working through other things.

Q412 Mr Todd: One of the DSOs is to professionalise the finance function in government. At the moment only 22% of bodies which are required to report accurately on a timely basis monthly do so to the standards required. Is that reasonable?

Sarah McCarthy-Fry: No, of course it is not reasonable. That is why there is the process of professionalising—

Q413 Mr Todd: But we have been attempting to professionalise this area for some time.

Sarah McCarthy-Fry: Yes, and work is ongoing. We have the requirement that all the directors should be qualified with a financial qualification.

¹ Ev 110

² Ev 110

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Q414 Mr Todd: Are we there yet?

Sarah McCarthy-Fry: I believe so.

Q415 Mr Todd: I seem to remember the MoD was one of the big exceptions.

Sarah McCarthy-Fry: I do not know about the MoD. This was referring to the Treasury, and certainly within the Treasury I believe we are now there.

Q416 Mr Todd: Bearing in mind the Treasury's important responsibility to manage public expenditure, accurate reporting from people who know how to do their job professionally is surely a pretty critical part of your function.

Sarah McCarthy-Fry: Yes, it certainly is. It is why it has had a large focus, in that we want to make sure that our financial reporting is accurate and meets all the required standards.

Q417 Mr Todd: That focus seems to have been rather dim if the outcome seems such a gentle one so far.

Sarah McCarthy-Fry: It does not mean we are not on the right track.

Q418 Mr Todd: What are we doing to do to improve that further?

Sarah McCarthy-Fry: We are initiating a review of the Corporate Governance Code. We are making sure the finance directors are able to improve the financial management across government. They are going to introduce benchmarking and to implement a self-assessment tool through CIPFA that we can monitor.

Q419 Mr Todd: One of the obvious reasons why this is important is that we are entering a period of greater stringency, in which the management of resources is even more critical than it has been before. If we were not getting it right in what were gentler times in the reporting period involved, it is not very encouraging, is it?

Sarah McCarthy-Fry: The benchmarking will be important, because then we can see where the focus needs to be addressed. Using the self-assessment tool will enable us to monitor that.

Q420 Mr Todd: In an inquiry with the HMRC I asked a number of questions about the Mapeley contract on property. I said how, based on the extraordinary terms of the ability to return property to Mapeley for them to resolve its future, a tremendously good deal had been struck. The bit that I did not ask about—and that was my mistake but the NAO has remedied that—was from the other point of view, which was to examine the risk to Mapeley of such an aggressive programme of transfer of property. Have you examined that?

Mr Timms: Yes. As you say, the NAO has just issued a report on this, and I think there is going to be a PAC hearing in January exploring the work that the NAO has done. But we certainly have been considering the issues that might arise with the Mapeley contract, including whether there is a risk

to Mapeley and other contingencies that we need to think through. Our view is that we have obtained quite impressive value from the contract, for some of the reasons that you referred to when you commented on this before. The NAO has said in its new report that a number of things need to be done to ensure that we do secure the full value from that contract over its life. We accept that. We agree that there is work to be done, and officials will be commenting in detail on that at the PAC hearing in January.

Q421 Mr Todd: The NAO has identified that the contract has cost £312 million more than forecast. There are a number of possible reasons for that. What is your perspective on that?

Mr Timms: There have been a number of changes since the contract was signed. One of the issues, which I know the NAO picked up correctly, is that some of the flexibility for vacating space which was available early on in the contract was not in fact taken up. That is now being taken up. We believe that the department will have made full use of all the flexibility to vacate by the end of 2010–11.

Q422 Mr Todd: So part of this is about timing.

Mr Timms: I think it is, yes.

Q423 Mr Todd: But then one goes back to the issue of Mapeley's capability to absorb a large amount of property being transferred back to it in a recession.

Mr Timms: We are certainly aware of those challenges, which are indeed clear, and we are aware of the risks that they pose to Mapeley, and so HMRC has carried out quite a lot of work to understand the nature of the financial risks to Mapeley and how they can be addressed.

Q424 Mr Todd: I think I am right in saying that this is much the largest contract Mapeley has. Is it?

Mr Timms: They certainly have other contracts, but I imagine this will be the largest of them. It is worth underlining that that flexibility to vacate properties is a very important benefit of the contract.

Q425 Mr Todd: It is.

Mr Timms: As you pointed out when you commented on this before. Of course HMRC pays Mapeley a premium for that benefit.

Q426 Mr Todd: Just to finish this, the obvious point is that this contract was struck at a very different time in the property market, and if you suddenly transfer a large chunk of the property at a point where its passing on to other tenants is, frankly, rather unlikely, it would not be very surprising if this stressed the contract to a very significant extent.

Mr Timms: That possibility is the reason for the very substantial work that HMRC has done.

Q427 Mr Todd: Could you share this work a little bit more with us in a note perhaps?

Mr Timms: I would be very happy to see what we can provide.³

Q428 John McFall: I think that is important, minister, because the NAO press release was very clear in saying that HMRC has not achieved value for money on the contract. It goes on to say that HMRC does not have an agreed way forward with Mapeley and if Mapeley were to default on the contract then HMRC could incur significant one-off and ongoing costs. Maybe the picture is not as rosy as you suggested at the beginning.

Mr Timms: The message that I took from the NAO Report was that of the need to take a number of steps to make sure that over the full lifetime of the contract we achieve the full value-for-money benefits that it offers. The points the NAO made were entirely appropriate about that. There is work that needs to be done. I am equally confident we will be able to do it.

Q429 John McFall: What is the obstacle to agreeing a way forward with Mapeley at this stage?

Mr Timms: We have a contract with Mapeley and that contract is being observed.

Q430 John McFall: The NAO was very clear that you do not have an agreed way forward.

Mr Timms: We do have an agreed contract. I am not quite sure what the way forward they were referring to was.

Q431 John McFall: They are talking about this vacations programme creating “areas of specific financial pressure for Mapeley, exacerbated by the economic downturn and falling property values” and “HMRC is now planning to vacate a significant number of its buildings by 2011.” You do not have an agreed way forward, I presume, on that area, and if Mapeley were to default then you are going to find yourself with extra costs here.

Mr Timms: We are proceeding in the terms of the contract. The contract is absolutely clear. HMRC is paying a premium to be able to have the flexibility that the contract offers. We are now taking use of that flexibility. We are aware that there could be pressures on Mapeley in the future and we are looking very carefully at what those pressures might be. In terms of having an agreed way forward, we are complying and Mapeley is complying with the terms of the contract.

Q432 Chairman: Perhaps you could let us have a note, just to reassure us on that.

Mr Timms: I would be happy to do that.⁴

Q433 Chairman: Thank you. Could one of you help me with the way you assess these outcomes. Outcome 2(a) “Supporting low inflation” you describe as “met—ongoing” when in fact you missed the inflation target with three of the four quarters in 2008–09. What does “met—ongoing” mean?

Sarah McCarthy-Fry: It is across the balance as a whole and looked at over the whole period.

Q434 Chairman: But looking at it over the year, the target was missed in three out of four quarters, so how can it be met?

Sarah McCarthy-Fry: I believe it is because we are looking at it across more than one year. Let me just check that one for you.

Q435 Chairman: This is your Annual Report, you are reporting on the target, the target was missed in three out of four quarters, and you call it “met—ongoing”.

Sarah McCarthy-Fry: It is presumably because we got there at the end of the year. I am afraid I cannot go any further than that. I will have to come back to you on that one.⁵

Q436 Chairman: Sure. Maybe you can come back with a better answer before we finish this morning.

Sarah McCarthy-Fry: Yes, hopefully.

Q437 Chairman: Would you like to reflect on that.

Sarah McCarthy-Fry: Yes, I will.

Chairman: Thank you.

Q438 Jim Cousins: Pursuing that particular issue a little further, in the Annual Report two risks to the future delivery of the inflation target are set out. The nearer term one is the large negative output gap which is depressing prices and wages, and then further out is the lagging effect of the depreciation of sterling. Which of those two risks matters more to the Government?

Sarah McCarthy-Fry: I would say that both risks matter to the Government, but obviously, as far as inflation is concerned, it is the responsibility of the MPC to keep within the inflation target. We can see that from their minutes when they have debated those risks.

Q439 Jim Cousins: The large negative output gap would obviously point to low interest rates, whereas a concern about the lagging effects of the depreciation of sterling would point to higher interest rates. Do you not think that the MPC needs some guidance as to which of those risks the Government considers to be the more important?

Sarah McCarthy-Fry: The MPC has a very clear remit. That was the whole purpose of making the Bank of England independent, that they would manage those risks. Their remit is to manage the inflation target. Those are both risks that they would have to take into account in their deliberations.

Q440 Jim Cousins: Surely it is not for the MPC to choose which of those risks it regards as being the more significant and let the Government know?

Sarah McCarthy-Fry: All I can say is that it is a matter for the MPC. We have their published minutes: we can see how they reach their

³ Ev 110

⁴ Ev 110

⁵ Ev 111

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conclusions. They have a remit for their inflation target and if they do not meet that they have to write to us.

Q441 Jim Cousins: The other matter I wanted to raise with you, which is more a matter for your comment, was on this issue of pensioners, who of course are not reflected in the Annual Report. I did ask about that, and more information was very kindly supplied to the Committee in which it was pointed out that of the three million pensioners plus who were not claiming the higher rate pension personal tax allowance for pensioners, most had incomes so low that it did not matter whether they claimed it or not. You will see straightaway that, however reassuring that might be on the technical point, it does raise slightly broader issues. Could you in any way enlighten the Committee as to how many of the three million plus pensioners who are not claiming the personal tax allowance to which they are entitled would have benefited from so doing?

Mr Timms: I think the issue is how much they would have benefited rather than that they would have benefited at all. I can give some information that might shed some light on this. As you know, we launched our Taxback Campaign on 26 October.

Q442 Jim Cousins: That is the savings issue which I was going to come on to later.

Mr Timms: Yes, the tax reclaim issue.

Q443 Jim Cousins: Large numbers of pensioners are paying tax on their savings when, probably speaking, they should not.

Mr Timms: That is right. That is why we are writing to 3.4 million Pension Credit recipients over a six-week period. So far (by 27 November) we have issued 2.9 million letters, we have received 13,205 claims, we have processed 1,591 of them, and the average repayment is £53.19. That gives some indication of the extent to which pensioners in the past were not getting the full benefit to which they were entitled.

Q444 Jim Cousins: Thirteen thousand out of 2.9 million have responded.

Mr Timms: So far.

Q445 Jim Cousins: So far, yes.

Mr Timms: This is a continuing campaign.

Q446 Jim Cousins: Will you write to people again next year about this?

Mr Timms: There are periodic Taxback Campaigns. This is the ninth. The last one was in November of last year. No firm decision has been made, but I would certainly expect these efforts to continue.

Q447 Jim Cousins: You will appreciate that the tariff income schedule, which measures the value of pensioners' savings for the purposes of means-tested benefits, assumes an interest rate of something like 25%, so to have large numbers of pensioners cheated of their money by overpaying tax on their savings on the other hand is obviously an important point.

Mr Timms: I certainly agree. It is an extremely important point. That is the reason for this campaign and the campaign of advertising and the other steps we are taking, working with Citizens Advice, Age Concern, Help the Aged and so on, to ensure that everybody has the opportunity to reclaim their tax back.

Q448 Jim Cousins: Do you regard the average repayment of £53 as being an important figure or not?

Mr Timms: It is certainly important for those who receive it, absolutely.

Q449 Jim Cousins: Exactly.

Mr Timms: I want to take issue though with your point about the implied interest rate of 25%. I do not think that is accurate because the assumptions allow for the fact that it is reasonable to expect that people will be able to use some of their savings for meeting their needs, so it is not assumed that people are simply living on interest from their savings.

Q450 Jim Cousins: Coming back to the issue of the three million pensioners who are not claiming the personal tax allowances to which they are entitled, how many of those pensioners do you think would benefit from so doing?

Mr Timms: As I understand our assessment of the data, the great majority have income below the tax allowance figure.

Q451 Jim Cousins: How many do not?

Mr Timms: Our estimate is that it is about half a million. Of the 3.2 million total, 2.7 million have income below the tax allowance figure.

Q452 Jim Cousins: So out there are half a million pensioners, you think, who would benefit from claiming the higher rate of personal tax allowance but are not doing so.

Mr Timms: That is the best figure that I have.

Q453 Jim Cousins: What are you doing about that?

Mr Timms: As I was saying on the earlier topic, we are working with organisations like Citizens Advice and Help the Aged to ensure that as many people as possible understand the opportunity that there is and take advantage of it, and we will continue to work at that.

Q454 Jim Cousins: How many of the people who are overpaying tax on their savings and not claiming the tax allowances that would help them, are in fact older women living on their own, which is typically the group who most lose out in this because they simply do not understand it?

Mr Timms: I am not able to give you a precise figure but you are undoubtedly right that a very significant proportion will be.

Jim Cousins: Thank you.

Q455 Ms Keeble: Are you concerned about the stall in progress on the relative poverty target?

Mr Timms: Yes. We made very substantial progress on reducing child poverty in the early years after the commitment was made in 1999. Since then there has been a plateau, but we have made, particularly in the Budget last year, further announcements. As you know, on the most recent figures child poverty since 1999 has fallen by half a million. Our assessment, and I think the assessment of independent analysts, is that the additional announcements we have made will reduce the figure by a further half million. We will see further substantial progress.

Q456 Ms Keeble: But will we reach the 2010 target?

Mr Timms: Hitting the 2010 target would be a stretch. Clearly there is an opportunity for the Chancellor to make an announcement this week and further opportunity in the Budget next year. The assessment that the IFS has made is that, by the time at which that target will be assessed, we will have reduced child poverty by 1.1 million, which means we will be almost two-thirds of the way towards the target but not actually hit it.

Q457 Ms Keeble: In the measures that were announced in 2007 that were going to roll forward, all but one has been completely implemented. The only one remaining is a Housing Benefit change. The Permanent Secretary was unable to say what the progress was. He said he just assumed it was going okay, although in fact implementation had been knocked back a month without anybody being told, I think. What is your assessment of the success of the implementation of that particular change, given it is the last one before an election comes and before the target date?

Mr Timms: I am rather in the same boat as the Permanent Secretary on this. It is not a concern that has been raised with me.

Q458 Ms Keeble: Perhaps I can raise some particular concerns with you then. Can you confirm the number of families that were supposed to be helped? I see here that we have 200,000 getting £20 a week, which is £200 million, I think, if my maths is right. I thought it was more than that. I thought it was either £250 million or £350 million that was originally announced when these were first announced back in 2007. Can you confirm the figure?

Mr Timms: I am afraid I do not have those figures in front of me, but I can certainly come back having checked those.⁶

Q459 Ms Keeble: That would be helpful. Something again which I raised with the Permanent Secretary—and he was not able to say and his note is not clear—is that, whilst there are changes in Housing Benefit, they only affect social housing tenants, they do not affect people on Rent Allowance, and they do not affect people who are now on Local Housing Allowance. For both of those groups the pressures are massive, and certainly for those with Local Housing Allowance the recent changes will tip some families into poverty because of the claw-back. Why

have those not been factored into the figures? Is there not a real risk of the numbers starting to go in the wrong direction because of those particular issues?

Mr Timms: I am not sure which figures you are suggesting they should be factored into. The projection—

Q460 Ms Keeble: The total number of families living in poverty.

Mr Timms: The figure that we have published, the half million figure, does take account of all the changes that had been put into effect up until the point to which those figures applied. The projections are not from the Government, they are from the Institute of Fiscal Studies.

Q461 Ms Keeble: The note we have says that the Government does not hold quality assured data on the family breakdown of LHA customers. You do not have the data, is that right?

Mr Timms: I think what the note says about that is correct. But that is a slightly different issue from the child poverty figures, where the half million does take account of all the changes there have been up to the point where that was measured. The next set of figures, equally, will take account of all the changes—

Q462 Ms Keeble: It will take account of the changes to Local Housing Allowance and the fact that quite a lot of poor families are facing a claw-back in income because of these rule changes, which, as you know, a lot of people are very concerned about.

Mr Timms: Yes, it certainly will. The data takes account of all people's sources of income.

Q463 Ms Keeble: On the childcare element of the Tax Credit, which is specifically your responsibility, are you surprised at the low average weekly rates of money provided? Do they not indicate that they are being claimed for part-time work and quite minor part-time work and that people are not taking it up in quite the way that was perhaps originally intended?

Mr Timms: I must say I had not been struck by that as a surprise. We have seen an encouraging increase in the number of people taking up the childcare element of the Tax Credit.

Q464 Ms Keeble: Two hundred thousand.

Mr Timms: I am sure there is scope to do better still. Certainly many parents will be using that support to help them manage childcare alongside a part-time job; others will do so for full-time work. It is clear that part-time work is a very important contribution to the progress we have made on child poverty. There are some parts of the country where part-time work is harder to get than others and that is a reason why we have had some difficulties in those parts of the country. But I have not been surprised myself by those figures.

Q465 Ms Keeble: I want to press you on that. It surprises me, because certainly in my own constituency somebody was paying £500 a month

⁶ Ev 111

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for three days childcare a week, and your average claims here are £68.69. That would barely pay for a bit over half of a part-time place, let alone anywhere near somebody being able to go out to full-time work. What studies are being done of all of this data and of the take-up in what is happening to women?

Mr Timms: We have looked very carefully at the take-up point and we are working to increase take-up and we are looking as well at whether there are more effective ways in which childcare provision can be supported.

Q466 Ms Keeble: Material deprivation indicators are another of the measures of poverty. Are you concerned, since again it was your specific responsibility in the Bill, that the very excellent indicators of material deprivation are not enforceable and are not costed?

Mr Timms: I agree that the indicators of material deprivation in the Bill are excellent. It is worth making the point that they are the result of quite a lot of academic work and reflection—I cannot claim credit for them myself. Their role is to measure material deprivation, so they are not things that are for enforcement, they are for telling us what is happening in the lives of children.

Q467 Ms Keeble: Is it not of concern that you have an indicator which you measure and for which you have graphs but it is reliant on things which are not costed and which cannot be enforced? Does it not make that aspect of the Government's commitment on child poverty a wish rather than any firm commitment or anything that is achievable?

Mr Timms: The indicators and the measurements which go with them are informing us about the lives of children in the UK. The commitment in the Bill is that the proportion of children who suffer material deprivation and are of relatively low income should be less than 5% by 2020. It is a measuring tool. That is the purpose of those indicators. We are not saying that people want to abolish the position where anyone on any one of the 21 indicators is below a certain level. That is not the nature of them. It is about getting a view across the board of the level of material deprivation amongst children in the UK and a commitment to ensure that that level is very sharply reduced between now and 2020.

Q468 Ms Keeble: I want to ask one more question about the Asset Protection Scheme, a completely different subject. What information do you have about the Treasury's calculations of potential losses and when you might expect to see them start to crystallise? There has been much speculation about it and it is a key factor in terms of the cost of these special measures.

Sarah McCarthy-Fry: I think it is too early to say. We have put the additional cost in with the excess vote. We do anticipate that we are going to get as much back as we can. It is too early to say when we expect or even if we expect any of this to crystallise.

Q469 Ms Keeble: But it has been too early to say, I have to say, for quite a long time. There must be some sort of scoping out of what the future is likely to look like, given that if the costs do start to crystallise then they could be quite substantial.

Sarah McCarthy-Fry: It is an ongoing situation and I do think it is too early to give any timetable or exact figures at this stage.

Q470 Mr Brady: The Permanent Secretary told us that UK taxation is far too reliant on receipts from the financial sector and the housing market. He said that there are important lessons to be learned for the future. What lessons for the future have you learned?

Mr Timms: I think he said that we have to look for tax where we can find it (or an expression of that kind). As you know, the key commitment that we have made on this is to reduce the deficit by half over the next four years. We have made a number of announcements on tax measures which will contribute to that target already. The Chancellor no doubt will comment on this again when he stands up to address the House in the Pre-Budget Report tomorrow. One area that I would highlight is the work we have been doing on addressing both avoidance and evasion and making sure that the tax that is due is collected in. We have taken a number of steps to close loopholes and to bring in tax that otherwise would have been lost, and I think that is going to be very important work over the next four years while we seek to halve the deficit.

Q471 Mr Brady: Would you envisage the proportion of the tax take coming from financial services and the housing market being less during a recovery than it is at the moment or than it has been historically?

Mr Timms: That is going to depend in particular on the level of profitability in the financial sector, and at the moment, of course, things look rather more buoyant on that front than they did a year ago, or, indeed, rather less than a year ago. But it is the amount of corporation tax paid by those institutions that will be the key determinant of that.

Q472 Mr Brady: You are hoping that we will be just as reliant on tax from financial services in the future as we have been in the past.

Mr Timms: I suspect that the UK economy as a whole is not going to be able to depend on growth in the financial sector to the extent that we have been able to over the last decade. Of course that is the strategy that Lord Mandelson has just set out, the New Industry, New Jobs strategy which involves, as the CBI have been calling for, for government to identify parts of the economy where we can look forward to higher growth (like, for example, the digital sector, for which I also bear ministerial responsibility) and the Government then making sure that we have the wherewithal in place for those sectors to thrive and do well to contribute tax revenues and contribute employment as well.

Q473 Mr Brady: To turn to the temporary VAT reduction, do you regret the decision to end it on 1 January?

Mr Timms: No. The key thing with the change—and by the way I do believe that the VAT reduction has been a very significant contribution to limiting the damage that the worldwide downturn has inflicted on the UK economy—was to be absolutely certain at the outset of when the rate was going to go back up, so that people had confidence to plan for that change. It is also important in order to maximise the stimulus benefit of the announcement, because clearly people have an incentive at the moment to make purchases now and in the early few days after Christmas, ahead of the rate going up. The key thing was to say when it was going to happen and to stick to it, and not to change it. That is what we have done.

Q474 Mr Brady: Is not 1 January the most inconvenient date possible for many businesses?

Mr Timms: That point has been made to me by retailers. I understand the difficulties that they might face, but talking to the British Retail Consortium, their overriding concern was that they should have plenty of time to plan for the change. They would have preferred that it was not at the beginning of the January sales but, more than that, they wanted to be absolutely sure when it was going to be.

Q475 Mr Brady: What other dates did you consider?

Mr Timms: I do not think we looked at any specific alternative date. We did consider whether it would be right to have a different date, either an earlier date or a later date, but there was not any particular date that we considered, and of course if the date had been deferred at all then there would have been a significant impact. The cost of a month's delay, for example, is of the order of £1 billion. Given the importance of consolidating the public finances, change along those lines was not attractive.

Q476 Mr Brady: Do you believe there has been the stimulus effect that was intended at the outset?

Mr Timms: Yes. Clearly this is something that the economists are going to be looking at for some time, mulling over the data as it emerges, but I think the evidence is clear. It is one of the reasons, certainly, compared with previous recessions, why we have seen retail sales have been very buoyant. The economy has supported a lot of jobs and meant that the expectations that people had about reduced employment or repossessions and so on have not been fulfilled. I think the VAT reduction has been a very important and effective part of the stimulus.

Q477 John Mann: My questions are about HMRC. Are you proud of your management of HMRC?

Mr Timms: I am proud of a lot that HMRC has achieved.

Q478 John Mann: Are you proud of your people management?

Mr Timms: HMRC has achieved an extraordinary amount in a relatively short time under enormous pressure. It has, for example, delivered a very

significant reduction in its workforce from, in full-time equivalent terms, 98,000 to 78,000 between April 2004 and October 2009, so just over five years. That is a dramatic change.

Q479 John Mann: Are you proud of your people management?

Mr Timms: It is undoubtedly the case—and I imagine this is what you are referring to—

Q480 John Mann: I am referring to your people management. Are you proud of your people management?

Mr Timms: I want to set out the scale of the people management challenge.

Q481 John Mann: With respect, Minister, you seem to be avoiding my question. Are you proud of your people management in HMRC?

Mr Timms: No, I am not trying to avoid your question. I am attempting to answer it and I hope you will allow me to do so. There has been a huge people management challenge in HMRC. You have seen the effect of that in the very disappointing results of the staff survey on morale. Another big hit on morale has been the workforce change exercise and the work we have gone through to close down offices. We were talking earlier on about the flexibility in the Mapeley contract that has allowed us to do that. That had to be done, it was necessary, but it has been extremely difficult for staff in HMRC, particularly when a number of them did not know where they were going to be working.

Q482 John Mann: Are you proud of your people management in HMRC?

Mr Timms: Having done that, I think we can look forward to a much more certain future for people in HMRC. I hope we will see an improvement in staff survey results, reflecting good people management in the future.

Q483 John Mann: Would it be possible to have anything other than improvement in the survey results?

Mr Timms: I certainly very much look forward to an improvement. I agree that one is much needed. HMRC recognises that.

Q484 John Mann: Do you have confidence in your senior civil servants in HMRC?

Mr Timms: Yes, I do.

Q485 John Mann: Why is it that 89% of the staff do not have confidence? Why do they have a different view from yours?

Mr Timms: I think that is a reflection of the challenges the organisation has had to go through over the last few years, as I have set out. With the appointment of Mike Clasper as Chairman of HMRC and Lesley Strathie as Chief Executive, there is now a very impressive team at the top of HMRC. They have been talking me through their proposals for strategy for the organisation. The strategy that is emerging is a very compelling

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strategy and I do believe that will be translated into better and more successful people management and a more confident organisation in the period ahead.

Q486 John Mann: The Treasury loves evidence-based analysis. What analysis do you have that demonstrates anything other than high morale leads to high performance?

Mr Timms: The evidence that high morale leads to good performance is compelling.

Q487 John Mann: In HMRC there is evidentially low morale. How much have you quantified the consequential low performance?

Mr Timms: If you look at what HMRC has achieved—that is something that we measure very carefully and some of the data is in the report that the Committee has—the achievements have been very impressive through what I have said has necessarily been a very difficult period. Could it have been better if it had not been necessary to reduce the size of the organisation? Perhaps.

Q488 John Mann: What tax loss do you project because of the ongoing low staff morale?

Mr Timms: I do not have a projection for that.

Q489 John Mann: Does anybody in HMRC have a projection for that, whether published or otherwise?

Mr Timms: I would imagine probably not.

Q490 John Mann: Why not? If one looks at how every other business does its business, quantifying staff morale and importance would be a fairly mainstream and important factor. There seems to be uniqueness in HMRC—

Mr Timms: No, I do not think that is fair.

Q491 John Mann: You do not appear to have quantified the potential loss in output from low staff morale. We can quantify low staff morale.

Mr Timms: Yes, indeed.

Q492 John Mann: What attempts have been made to quantify the consequential performance reduction and, specifically, the projected tax loss to be quantified from that low staff morale?

Mr Timms: It is important that credit is given to HMRC for tracking staff morale in the way that you describe. It certainly is not the case that that is not a subject of interest or that it is not properly tracked. It is properly tracked and carefully for exactly the reasons you state. Would HMRC have been able to achieve more if it had not had to reduce its staff numbers by 20,000, if it had not had to shut down offices and so on? Perhaps it might. As far as I know, no attempt has been made to quantify what that might have been. Instead, what is being done—and in my view this is absolutely the right thing—is setting very clear objectives for closing the tax gap, for example, and putting in place the organisational changes, the IT changes, that will enable HMRC to do a better job in the future.

Q493 John Mann: Have you personally, as the Minister, experienced over the last two years any evidence of discrimination, harassment or bullying at work within HMRC?

Mr Timms: Have I personally experienced that? No.

Q494 John Mann: Have you witnessed any?

Mr Timms: No.

Q495 John Mann: Are you aware of any?

Mr Timms: I am aware from correspondence that I have received that from time to time complaints of that kind are made.

Q496 John Mann: How prevalent in your judgment is it?

Mr Timms: I have not been able to substantiate personally any of the complaints that have been raised with me about that.

Q497 John Mann: I would not necessarily expect you as the Minister to substantiate individual cases, but, because it is your role to have a view of the overall position, how prevalent is harassment, discrimination and bullying at work within HMRC?

Mr Timms: I do not believe any of those are prevalent in HMRC.

Q498 Mr Tyrie: Within a one-year period, 84% of your staff have experienced it. Do you know of anywhere else within the public sector where there is that level of discrimination, harassment and bullying being self-identified by staff?

Mr Timms: I think you are slightly misrepresenting the data. I do not think that is 84% of people who have experienced those things.⁷

Q499 John Mann: I am not misrepresenting the data. Any self-defined expression of view is subjective: that is what the person thinks. The data is that 84% of your staff say they have experienced discrimination, harassment or bullying at work in the last 12 months.

Mr Timms: I do not think they are saying they have been on the receiving end of those things. That is as I understand the survey.

Q500 John Mann: They are saying they have experienced it. Whether it is them personally or whether they have witnessed it, I have no idea, but they have experienced it. Is there anywhere else in the public sector with this level of bullying and harassment problems?

Mr Timms: There is probably nowhere else in the public sector that has undergone the scale of difficult and demanding change that this organisation has been through over the last five years.

⁷ *Note by witness:* The figure across HMRC is 16% experiencing bullying, harassment or discrimination. There appears to have been some misunderstanding of the survey results. The breakdown of the results gives percentage positive scores meaning that 84% have **not** experienced bullying, harassment or discrimination. There is a footnote in the results which states “Positive = no, staff have not had this experience and Negative = yes, staff have had this experience”.

Q501 John Mann: Organisations change all the time. Management change is ongoing throughout society for all employers. Are you aware of any private sector organisation where the staff feels so disenchanting with their employer?

Mr Timms: I think it is the case that there are examples in the private sector of findings from staff surveys comparable with those that HMRC are finding.

Q502 John Mann: So I come back to my initial question: Are you proud of your management of people at HMRC?

Mr Timms: I want to assure the Committee that HMRC top management, the Chairman and Chief Executive—and you have had the opportunity to explore this with them—are absolutely committed to improving the morale and reducing those very damaging and worrying figures that the staff survey contained.

Q503 John Mann: I have just two more questions which are slightly different but on the same theme, and they are about the future. You are putting staff into bigger centres, mainly in the centre of cities—places like Nottingham and Leeds, for example. Have you green-proofed these changes?

Mr Timms: There certainly has been, in the course of the Workforce Change programme, an assessment of the environmental impact of the changes that are being made.

Q504 John Mann: A lot of people have to drive further into cities, where properties prices are tending to go up. To take those two cities, Nottingham and Leeds, in different ways a form of congestion charge is now being proposed for employees entering the city. Have you built that into your calculations in closing down local tax offices?

Mr Timms: I think I am right in saying, yes, an assessment of the environmental impact that was made did take account of that issue.

Q505 John Mann: I would put it to you that the projected future costs of “congestion charge style” local taxes in cities has not been costed in and that may be one of the reasons that many of your staff are concerned about having to move to these cities.

Mr Timms: Manchester is certainly a case in point. There has not been assessment made of which other cities might in the future introduce congestion charges and therefore adding in the costs of putative future schemes into the changes, that is true, but I would not myself favour attempting an exercise of that kind. Your question was about green-proofing; the environmental impact of the changes certainly has been assessed. Perhaps I could make one final point on this. I do not want for a moment to take away from the seriousness of the concerns with the survey. The Committee is absolutely right to focus on those. Everybody at HMRC wants to do better in the future. It is worthwhile making two further points. The survey did of course show a very large proportion of people committed to staying in HMRC. That is a positive finding. The other point I

would make is that visiting HMRC offices, as I do, and particularly where the PaceSetter form of working has been adopted, the people who are working in those offices say to me that are enjoying their work and that they have found the management changes that have been made incentivising and encouraging and welcome, and they have very high motivation in setting about their work. I think there is a better side of the story to be told beyond those, as I fully accept, very disappointing and concerning figures in the staff survey.

Q506 Nick Ainger: I would like to ask some questions on the Royal Mint. When Andrew Stafford the Chief Executive gave evidence to the Committee, I asked him some questions about the Operational Efficiency Programme, the Gerry Grimstone Review, and it emerged that Mr Grimstone had not visited the Royal Mint at Llantrisant, nor had he spoken to the management or met the management. Do you find that surprising, that he is recommending the future of an organisation like the Royal Mint but is not meeting its management or visiting the only site it occupies?

Sarah McCarthy Fry: Not when you consider that the review team visited, so it was not as if there was no information that was coming back. Their review was actually led through the Shareholder Executive that reported to Gerry Grimstone, so while he did not visit himself I am satisfied that he had all the information that he needed in order to conduct the review because it had been visited by members of the review team.

Q507 Nick Ainger: That was not the evidence that was given us by Andrew Stafford. You may be right, but certainly in his answers he made no reference to the review team visiting Llantrisant. I also asked Mr Stafford about what the advantages were of vesting the Royal Mint and moving to a government trading company, and he told us that there were two things: first of all that they could acquire companies outside the UK to expand their business, and the second was “joint ventures with overseas partners to enable us to penetrate markets”. Should that be the role of the Royal Mint, to start acquiring companies—I do not know where—in Europe or in the Far East?

Sarah McCarthy Fry: But if you consider that the majority of the Royal Mint’s output is for the export market and not for the UK you can see where that would come in, that they will be able to generate better business, they will be able to be more commercial by going into joint ventures overseas. We need to maintain the ability in my view to strike our own coinage in this country, but also, if we have now have got it as a vested company, I think it does give them the opportunity to operate on a more commercial basis and make it better value for the taxpayer.

Q508 Nick Ainger: But here we have an organisation which in the past has been loss-making; it has only recently returned to profitability, now wanting to start acquiring, I assume, other manufacturers as

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well as getting access into other markets. Is there not a risk that if that does not work out well it could come back and put the whole organisation at risk?

Sarah McCarthy Fry: I do not think so. I think they have shown in the past two years that they are able to bring it back into profit, that this current management team is able to run it as a profitable organisation, and they have turned the organisation round. I personally visited the Mint myself a couple of weeks ago, so I have seen what they do there and how it operates. There is another reason why I think vesting will be good as well as them being able to go into joint ventures and find trading partners around the world and build the business. It is also that they believe that they will be able to attract a better quality management team within a vested organisation and they believe a company structure is more likely to do that because they have greater freedom to act and have the clarity of governance to enable them to operate as a commercial organisation. However, of course, as I say, it is my strong belief that we should maintain the ability to strike our coinage here in the UK. There are world-class facilities down there and if we can get better value for the taxpayer by them being able to bring in more business I think that is a good thing.

Q509 Nick Ainger: I have also visited the Royal Mint and I too was impressed with the workforce and the effectiveness of the management because, after all, it is this management which has turned round a loss-making situation and they are now giving greater returns than required. However, coming back to the public policy objectives of the Royal Mint, there are four. The first one is to deliver a commercial return on capital employed, the second one to ensure a secure and timely supply of UK circulating coins, the third to provide expertise to the Government on coin and minting issues, and the fourth is to meet all relevant legislative requirements. Only the first one is a commercial issue, obviously. The other three issues are not commercial issues. Is it your intention, following vesting, in the longer term to privatise the Royal Mint?

Sarah McCarthy Fry: The purpose of vesting was not to privatise the Royal Mint. We are working through vesting and we are looking to see what we can gain as an advantage. As I say, it is my belief that we need to be able to strike our coinage here in the UK and use the expertise that we have in the UK to do that. I do think that operating commercially and bringing in more business overseas will help to deliver better value for the taxpayer and help us deliver those other objectives that the Royal Mint has.

Q510 Nick Ainger: But the current view within the Treasury is that the Royal Mint will not be privatised?

Sarah McCarthy Fry: The current view is that the purpose of vesting was not as a prelude to privatisation.

Q511 Chairman: If I may turn to the Valuation Office, last year we reported on the ports revaluation. Perhaps, Mr Timms, you could tell us to what extent the port owners have taken on the backdated liability as payable by port occupiers that the Valuation Office identified.

Mr Timms: I do not think I do have much information about that. As you know, since we had the discussion on that subject we have announced the arrangement by which businesses in port areas will be able to pay by interest-free instalments over eight years the backdated liability, reducing the amount the businesses have to pay up front by 87.5%. I do not think I have data though about the extent to which port owners have stepped in to help. Anecdotally, I suspect that the extent to which that has happened is very modest, if at all, but I do not have data on it.

Q512 Chairman: Okay, but have ministers been involved in exploring options for a fairer distribution of the liability between occupiers and owners?

Mr Timms: That is clearly a matter between the ports and their tenants. As you know, it is the Department for Communities and Local Government that has been dealing with—

Q513 Chairman: Yes, I know that, but what is the answer to the question? Have ministers been involved in exploring options for a fairer distribution between owners and occupiers?

Mr Timms: I am not aware of ministers having been involved in that, but, as I say, it would be a matter, I think, for the landlords and their tenants rather than for ministers.

Q514 John Thurso: If I can turn to the Office of Government Commerce, the NAO recently warned that public projects worth approximately £200 billion are at risk because the Government lacks the commercial skills to deliver them. They also said that the OGC lacked a performance management system to measure the success of its individual initiatives. Given that they have been going for a decade now, is this not rather a disappointing assessment?

Sarah McCarthy Fry: I think we are moving forward with the Office of Government Commerce. We have completed our first wave of procurement capability reviews as we move towards professionalising the procurement service, and certainly our new chap who is in charge of the Office of Government Commerce—his name has totally escaped me⁸—I have met and I am very impressed with how he is taking the department forward, and, of course, he brings a great deal of private sector expertise into this. We have some challenging targets for them to meet with collaborative procurement, but I do think there is a lot that we can do and a lot that we have achieved so far.

⁸ Note by witness: Nigel Smith

Q515 John Thurso: The whole point of OGC is to make procurement more effective and that is why it was dreamt up ten years ago. Do you not find it rather bizarre that an organisation that was created specifically for that purpose lacks the performance management systems to measure the success of its initiatives, and is that not the very core of what it ought to be doing?

Sarah McCarthy Fry: Except that we are getting those performance management processes in place and we are starting to see the savings now coming through. We have got a self-assessment tool that is being used which is highly objective and validated through—

Q516 John Thurso: How does that tool work?

Sarah McCarthy Fry: It is an assessment tool that is validated through an assurance process, and then that can escalate from the head of procurement out into the departments, and we have got four procurement transformation managers now in the OGC team so that we can take that out into the departments.

Q517 John Thurso: Are four enough for the whole job that is before Government in improving?

Sarah McCarthy Fry: It is rolling out into departments so that we can make sure that every department is picking up on that. We have got our first government-wide agreement on the priority policies that are going through public procurement to move out beyond the first things that we have picked up, and we are looking at the reduction of barriers to SME engagement in public procurement, promoting skills, creating apprenticeships, resource efficiency, fitting in carbon reduction and a supplier charge, so we are moving beyond just using procurement to save money, which, obviously, is the main objective on this collaborative procurement. We are looking at in what other ways we can use the power of public procurement for our objectives.

Q518 John Thurso: Those are many and various soft initiatives. The core of what it does is to procure more effectively and efficiently, which means better value, which is either better quality for the same price or the same quality for a lower price. What specific targets and measures would you put in place or are you putting in place to ensure that that is what they deliver?

Sarah McCarthy Fry: We have already delivered in our report £900 million of savings against the target of £700 million. There has been a lag in getting the full data. We have since revised upwards to £1,400 million of savings we have achieved. We do believe we are on course for our £4 billion spending review 2007 target, so I think we can demonstrate that we have put the progress in there. We have got the operational efficiency programme and the collaborative procurement is delivering the savings that we need, and five of our strands are currently out-performing their targets or are on target. We have got three under-performing which we are going to concentrate on, which are ICT, Travel and Office Solutions, and then we are going out on strategies

that deliver to the wider public sector where 70% of the spend takes place, so we are making sure that it is across the whole of government spend.

Q519 John Thurso: Can I turn to the Crown Estate? I think that is yours as well, is it not?

Sarah McCarthy Fry: Yes.

Q520 John Thurso: What discussions have you had with the Crown Estate regarding seabed leasing for renewable energy offshore?

Sarah McCarthy Fry: We manage the Crown Estate at arms length, as I am sure you are aware. The Crown Estate does keep the Treasury informed regularly—

Q521 John Thurso: But have you had any discussions with them on that subject?

Sarah McCarthy Fry: We have not had discussions. There has been some correspondence around it but mainly it is within their remit. It is their remit to deliver best value for the taxpayer.

Q522 John Thurso: So the Treasury has not discussed licensing of renewable energy seabed leases with the Crown Estate?

Sarah McCarthy Fry: That is for the Crown Estate to manage. They have to deliver within their remit to us.

Q523 John Thurso: Have you had any discussions with DECC regarding the Crown Estate's role in licensing of offshore?

Sarah McCarthy Fry: I personally have not. I am not aware if any officials have but I can certainly find out.

Q524 John Thurso: And what discussions have you had with the Secretary of State for Scotland, bearing in mind that there are two Secretaries of State who have the power to direct, namely, the Chancellor and the Secretary of State for Scotland? Have you had any discussions on this matter with him?

Sarah McCarthy Fry: I personally have not had discussions with the Secretary of State for Scotland but I am sure that the Chief Executive of the Crown Estate has.

Q525 John Thurso: I am sure he has too but I am more interested in whether you have.

Sarah McCarthy Fry: I personally have not, no.

Q526 John Thurso: In fact, I know he has had discussions but I am more interested in whether the Treasury has. The Government's White Paper requires there to be 33 gigawatts of offshore energy, mostly through offshore wind but some through tidal energy, by a date into the 2020s. That is equivalent to half the installed capacity of the United Kingdom's generation of energy. Do you not find it extraordinary that as the department that is charged with oversight of the Crown Estate, who are the people who are going to license this, you have had no discussions with them on how they are going to license Britain's energy future?

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Sarah McCarthy Fry: As I said, the Crown Estate are managed at arm's length and we know that they are trying to build their board so that they have the expertise on there to be able to deliver to the Treasury their remit, to manage the Estate to deliver a return, which is an agreed return, but also to do it in a sustainable manner.

Q527 John Thurso: The reason I ask these questions is that I was given to understand in informal discussions with DECC that they had tried to see the Crown Estate and had a very unsatisfactory brush-off on the grounds that they report to you and not to them, so I was just interested to know whether you had actually had any discussions and it would seem that perhaps there have not been any.

Sarah McCarthy Fry: As I say, I personally have not but I will find out whether officials have.⁹

Q528 John Thurso: Do you intend in the future to keep a closer eye on what they are doing?

Sarah McCarthy Fry: I think this is an area that it is important to keep track of, particularly as they are responsible for the offshore areas, and I think it is something that will get a greater focus.

Chairman: Let us turn to National Savings.

Q529 Mr Brady: Can I ask what NS&I's top priority for the future should be? Is it there to provide value for its customers or to support government macroeconomic policy?

Sarah McCarthy Fry: The sole aim of NS&I is to reduce cost to the taxpayer of Government borrowing now and in the future, and they do that through the sale of savings and investment products to the retail market.

Q530 Mr Brady: So it is not there for its customers; it is there for Government macroeconomic policy?

Sarah McCarthy Fry: That is the purpose of it, and, obviously, if they can help their consumers and their customers—they do not set out to be the absolute best buy, so in that sense they are not setting out to attract the customers. Their aim is to reduce the cost to the taxpayer of Government borrowing.

Q531 Mr Brady: And was it right for NS&I to stop discretionary marketing during the flight to safety?

Sarah McCarthy Fry: Yes, I believe it was. We had targets that they had to meet. They had over-achieved those targets and it was felt right that then that should cease.

Q532 Mr Brady: And did they ask for Treasury approval before making that decision?

Sarah McCarthy Fry: Yes, I believe so.

Q533 Mr Brady: What consideration was given to the possibility of going further and stopping taking deposits at that point?

Sarah McCarthy Fry: I am not aware that that was considered.

Q534 Mr Brady: How are you monitoring NS&I's performance now that they have suspended the value-add indicator?

Sarah McCarthy Fry: As I say, they have already over-achieved against their target, so now it is just a question of monitoring to ensure that they fit within the market place as they had intended, not to be right at the top.

Q535 Mr Brady: There is no other performance indicator expected of them?

Sarah McCarthy Fry: Not to my knowledge.

Q536 Mr Brady: Can you look into that?

Sarah McCarthy Fry: I will get back to you on that.¹⁰

Mr Brady: Thank you.

Q537 Peter Viggers: The Government announced in the Budget of 2007 that public sector accounts would be prepared in accordance with International Financial Reporting Standards, IFRS, with effect from 2008–09, but there was some slippage and the reason for the slippage was given to us as “uncertainties around the impact of the introduction of IFRS on public sector net debt”. There has been further slippage. The Department of Health and the Ministry of Defence have negotiated exemption from trigger points and we have been critical of that and said that the adoption of International Financial Reporting Standards will fail if the Treasury does not assert its authority and aid departments in meeting the agreed milestones. How high a priority for you is the implementation by government departments of IFRS?

Sarah McCarthy Fry: I think it is important that we move to International Financial Reporting Standards; it is a priority for us, and we have made steady progress against the 32 trigger points. I believe that Louise Tulett advised the Committee that 41 out of 43 departments have now met the deadline for the September accounts to be in to the NAO. We are taking stock of the progress against that and we are moving forward, and it is a priority that we move towards the standards.

Q538 Peter Viggers: The two non-compliant departments presumably being Health and Defence?

Sarah McCarthy Fry: I am not where which the two are but we are working closely with them.

Q539 Peter Viggers: When the Government does become fully compliant more PFI deals will have to be put onto the balance sheet. What estimate have you made of the impact on the Government's net debt figure?

Sarah McCarthy Fry: A lot of PFI deals, of course, already are on the balance sheet and I think the newer ones coming on are on there. I do not have a figure but I can certainly write to the Committee.

Q540 Peter Viggers: Have you allowed IFRS to slip because you do not wish to publish the larger debt figures?

⁹ Ev 111

¹⁰ Ev 112

Sarah McCarthy Fry: Absolutely not. It is still a priority that we move towards the IFRS. It is what we set out to do.

Q541 Peter Viggers: What assessment have you made of the impact on the Government's net debt figure of full compliance?

Sarah McCarthy Fry: I do not have those figures to hand. I will write to the Committee about that.¹¹

Peter Viggers: It would be helpful to have that estimate. Thank you.

Q542 Chairman: When will we see finally the Whole of Government Accounts?

Sarah McCarthy Fry: We have said that the 2009–10 accounts will be prepared on a Whole of Government Accounts basis.

Q543 Chairman: So we will see them in July; is that right?

Sarah McCarthy Fry: For 2009–10.

Q544 Chairman: For 2009–10, so we will see them in July 2010?

Sarah McCarthy Fry: That is the plan and we are on course to do that.

Q545 Chairman: So the current year's accounts will be Whole of Government Accounts, is that right? We will see them next July?

Sarah McCarthy Fry: Yes. We are currently in 2009–10. The NAO, as you know, have reviewed the dry run that we did and there are still some issues outstanding.

Q546 Chairman: You are going to exclude the part-nationalised banks, is that not right?

Sarah McCarthy Fry: That is right. They are not going to be consolidated within the Whole of Government Accounts.

Q547 Chairman: How will that impact on the NAO's opinion?

Sarah McCarthy Fry: That will be a matter for the NAO.

Q548 Jim Cousins: I would like to clarify a factual question; I am not trying to bowl some kind of googly here. The Committee has been concerned about what proportion of the assets covered by the Asset Protection Scheme, which now, of course, and in the future will only apply to RBS, represented assets outside the UK. Yesterday I believe a figure of 60% was given for that, that 60% of the assets being protected are outside the UK. I would be grateful if that figure could be properly confirmed. It is obviously of some importance to get the facts right, but I am not expecting an answer right now.

Sarah McCarthy Fry: We will write to you on that.¹²

Q549 Ms Keeble: May I ask a final question on the child poverty figures? I understand that the figures that were provided at the time of the 2007 Budget were that 180,000 families were to be gainers in 2009–10 and then 350,000 in 2010–11. Presumably the numbers have slipped a bit because of the month later starting date, but in our brief we have got a figure of 200,000 working families. Where did that come from and what are the accurate figures, particularly given the later starting date?

Mr Timms: These are the figures relating to the housing benefit change?

Q550 Ms Keeble: Yes.

Mr Timms: I am afraid I do not have those in front of me but I would be very happy to take that question away and provide a note.

Q551 Ms Keeble: Could you, because there are two things? One is clearly how they are going to impact on the 2010 target. If the original figure given was 180,000 and then 350,000 but the scheme starts a month late because it was due to start from the beginning of October and in fact started on 2 November and you have given us a figure of 200,000, there are real discrepancies about what is happening. I am concerned about the lack of rigour in some of the figures around all of this on what is obviously a very important target.

Mr Timms: The reassurance I can provide is that the data when it is compiled for how many children have been lifted above the poverty line will be very rigorous, but I take your point that this change could be one of the influences on that outcome.

Q552 Ms Keeble: It was the only one that was left out of the three announced in the 2007 Budget. We have seen all the others come through. This is the only one which is going to start getting things heading in the right direction.

Mr Timms: But those other measures have not yet been reflected in the figures. As I said earlier, the latest figure we have is half a million children lifted above the poverty line. Measures we have taken since that measurement was made we believe will lift an additional half million above the line.

Q553 Ms Keeble: This was the biggest one.

Mr Timms: That clearly could have an impact and I will come back to the Committee with a note on that.¹³

Q554 Chairman: Just a final question from me. Last year we expressed concern that the Treasury itself had underspent on its spending limit for the sixth consecutive year. Now we find you have underspent for the seventh consecutive year by £22 million or 10% of your budget. What do you intend to do with the end-year flexibility you have accumulated with this repeated underspending?

¹¹ Ev 112

¹² Ev 113

¹³ Ev 106

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Sarah McCarthy Fry: Obviously, we will look at it in the light of the requirements that we have coming forward. We try and manage our estimates the best we can and we always put in the resource accounts the reasons for the underspend, and I think it varies from year to year.

Q555 Chairman: But it always varies the same way is what concerns this Committee. You are persistently underspending and the Permanent Secretary told us that he was frustrated by that, so what are you doing about it?

Sarah McCarthy Fry: As I say, we do try and match our estimates to our resources as best we can. This year it was caused by a higher than expected income. Last year it was caused by lower than expected costs, so we are doing our best to try and manage it. Obviously, it is in everyone's interests if it is more accurate.

Q556 Chairman: Have you changed end of year flexibility policy for the other government departments?

Sarah McCarthy Fry: Not to my knowledge, no.

Q557 Chairman: Because the NAO reported that several of the other departments had rather lost confidence in the system. They were not clear about end-year flexibility.

Sarah McCarthy Fry: If they are not clear then I am sure we will make it clear to them. If that is the reporting I was not aware of that. Could I just clarify on the Whole of Government Accounts that it was quite right to say that the nationalised banks are not consolidated. However, our investment is accounted for in our own Treasury Resource

Accounts which obviously then form part of the Whole of Government Accounts. It is just that they will not be consolidated in there.

Q558 Chairman: So they will appear in the Whole of Government Accounts?

Sarah McCarthy Fry: But not consolidated into them.

Q559 Chairman: Is that not the point of Whole of Government Accounts? Is not consolidation the whole point?

Sarah McCarthy Fry: Yes, but the point we make is that we do not consider the nationalised banks to be appropriate to be consolidated into the Whole of Government Accounts.

Q560 John Thurso: Presumably that means you will be showing the acquisition costs in the balance sheet rather than consolidating it so you have a cost. Will you mark that to market and show it?

Sarah McCarthy Fry: Yes, it will be marked to market.

Q561 John Thurso: So how will you account for the loss?

Sarah McCarthy Fry: That is a very good question.

Q562 John Thurso: Will you run that through the P&L or other resource account as a resource expended?

Sarah McCarthy Fry: I will have to go back to the technical experts and ask them about that one.¹⁴

Chairman: That is fair enough. You have offered us a number of notes this morning. We will need those by Christmas, please, because we have to report on all of this in the new year. In the meantime, thank you very much for your attendance today.

¹⁴ Ev 113

Written evidence

Spring Supplementary Estimates Memorandum 2008–09 submitted by HM Revenue and Customs

INTRODUCTION

The HMRC spring supplementary for 2008–09 seeks the necessary resources and cash to support the functions of the Department.

The purpose of this memorandum is to provide the select committee with an explanation of how the resources and cash sought in the spring Supplementary Estimate will be applied to achieve Departmental Strategic Objectives. This includes information on comparisons with the resources provided in earlier years in Estimates and departmental budgets. Details of changes in resources relative to original plans set out in the last Spending Review are provided.

During this spring round, the increases in provision sought in this Supplementary Estimate relate primarily to:

- £62,500,000 near-cash drawdown of the Modernisation fund (Resource DEL).
- £13,000,000 drawdown of the Modernisation Fund (Capital DEL).

An explanation of key terms used in the memorandum is provided as an annex.

SUMMARY OF THE MAIN SPENDING CONTROL FIGURES CONTAINED IN THE ESTIMATE VOTED PROVISION

The Supplementary Estimate provides a 3.3% increase in voted Net Resources and a 4.6% increase in the Net Cash requirement:

— Increase in the Net Resource Requirement (NRR) of	£514,892,000;
RfR1	£172,248,000
RfR2	£2,644,000
RfR5	£340,000,000
— Increase in the Net Cash Requirement (NCR) of	£723,559,000

BUDGETARY DATA

The changes to key budgetary figures are:

Resource Departmental Expenditure Limit increased by **£62,248,000**

The increase in resource DEL results mainly from a near-cash drawdown of the Modernisation Fund.

Capital Departmental Expenditure Limit increases by **£13,000,000**

This increase is due to drawdown of capital from the Modernisation Fund.

Annually Managed Expenditure **£452,644,000**

This increase is due to a £315,000,000 increase to the Child Benefit forecast, a £10,000,000 increase to the Child Trust Fund forecast, and a £15,000,000 increase to the Health in Pregnancy Grant forecast. There have also been increases of £22,644,000 to the revaluation losses forecast and an increase of £90,000,000 to the e-filing incentive payment forecast. Of the £22,644,000, RfR1 contains £20,000,000 within the same section as e-filing incentive payments in the Part II table of the Estimate.

DETAILED EXPLANATION OF CHANGES IN PROVISION SOUGHT IN THE SUPPLEMENTARY ESTIMATE, AND IMPLICATIONS FOR BUDGETS

<i>Amount</i>	<i>Description</i>
	<i>Movements in provision related to DEL</i>
	<i>Draw down of Modernisation Fund</i>
£75,500,000	Draw down of resources from a modernisation fund of £62,500,000 resource and £13,000,000 capital to support costs for various programmes supporting the modernisation of the Department. The following programmes are the recipients: Workforce Change Estates Consolidation Government Banking Modernising PAYE Processes for the Customer (MPPC) Carter Programme Enterprise Infrastructure Foundation Programme

<i>Amount</i>	<i>Description</i>
	<p>More details follow:</p> <p>The <i>Estates Consolidation Programme</i> will create a modern working environment rationalising areas where HMRC occupies multiple properties to create strategic zones. Several buildings have and are in the process of being optimised which means that HMRC will alter the property to maximise the potential and space these buildings have to offer;</p> <p><i>Workforce Change</i> aims to put in the right people with the right skills into the right places. On current plans around 700 staff will be released this financial year through AER. We are also looking to fund low cost FES release schemes and other initiatives such as Assisted Home Moves and Public Sector Releases.</p> <p><i>MPPC</i> will be predominantly complete by autumn 2010 and is aiming to modernise the existing 14 regional databases for PAYE records and replace them with a single integrated system encompassing workflow based on the NIRS platform which meets the latest security standards.</p> <p><i>The Government Banking Programme</i> is HMRC's solution to the Bank of England's decision to withdraw from the retail banking market. The projects under this banner will provide an integrated banking service for Departments and other public bodies. During 2009 HMRC will be moving its banking business from its existing bankers to the Royal Bank of Scotland (RBS) and Citibank;</p> <p><i>The Carter Programme</i> has arisen as a result of Lord Carter's review of online services and will deliver more online capacity around the major heads of duty. The Modernisation Fund monies will be spent on 3 discrete projects within the Programme: Carter VAT; Carter Corporation Tax; PAYE In-Year forms (P45, P46 online). As part of the next phase of the Carter changes the Carter VAT project has been launched and is aiming to deliver a Local Test Service in April 2009 as the first step towards mandation of online filing by VAT traders in April 2010. In addition, the Carter Corporation Tax project has launched and will deliver a Local Test Service in February and a Third Party Validation Service for software vendors in April 2009;</p> <p>The <i>Enterprise Infrastructure Foundation Programme</i> is investing in more modern technology to improve the efficiency of HMRC's IT estate. (RfR1: subhead A1)</p>
	Transfers to Other Government Departments
–£252,000	Transfer to the Department for Innovation, Universities & Skills in respect of the Skills Strategy for Government. (RfR1: subhead A1)
£75,248,000	Total change in provisions related to DEL
	<i>Movements in provision related to AME</i>
	Changes in AME
£340,000,000	Increases to the Child benefit, Child Trust Fund and Health in Pregnancy Grant forecasts of £315,000,000, £10,000,000 and £15,000,000 respectively. (RfR5: subhead A3, B3, C3)
£2,644,000	Increase of £2,644,000 to the revaluation of losses forecast (RfR2: subhead B2)
£90,000,000	Increase of £90,000,000 for e-filing incentive payments to bring funding in line with expected levels of payments. (RfR1: subhead B3)
£20,000,000	Increase to forecasts of £20,000,000 for annual impairment reviews which are required as part of our accounting policy. (RfR1: subhead B2)
£452,644,000	Total changes in provisions related to AME
	<i>Movements in provision neutral in budgets</i>
	Transfer from non-voted DEL (Departmental Unallocated Provision)
£3,648,000	Draw down of non-voted Capital DUP of £3,648,000 taken up as voted provision to facilitate improvements to key activities, primarily on lockable storage. (RfR1: subhead A7)
£3,648,000	Total change from the take up of DUP

<i>Amount</i>	<i>Description</i>
Changes in operating appropriations-in-aid (fully offset by changes in spending)	
£65,204,000	An increase in near-cash admin receipts of £25,756,000 largely in respect of a compensation payment, and an increase in near-cash programme receipts of £39,448,000 in respect of National Insurance activity, due mainly to improved procedures in the identification of costs. These are matched by a commensurate increase in expenditure. (RfR1, RfR2: subhead A5)
£65,204,000	Total change in operating appropriations-in-aid
<i>Changes to net cash requirement</i>	
£723,559,000	This increase is made up of all entries within the “Movements in provision related to DEL and AME” sections above, plus adjustments to remove non cash items and to add in movements in creditors and use of provisions. The main factors are the utilisation of provisions for Child Trust Fund payments and forecast decreases in creditor balances.
<i>Increases in Consolidated Fund Extra Receipts</i>	
Income	
£68,000,000	This increase in “Other amounts collectable on behalf of the Consolidated Fund” is mainly due to new penalty regimes creating additional income.
Receipts	
£14,000,000	This increase in “Other amounts collectable on behalf of the Consolidated Fund” is mainly due to new penalty regimes creating additional receipts. The figure is lower than the income reported above due to the time lag between raising penalty charges and collecting them.

Impact on Departmental Strategic Objectives

Objective I:- Improve the extent to which individuals and businesses pay the amount of tax due and receive the credits and payments to which they are entitled.

£75,500,000 Modernisation Fund

Draw down of admin near-cash from the ring- fenced modernisation fund of £62,500,000 resource and £13,000,000 capital to support our transformational programmes and projects.

Objective II: -Improve customer experience, support business and reduce the compliance burden.

£75,500,000 Modernisation Fund

As detailed in Objective 1.

Objective III: -To strengthen frontier protection against threats to the security, social and economic integrity and environment of the United Kingdom in a way that balances the need to maintain the UK as a competitive location in which to do business.

DEPARTMENTAL EXPENDITURE LIMIT

This Supplementary Estimate will result in an overall increase in Capital DEL of £13,000,000, and an overall increase in Resource DEL OF £62,248,000. Details of DEL in Estimates are:

<i>£ '000s</i>	<i>Voted</i>	<i>Non-voted</i>	<i>TOTAL</i>
<i>Resource DEL</i>			
Main Estimate	3,975,044	391,401	4,366,445
Winter Supplementary Estimate	4,082,544	347,739	4,430,283
Spring Supplementary Estimate	4,144,792	347,739	4,492,531
<i>Capital DEL</i>			
Main Estimate	257,366	3,648	261,014
Winter Supplementary Estimate	284,866	3,648	288,514
Spring Supplementary Estimate	301,514	301,514	
<i>Revised Total DEL*</i>	<i>4,267,306</i>	<i>347,739</i>	<i>4,615,045</i>

*Depreciation, which forms part of RDEL, is excluded from total DEL since CDEL includes capital spending and to include depreciation of those assets would lead to double counting.

The table below compares outturn for 2005–06, 2006–07 and 2007–08 with planned DEL. The DEL provision for 2008–09 is also detailed in the table for comparison purposes:

<i>Year</i>	<i>Voted</i>	<i>Non-voted</i>	<i>TOTAL</i>	<i>Outturn £ '000s</i>	<i>Variance</i>
<i>Resource</i>					
2005–06	4,236,827	349,051	4,585,878	4,392,771	– 4.20% *
2006–07	4,271,163	347,939	4,619,102	4,574,712	– 0.96% **
2007–08	4,164,498	372,813	4,537,311	4,410,929	– 2.78% ***
2008–09	4,144,792	347,739	4,492,531		
2009–10	3,868,769	389,724	4,258,493		
2010–11	3,765,419	388,074	4,153,493		
<i>Capital</i>					
2005–06	374,269	2,977	376,635	377,889	+ 0.33% *
2006–07	338,331	0	338,331	305,613	– 9.67% **
2007–08	288,230	3,739	291,969	260,427	– 10.80% ***
2008–09	301,514	0	301,514		
2009–10	250,955	3,559	254,514		
2010–11	244,642	3,472	248,114		

The Resource DEL outturn for 2007–08 of £4,410,929 represents an underspend of £126,382 compared to a final provision of £4,537,311k (equivalent to 2.78 per cent of Resource DEL). This was mainly attributable to Departmental Transformation Programme and general administrative underspends including paybill. The Capital DEL Outturn for 2007–08 of £260,427k compares against a final provision of £291,969k. The underspends primarily relate to Information Technology.

* Removes baseline transfer and costs associated with a machinery of government change to SOCA in 2006–07. The outturn figure has been taken from the HMRC Spring Report.

** Figures are those published in the Public Expenditure Outturn White Paper published in July 2007 (CM7156).

*** Figures are those published in the Public Expenditure Outturn White Paper published in July 2008 (CM7419).

DEL End-Year Flexibility

The 2007–08 EYF stock for HMRC was reported in the Public Expenditure Outturn White Paper 2007–08 (PEOWP) (Cm 7419). The breakdown below shows changes since the 2006–07 PEOWP (CM7156).

<i>£'000</i>	<i>Admin Resource</i>	<i>Other Resource</i>	<i>Total</i>	<i>of which: Near-cash</i>	<i>Non-cash</i>	<i>Capital</i>
PEOWP (July 2007)	61,825	63,106	124,931	155,790	– 30,859	33,257
Take-up in Winter Supplementary Estimate	–	1,400	1,400	1,400	–	–
Balance of EYF After Spring Supplementary Adjustments To PEOWP July 2007	61,825	61,706	123,531	154,390	– 30,859	33,257
PEOWP (July 2008)	63,325	60,206	123,531	123,531	35,552	–
2007–08 Underspend	144,432	– 18,050	126,382	62,289	31,202	–
Reductions For Virement Out of Admin Budgets	– 18,050	18,050	–	–	–	–
Reductions for Reserve Claims	– 30,000	–	– 30,000	– 30,000	–	–
Other Adjustments	299	–	299	299	–	–
2008–09 Entitlements	160,006	60,206	220,212	156,119	66,754	–

Administration Budget

The Supplementary Estimate will increase the administration budget by £62,248,000 to £4,392,050,000. A comparison with earlier years (outturn) and plans is set out below.

Administration budget (previous years)

Year	Plans	Outturn
2005–06 *	4,447,899	4,246,352
2006–07 **	4,523,493	4,496,817
2007–08 ***	4,441,607	4,297,275

During 2005–06 an underspend was generated mainly as a result of the de-scoping and deferral of some projects following a review of our change portfolio.

For 2006–07 there was a small voted underspend. An excess level of receipts was added to this, which led to a surplus of £26,676k for EYF purposes.

The 2007–08 underspend of £144,332k mainly relates to Departmental Transformation Project and general administrative underspends including paybill.

*Removes baseline transfer and costs associated with a machinery of government change to SOCA in 2006–07. The outturn figure has been taken from the HMRC Spring Report.

**Figures are those published in the Public Expenditure Outturn White Paper published in July 2007 (CM7156).

*** Figures are those published in the Public Expenditure Outturn White Paper published in July 2008 (CM7419).

The changes to the current year's Administration Budget are:

Changes to administration budget in 2008–09

1 April 2008 at Main Estimate	4,265,924
Change announced in winter supplementary	63,878
Change announced in spring supplementary	62,248
Revised Administration Budget	4,392,050

Administration budget (remaining CSR years)

Year	Plans
2009–10	4,159,572
2010–11	4,055,972

Machinery of Government Changes

There are no changes resulting from Machinery of Government.

Description	RfR and section	Date of transfer	Amount £000	Transferring Dept	Receiving Dept
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Approval of Memorandum This memorandum has been prepared with reference to guidance in the *Estimates Manual* provided by HM Treasury and that found on the House of Commons, Scrutiny Unit website. The information in this memorandum has been approved by the Chief Executive Officer of HMRC.

Glossary of Key Terms

Appropriations-in-aid—income received by a department which it is authorised to retain (rather than surrender to the Consolidated Fund) to finance related expenditure. Such income is voted by Parliament in Estimates and accounted for in departmental resource accounts.

Administration Budget—a Treasury control on the resources consumed directly by departments in providing those services which are not directly associated with frontline service delivery. Includes such things as: civil service pay, resource expenditure on accommodation, utilities and services. The Administration Budget is part of Resource DEL.

Annually Managed Expenditure (AME)—a Treasury budgetary control for spending that is generally difficult to control, large as a proportion of the department's budget, and volatile in nature.

Departmental Expenditure Limit (DEL)—a Treasury budgetary control for spending that is within the department’s direct control and which can therefore be planned over an extended (Spending Review) period (such as the costs of its own administration, payments to third parties, etc).

Departmental Unallocated provision (DUP)—a part, usually between 1% and 1.5% of a department’s total DEL that is not allocated to particular spending, but held back by the department to meet unforeseen pressures.

End Year Flexibility (EYF)—a mechanism whereby departments are allowed to carry forward unspent DEL provision into later years.

Estimates—a statement of how much money government needs in the coming financial year, and for what purposes, by which Parliamentary authority is sought for the planned level of expenditure and receipts in a department.

Estimates Memorandum—an explanation to the relevant department’s select committee setting out the links to other spending controls and the contents of a department’s Estimate.

Near-cash—resource expenditure that has a related cash implication, even though the timing of the cash payment may be slightly different. For example, expenditure on gas or electricity supply is incurred as the fuel is used, though the cash payment might be made in arrears on a quarterly basis.

Non-cash—costs where there are no cash transactions but which are included in the body’s accounts (or taken into account in charging for a service to establish the true cost of all resources used).

Request for Resources (RfR)—a function based description of the organisational level of the department. These can vary between one or more RfR and should be objective- based, referring to the purpose for which the functions being carried out by the department are intended to meet.

Revised Spring Supplementary Estimates Memorandum 2008–09 submitted by HM Treasury

1. This memorandum provides details of changes sought in the Treasury’s Revised Spring Supplementary Estimate for 2008–09 published in “Central Government Supply Estimates 2008–09: Revised Spring Supplementary Estimates” HC265. Further details of the work of the Treasury and its finances can be found in the “HM Treasury Annual Report and Accounts 2007–08” CM 7048. Supply Estimates and the Treasury’s Departmental Report are available from www.hm-treasury.gov.uk

2. The purpose of this memorandum is to provide the select committee with an explanation of how the resources and cash sought in the Spring Supplementary Estimate will be applied to achieve departmental objectives and Public Service Agreement (PSA) targets. This includes information on comparisons with the resources provided in earlier years in Estimates and departmental budgets. The Revised Supplementary Estimate is being taken to include provision for the cost of capital on the Treasury’s financial investments and loans.

SUMMARY OF THE CHANGES SOUGHT IN THE ESTIMATE

3. The Estimate seeks an increase of £20,745,496,000 in net resources and an increase of £4,102,071,000 in the net cash requirement. The increase in resources is the net effect of transfers to and from other Government departments and the draw down of the balance of our administration Departmental Unallocated Provision (DUP) and programme DUP. The increase in the net cash requirement comprises the near cash consequences of the net resource increase above plus capital payments in respect of financial institutions.

DETAILED EXPLANATION OF THE CHANGES BEING SOUGHT

Request for Resources 1: *Raising the rate of sustainable growth and achieving rising prosperity and a better quality of life, with economic and employment opportunities for all*

4. The increase in resources is the net effect of the following:

Inter-departmental transfers

5. A transfer to the Department for Innovation, Universities and Skills (DIUS) of £17,000 administration costs as a contribution towards the implementation costs of the Skills Strategy for Government.

Movements between RfRs

6. There is an increase of £2,450,000 administration costs for core Treasury following the transfer of £250,000 from RfR 2 outlined at paragraph 158 below, and £2,200,000 from RfR 3 as outlined at paragraph 23.. This increase is to fund increased spending in connection with financial stability.

Departmental Unallocated Provision

7. There is a draw down of administration DUP of £3,106,000 and £1,025,000 for programme DUP to fund increased spending in connection with financial stability (administration) and spending on financial inclusion (programme) for core Treasury. DMO administration spending is increasing by £420,000 and programme spending by £800,000, funded by draw down of DUP, to cover new administration activities, mainly the Credit Guarantee Scheme, and increased programme spending due to increased brokerage and transaction costs.

Increased spending offset by income

8. Income for core Treasury in Section A is forecast to increase by £19,490,000 to offset a matching increase in gross spending. The income arises from recharging financial institutions for the cost of advisers fees. DMO income in Section B is forecast to reduce by £487,000. This is the net effect of an increase in programme income of £300,000, mainly from increased commission from gilt purchases and sales, less a reduction of £787,000 in administration income mainly due to a forecast under-recovery of Public Works Loan Board income.

Changes in forecasts—AME

9. The cost of capital charge on the Treasury's investment in the Bank of England has been increased by £24,000,000 because of a large increase in the forecast net asset value of the Bank at 31 March 2009 due to increased profits.

Cost of capital charge on financial investments and loans

10. There is provision of £700,000,000 for the cost of capital charge on the Treasury's financial investments in banks, and associated loans, which attract a cost of capital charge of 3.5%, in accordance with the Financial Reporting Manual.

Impairment of value of fixed assets—AME

11. There is provision for impairment of fixed assets totalling an estimated £20,016,635,000. The impairment provision comprises £20,000,000,000 to reflect estimated impairments on the Treasury's financial investments and £16,635,000 in respect of the fall in the value of the 1 Horse Guards Road land and building.

Capital AME

12. The increase in capital AME of £1,195,000,000 is required for the following:

- (i) Bradford & Bingley—the forecast of the total working capital loan facility requirement for the year is £6,000,000,000, which reflects an increase of £265,000,000 over the £5,735,000,000 included in the winter Supplementary Estimate.
- (ii) London Scottish Bank—an increase of £265,000,000 to finance a loan to the Financial Services Compensation Scheme (FSCS) in respect of payments to depositors in London Scottish. £100,000,000 will be paid in this financial year, with the balance of £165,000,000 included as a provision for payments in future years.
- (iii) Kaupthing Singer & Friedlander (KSF)—an increase of £665,000,000 to finance a loan to the FSCS in respect of payments to depositors in KSF. £135,000,000 of the total is included as a provision in respect of payments in future years.

Capital DEL

13. There is an increase in capital DEL spending of £700,000 financed from the capital DUP. The increase is to finance the latest forecast of spending on IT projects.

Request for Resources 2: *Cost-effective management of the supply of coins and actions to protect the integrity of coinage*

14. The reduction in resources is the net effect of the following:

Changes due to revised forecasts of requirements—DEL

15. The cost of the manufacturing element of coinage production is forecast to be in the region of £18.3 million, with the cost of capital on the manufacturing element of coinage stock estimated to be £100,000 programme DEL, which will be financed from the forecast underspend on coinage production. The resulting reductions in existing provision of £250,000 administration costs and £1,900,000 programme costs are being reallocated to RfR 1.

Changes due to revised forecasts of requirements—AME

16. The forecasts for the cost of capital charge on the Treasury's investment in the Royal Mint and on the metal element of coinage stocks have both been reduced, by £1,325,000 and £200,000 respectively.

Request for Resources 3: *Obtaining the best value for money from Government's commercial relationships on a sustainable basis*

17. The reduction in net resources of £1,935,000 is the net effect of the following:

Inter-departmental transfers

18. Contributions from DH and DCMS towards the costs of the Centre of Excellence in Sustainable Procurement comprising near cash administration costs of £45,000 each. The Centre of Excellence in Sustainable Procurement was created within OGC in response to the Sustainable Development Commission's 6th Annual Sustainable Development in Government (SDiG) Report.

Departmental Unallocated Provision

19. A net increase of £175,000 in programme spending to fund increases in provision for vacant leasehold properties due to increases in business rates.

Neutral changes

20. The reclassification of £45,000, from programme spending to the administration budget. The change is in respect of a transfer received in the winter Supplementary round from the UK Statistics Authority (UKSA). As the transfer was to support OGC's administration costs spending, the transfer was reclassified from programme costs to the administration budget.

21. There is an increase in gross provision of £163,000 non cash programme spending for cost of capital charge in respect of the investment in OGC.buyingsolutions, offset by a matching increase in dividend income.

Reductions

22. There is an increase in appropriations in aid within the administration budget of £1,890,000, mainly arising from sales of products, resulting in a matching reduction in net provision.

23. There is a reduction in gross administration provision of £310,000 arising from forecast underspends which, together with the £1,890,000 reduction is being reallocated to RfR 1. The total transfer to RfR 1 amounts to £2,200,000.

THE NET CASH REQUIREMENT

24. The increase in the net cash requirement amounts to £4,102,071,000. This comprises the increases covered in paragraphs 5, 7, 11 and 12 plus the draw down of £3,100,000,000 of a provision taken in the winter Supplementary Estimate for payments in respect of the refinancing of Financial Services Compensation Scheme loans to Icesave.

IMPACT ON THE DEPARTMENT'S PUBLIC SERVICE AGREEMENTS

25. The increase in capital AME of £1,195,000,000 is to support stability in the financial services sector and is in line with Treasury DSO outcome DSO 2(e): "Supporting fair, stable and efficient financial markets" and with PSA 6: Deliver conditions for business success in the UK".

DEPARTMENTAL EXPENDITURE LIMIT

26. The Resource DEL is increasing by £73,000 comprising the inter-departmental transfers covered in the explanation of the changes for RfRs 3 (paragraph 18 above), less the transfer out from RfR 1 (paragraph 5). There is an increase of £700,000 in Capital DEL. The following table shows a comparison between DEL plans between 2004–05 and 2007–08 (after changes made via Supplementary Estimates) and the outturns for those years, and the DEL for 2008–09.

<i>Comparison of expenditure against Departmental Expenditure Limits</i>					<i>£million</i>	
<i>Year</i>	<i>Voted</i>	<i>Non-voted</i>	<i>Total DEL</i>	<i>Outturn</i>	<i>Variance</i>	
<i>Resource</i>						
2004–05	217	31	247	192	– 55	
2005–06	227	29	256	215	– 41	
2006–07	225	21	246	206	– 40	
2007–08	212	20	232	201	– 31	
2008–09	21	222				
<i>Of which near cash</i>	<i>189</i>	<i>31</i>	<i>221</i>			

<i>Comparison of expenditure against Departmental Expenditure Limits</i>					<i>£million</i>
<i>Year</i>	<i>Voted</i>	<i>Non-voted</i>	<i>Total DEL</i>	<i>Outturn</i>	<i>Variance</i>
<i>Capital</i>					
2004–05	8	–	8	–28	–36
2005–06	5	–5	–9	–14	
2006–07	7	–	7	–1	–8
2007–08	7	–	7	–1	–8
2008–09	6	1	7		

DEPARTMENTAL UNALLOCATED PROVISION (DUP)

27. A total of £6,313,000 has been drawn down from the DUP comprising £6,138,000 for RfR 1 and £175,000 for RfR 3.

END YEAR FLEXIBILITY

28. No EYF will be drawn down in the Spring Supplementary. The following table shows the EYF entitlements for 2008–09.

					<i>£million</i>
<i>Administration</i>	<i>Other resources</i>	<i>Total resource EYF</i>	<i>Of which near cash</i>	<i>Capital</i>	<i>Total EYF</i>
70	132	202	202	73	275

ADMINISTRATION BUDGET

29. The Administration Budget is increasing by £118,000. This is the net effect of the increases set out in the explanations for RfRs 1 and 3 plus a reclassification of £45,000 programme spending to administration costs, as set out in paragraph 20 above. The following table shows a comparison between administration budget plans between 2004–05 and 2007–08 (after changes made via Supplementary Estimates) and the outturns for those years, and the budget for 2008–09.

<i>Comparison of Administration costs against limit</i>					<i>£million</i>
<i>Year</i>	<i>Voted</i>	<i>Non-voted</i>	<i>Total</i>	<i>Outturn</i>	<i>Variance</i>
2004–05	164	0	164	149	15
2005–06	167	0	167	161	8
2006–07	167	1	168	160	8
2007–08	171	0	171	160	11
2008–09	170	0	170		

CONTINGENT LIABILITIES

30. The following changes have been made to the list of contingent liabilities, in comparison with the winter Supplementary Estimates:

- (i) The liability concerning regulation of the Lloyd's insurance market has been removed;
- (ii) The guarantee arrangements for certain retail and wholesale deposits in Northern Rock (NR) has now been quantified at up to £16,000,000,000;
- (iii) The Treasury's guarantee to the FSA concerning NR operating above the minimum regulatory capital requirement has now been quantified at up to £3,400,000,000;
- (iv) An unquantifiable guarantee by the Treasury on indemnities given by United Kingdom Financial Investments to its directors against liabilities and losses in the course of their actions, has been included;
- (v) The back-up liquidity facility for NR has now been quantified at up to £3,200,000,000;
- (vi) The guarantee given on certain wholesale borrowings and deposits with Bradford & Bingley (B&B) has now been quantified at up to £17,000,000,000;
- (vii) The liabilities in respect of Kaupthing non-Edge accounts, Heritable Bank plc, Kaupthing Singer & Friedlander Ltd and Landsbanki have been removed.

- (viii) The Treasury's indemnity on the Bank of England Special Liquidity Scheme to allow banks to temporarily swap high quality mortgage-backed and other securities for Treasury Bills has now been quantified at up to £185,000,000,000;
- (ix) An indemnity given by the Treasury to the Bank of England against losses arising from its purchase of £50,000,000 of high quality private sector assets, as outlined in a letter from the Treasury to the Treasury Select Committee dated 19 January 2009, has been included;
- (x) A contingent liability, currently unquantifiable, arising from the offer of capital and asset protection on those assets most affected by the current economic conditions, as outlined in a letter from the Treasury to the Treasury Select Committee dated 19 January 2009, has been included. We expect this to become quantifiable once further details of the scheme's operation are announced;
- (xi) A contingent liability, currently unquantifiable, arising from plans to establish a new facility guaranteeing certain asset backed securities, as outlined in the Treasury's letter to the Treasury Select Committee dated 19 January 2009, has been included; and
- (xii) A contingent liability arising from the compensation scheme established under the Bradford & Bingley plc Compensation Scheme Order 2008, has been included. This is currently unquantifiable.

February 2009

Main Estimate Memorandum 2009–10 submitted by the Government Actuary's Department

INTRODUCTION

The Government Actuary's Department Main Estimate for 2009–10 seeks the necessary resources and funding to support the continuing function of the Department which, is to provide an actuarial consultancy service to Government and other clients principally in the public sector.

The purpose of this memorandum is to provide the select committee with an explanation of how the resources provided in the Main Estimate will be applied to achieve the department's objectives.

An explanation of key terms used in the Memorandum is provided at Annex A.

SUMMARY OF RESOURCES SOUGHT IN THE MAIN ESTIMATE

The Main Estimate provides for a:

Net Resource Requirement (NRR) of £ 588,000 and;
a Net Cash Requirement (NCR) of £ 272,000.

RfRI 588,000

Budgetary data The key budgetary figures are:

Resource Departmental Expenditure Limit (DEL)	£542,000
<i>Of which:</i>	<i>£55,000</i>
<i>near cash is</i>	
<i>Administration budget is</i>	<i>£542,000</i>
DEL Capital Budget is	£217,000
Annually Managed Expenditure (AME)	£46,000

CHANGES IN PROVISION COMPARED WITH THE PREVIOUS YEAR

Net resource requirement:	2009–10	£588,000
	2008–09	£603,000

Provision is currently 2.5% lower than last year

Net cash requirement:	2009–10	£272,000
	2008–09	£272,000

The lower cash requirement reflects the lower resource requirement

Resource DEL:	2009–10	£542,000
	2008–09	£557,000
Capital DEL:	2009–10	£217,000
	2008–09	£222,000
Annually Managed	2009–10	£46,000
	2008–09	£46,000

IMPACT ON DEPARTMENT'S PERFORMANCE MANAGEMENT FRAMEWORK (PMF)

GAD does not have a PSA but it has Performance Management targets which were set as part of the CSR07 settlement. The resources being provided as part of this Main Estimate impact on the following objectives:

Objective 1. Provide actuarial advice to Ministers, Government Departments and other GAD clients in respect of employer- sponsored pension arrangements and other employee benefits; and to provide actuarial advice necessary to underpin Ministerial decision-making on general pensions policy.

Objective 2. Provide the actuarial advice necessary for the regulation and supervision of financial institutions overseas.

General Objective. To provide mainly public sector clients with independent, professional, actuarial advice of the highest quality.

DEPARTMENTAL EXPENDITURE LIMIT (DEL)

The table below compares outturn from the last few years with planned DELs for the immediate future.

	<i>OUTTURN</i>				<i>PLANS</i>	
	<i>2005-06</i>	<i>2006-07</i>	<i>2007-08</i>	<i>2008-09</i>	<i>2009-10</i>	<i>2010-11</i>
Resource DEL	(553)	263	655	557	542	528
<i>Of which Near cash</i>	<i>(967)</i>	<i>(194)</i>	<i>231</i>	<i>57</i>	<i>55</i>	<i>54</i>
<i>Of which Non-cash</i>	<i>414</i>	<i>457</i>	<i>424</i>	<i>500</i>	<i>487</i>	<i>474</i>
Capital DEL	381	178	63	222	217	212
Less Depreciation	(265)	(320)	(291)	(366)	(356)	(346)
TOTAL DEL	(437)	121	427	413	403	394

£'000s

*Depreciation, which forms part of RDEL, is excluded from total DEL since CDEL includes capital spending and to include depreciation of those assets would lead to double counting.

The RDEL Plan for 2009-10 is £542,000 and compares against a final provision in 2008-09 of £557,000. This means a decrease of £15,000 equivalent to 2.69 per cent of the RDEL. This decrease was due to an increase in planned fee income relative to expenditure.

The CDEL Plan for 2009-10 is £217,000 and compares against a final provision in 2007-08 of £222,000 indicating a decrease of £5,000 equivalent to 2.7% of the CDEL.

The 2009-10 DEL plans are consistent with Comprehensive Spending Review settlement after taking account of subsequent reclassifications of £46,000 DEL spending into AME.

END YEAR FLEXIBILITY (EYF)

The 2007-08 EYF stock for GAD was reported in the Public Expenditure Outturn White Paper 2007-08 (PEOWP) (Cm 7419). The changes since then can be seen as follows:

	<i>Admin</i>	<i>Other resource</i>	<i>TOTAL Resource</i>	<i>Of which: near cash</i>	<i>Non-cash</i>	<i>Capital</i>
GAD EYF balance from PEOWP, July 2008	139	—	139	139	—	300
Winter supp	—	—	—	—	—	—
Spring supp	—	—	—	—	—	—
Balance of EYF March 2009						

£'000

The table above presents the position of the EYF stocks following the adjustments and drawdown since the publication of PEOWP 2007-08. The department currently estimates an underspend of £183,000 for the financial year just completed. The underspend was due to client demand throughout the last financial year being higher than planned relative to expenditure. Subject to Treasury approval the resource is now expected to be used in a future year if client demand is lower than planned leaving GAD unable to cover its expenditure through client fee income. Capital has been deferred in order to finance new pensions valuation software which is critical to the business of the department. A tender exercise is currently underway to select the software.

ADMINISTRATION BUDGET

A comparison with earlier years (outturn) and plans is set out below.

	<i>£'000s</i>					
	<i>OUTTURN</i>			<i>PLANS</i>		
	<i>2005–06</i>	<i>2006–07</i>	<i>2007–08</i>	<i>2008–09</i>	<i>2009–10</i>	<i>2010–11</i>
Administration budget	– 553	263	655	557	542	528

The administration budget decreases by £ 15,000 compared with last year due to an increase in planned fee income relative to expenditure.

MACHINERY OF GOVERNMENT CHANGES

There are no Machinery of Government (MoG) changes impacting on the Estimates.

PROVISIONS

There have been no major changes in provisions since the last Estimate was presented.

CONTINGENT LIABILITIES

GAD has no contingent liabilities.

APPROVAL OF MEMORANDUM

This Memorandum has been prepared by reference to guidance in the Estimates Manual provided by HM Treasury and that found on the House of Commons, Scrutiny Unit website.

GLOSSARY OF KEY TERMS**DEPARTMENTAL EXPENDITURE LIMIT (DEL)**

This is spending within the Department's direct control and which can therefore be planned over an extended period, such as the costs of its own administration, payments to third parties, etc.

ANNUALLY MANAGED EXPENDITURE (AME)

AME spending is generally less predictable and controllable than expenditure in DEL.

REQUEST FOR RESOURCES (RfR)

A Request for Resource is a function based description of the organisational level of the department. These can vary between one or more RfR and should be objective based, referring to the purpose for which the functions being carried out by the department are intended to meet.

SUBHEADS AND SECTIONS

Subheads and sections are lines within RfRs that detail the functions that the department is carrying out in pursuit of its objective. For example, subhead A1 is frequently 'Administration' in many departmental Estimates.

DEPARTMENTAL UNALLOCATED PROVISION (DUP)

A contingency reserve, which the department accesses, where necessary, by means of a Supplementary Estimate.

END OF YEAR FLEXIBILITY (EYF)

A mechanism that enables the Department to plan the use of resources over Spending Review years and therefore carry forward unspent provision in the Departmental Expenditure Limit (DEL) in one year to subsequent years.

VOTED AND NON-VOTED

Voted expenditure is that which has gone through the Supply Estimates process. Non-voted, as its description suggests, has not been through this process. It usually refers to expenditure that comes from another source eg consolidated fund standing services.

Estimates Memorandum Submitted by HM Revenue and Customs

INTRODUCTION

The HMRC Main Estimate for 2009–10 seeks the necessary resources and cash to enable the Department to meet its objectives for the coming year. This year, the core Department will be transferring its frontiers activity to the UK Border Agency (subject to the enactment of appropriate legislation). Additionally, the Valuation Office Agency will be taking on work of The Rent Service, which was previously held by the Department for Work and Pensions (DWP).

The purpose of this memorandum is to provide the select committee with further information on the main issues the Department will be dealing with over the coming year, it emphasises the Department's focus and sets out how HMRC will achieve its strategic objectives. This also includes comparisons with the resources provided in earlier years.

An explanation of key terms used in the memorandum is provided as an annex.

SUMMARY OF THE MAIN SPENDING FIGURES CONTAINED IN THE ESTIMATE

VOTED PROVISION

The Main Estimate provides for a:

- total Net Resource Requirement (NRR) of £16,454,336,000
 - RfR 1 £3,978,435,000
 - RfR 2 £1,000
 - RfR 3 £158,000,000
 - RfR 4 £32,900,000
 - RfR 5 £12,285,000,000
- Net Cash Requirement (NCR) of £16,407,454,000

BUDGETARY DATA

The key budgetary figures are:

Resource Departmental Expenditure Limit	£4,258,156,000
<i>Of which:</i>	
<i>Near-cash</i>	£3,960,122,000
<i>Administration budget</i>	£4,159,275,000
Capital Departmental Expenditure Limit	£254,714,000
Annually Managed Expenditure (Resource)	£32,045,903,000
Annually Managed Expenditure (Capital)	£370,000,000

EXPLANATION OF SIGNIFICANT CHANGES IN PROVISION COMPARED WITH THE FINAL SPRING SUPPLEMENTARY PROVISION FOR 2008–09

Net resource requirement:	2009–10	£16,454,336,000
	2008–09	£16,113,339,000

The total net resource sought for 2009–10 is 2.1% higher than the final net provision for 2008–09. The higher overall net resource requirement is due to increases in operational AME expenditure mainly in respect of Child Benefit payments. The 2007 Comprehensive Spending Review settlement for HMRC reduced total DEL by an average annual real reduction of 4.9% on its 2007–08 baseline. This excluded Modernisation Funds which are agreed separately.

Net cash requirement:	2009–10	£16,407,454,000
	2008–09	£16,292,835,000

The total net cash requirement for 2009–10 is 0.7% higher than the 2008–09 requirement, mostly relating to the AME increases mentioned above. Non-cash requirements cover depreciation (£175 million), cost of capital (£37 million) and provisions (£120 million).

DEL PROVISION:

	2009–10	2008–09	Decrease 2009–10 compared to 2008–09
Resource DEL	£4,258,156,000	£4,492,531,000	(5.2%)
<i>Of which:</i>			
<i>Near-cash</i>	£3,960,122,000	£4,186,797,000	
<i>Administration budget</i>	£4,159,275,000	£4,392,050,000	
Capital DEL	£254,714,000	£301,514,000	(15.5%)

The comparison between 2008–09 and 2009–10 is affected by a number of additions in 2008–09, including a Modernisation Fund. HMRC were given access to a total of £300 million ring-fenced Modernisation Funds in the CSR settlement, to meet specific costs directly related to reshaping the Department to be better placed for a changing business environment and for the future. The Department has accessed £234.5 million of that fund to date over the last two financial years.

Administration changes—RfR1A

Funding within RfR1a, which covers the administration costs of HMRC, increased during the two Supplementary Estimates in 2008–09 for the following reasons:

- Modernisation Fund: Draw down of £125 million resource to help with the modernisation and transformation of HMRC; Utilisation of £43.7 million Departmental Unallocated Provision (DUP) to facilitate improvements to key operational activities, which had been held as non-voted DUP as it required Treasury approval before draw down.

The draw down of additional Modernisation Fund and possibly HMRC's End Year Flexibility stock will be considered during the current year and reflected in a 2009–10 Supplementary where approval is given.

Managing the 4.9% DEL reduction applied in HMRC's 2007 Comprehensive Spending Review settlement

HMRC successfully delivered and exceeded all of its 2004 Spending Review efficiency targets over the period 2005–06 to 2007–08 to deliver £663 million efficiency savings against a target of £507 million, and a net reduction of 15,332 full-time equivalent posts against a target of 12,500. This over-achievement was planned to enable the Department to deliver its investment and transformational agenda, and to deliver services within its 2007 CSR settlement (reducing 4.9% year-on-year real terms in underlying funding over 2008–09 to 2010–11). This has put the Department in a strong position to build upon and deliver an ongoing efficiency agenda and further embed a culture of efficiency within HMRC.

During this year's planning round HMRC reviewed the investment programme and agreed a strategic allocation of resources that delivers DSO targets and examined the scope for achieving further Value for Money (VfM) savings.

It is expected that the border detection work will transfer to the UK Border Agency during 2009–10, subject to the successful conclusion of legislation through Parliament. This is a Machinery of Government change which will require funding to be transferred in a 2009–10 Supplementary, providing that the appropriate legislation is in place.

AME PROVISION:

£000s	2009–10	2008–09	Increase 2009–10 compared to 2008–09
Resource AME	32,045,903	30,278,879	5.8%
Of which voted	12,215,903	11,698,546	4.4%
Capital AME	370,000	297,667	24.3%

The increase to voted AME provision sought in 2009–10 reflects the following principal changes against HMRC's Requests for Resources (RfRs):

- A reduction in RfR1 of £100 million, which demonstrates: the tailing off of e-filing incentive payments, where requirement is forecast to reduce to zero in 2010–11; and the fact that HMRC is not expecting any AME revaluation costs compared with £20 million for 2008–09;
- An increase of £605m in RfR5 in respect of child benefit costs (£505 million) and Health in Pregnancy Grants (£100 million). The increase in child benefit spend reflects an increase in the rates of child benefit. The Health in Pregnancy Grant was introduced in April 2009 but claims could be applied early in the last quarter of 2008–09; consequently the 2009–10 cost represents a full year.
- The increase to capital AME is mainly related to Child Trust Fund endowments.

For non-voted, AME increases are related to tax credit payments.

PERFORMANCE

DEPARTMENTAL STRATEGIC OBJECTIVES (DSOs)

Objective 1: *Improve the extent to which individuals and businesses pay the tax due and receive the credits and payments to which they are entitled*

(DSO 1.1)

To reduce losses by £7 billion over the CSR 07 period. This will require HMRC to close the annual tax gap by at least an additional £4 billion in 2010–11.

(DSO 1.2)

To reduce the level of tax credit error and fraud to 5% by 2010–11

(DSOs 1.3 & 1.4)

To sustain take-up levels of Child Benefit and Child Tax Credit at current levels and to increase the take up of Working Tax Credit by 2011

Objective 2: *Improve customers' experience of HMRC and contribute to improving the UK business environment*

(DSO 2.1)

To improve the customer experience that the tax system is simple and even-handed, across all customer groups, by at least 3 percentage points (or up to 90% for any group) by 2011

(DSO 2.2 & 2.3)

To reduce the administrative burden which the UK tax administration imposes on UK businesses by at least 10% by 2011

Objective 3: *Reduce the risk of the illicit import and export of material which might harm the UK's physical and social well-being*

(DSO 3.1)

To maintain the level of disruption of the attempted import and export of illicit drugs, products of animal origin, and other illicit goods

(DSO 3.2)

To contribute to Government objectives on counter terrorism by maintaining the level of operational performance in screening traffic entering the UK for radiation.

DSO 3 responsibilities are expected to transfer to the UKBA in due course. However, as the UK's customs authority, HMRC will keep responsibility for the policy on collection of taxes at the border

Performance against these DSOs will be reported in HMRC's future published Departmental Reports.

DEPARTMENTAL EXPENDITURE LIMIT

The table below compares outturn from 2005–06 onwards with planned DEL from 2008–09:

£m	OUTTURN				PLANS	
	2005–06	2006–07	2007–08	2008–09	2009–10	2010–11
Resource DEL	4,393	4,577	4,361	4,493	4,258	4,153
<i>Of which:</i>						
<i>Near cash</i>	4,157	4,326	4,135	4,187	3,960	3,862
<i>Non Cash</i>	236	251	226	306	298	291
Capital DEL	379	305	257	302	255	248
<i>Less Depreciation</i>	–159	–186	–177	–179	–195	–218
TOTAL DEL	4,612	4,696	4,440	4,615	4,318	4,182

**Depreciation which forms part of RDEL is excluded from total DEL since CDEL includes capital spending and to include depreciation of those assets would lead to double counting*

HMRC is managing with a reduced DEL baseline over the Comprehensive Spending Review which is clearly demonstrated above.

DEL END-YEAR FLEXIBILITY

The 2007–08 EYF stock for HMRC was reported in the Public Expenditure Outturn White Paper 2007–08 (PEOWP) (CM 7419). The breakdown below shows changes since the 2006–07 PEOWP (CM 7156).

<i>£'000</i>	<i>Admin Resource</i>	<i>Other Resource</i>	<i>Total</i>	<i>of which: Near-cash</i>	<i>Non-cash</i>	<i>Capital</i>
PEOWP (July 2007)	61,825	63,106	124,931	155,790	– 30,859	33,257
Take-up in Winter Supplementary Estimate	–	1,400	1,400	1,400	–	–
Balance of EYF After	61,825	61,706	123,531	154,390	– 30,859	33,257
Spring Supplementary	–	–	–	–	–	–
Adjustments TO PEOWP July 2007	1,500	– 1,500	–	– 30,859	30,859	2,295
PEOWP (July 2008)	63,325	60,206	123,531	123,531	–	35,552
2007–08 Underspend	144,432	– 18,050	126,382	62,289	64,093	
Reductions For Virement Out of Admin Budgets	– 18,050	18,050	–	–	–	–
Reductions for Reserve Claims	– 30,000	–	– 30,000	– 30,000	–	–
Other Adjustments	299	–	299	299	–	–
2008–09 Entitlements	160,006	60,206	220,212	156,119	64,093	66,754

ADMINISTRATION BUDGET

The administration budget is £4,159 million. A comparison with earlier years (outturn) and plans is set out below.

<i>£m</i>	<i>2005–06</i>	<i>2006–07</i>	<i>2007–08</i>	<i>2008–09</i>	<i>2009–10</i>	<i>2010–11</i>
PLANS	4,449	4,523	4,442	4,392	4,159	4,056
OUTTURN	4,246	4,499	4,295			

During 2005–06 an underspend was generated mainly as a result of the de-scoping and deferral of some projects following a review of our change portfolio. The resulting savings added to HMRC's stock of End Year Flexibility (EYF).

For 2006–07 there was a small voted underspend. An excess level of receipts was added to this, which led to a surplus of over £20 million.

The 2007–08 underspend of around £145 million mainly relates to Departmental Transformation Project and general administrative underspends, including payroll.

MACHINERY OF GOVERNMENT CHANGES

On 1 April 2009 the functions of The Rent Service (TRS), an executive agency of DWP, will be transferred to the Valuation Office Agency (VOA). This involves a transfer of resources of £22 million. From this date the VOA will therefore be responsible for providing valuation and other services in connection with the Local Housing Allowance, Housing Benefit and Fair Rents.

It is expected that the border detection work will transfer to the UK Border Agency during 2009–10, subject to the successful conclusion of legislation through Parliament. As the required legislation has not yet been approved this will require funding to be transferred in a 2009–10 Supplementary.

PROVISIONS AND CONTINGENT LIABILITIES

None of our contingent liabilities fall into the categories specified for reporting to Parliament.

Provisions have been made to meet obligations for the early departure of staff as the Department has a liability to meet pension liabilities until staff reach the age of 60.

Provisions have been made to meet obligations under Child Trust Fund legislation which arises as a direct result of child birth. These obligations require payment of an element which is dependant upon income linked to Tax Credits, a provision is made for this uncertain value.

Other provisions include the cost of legal cases where there is a probability that the court action will be lost and costs awarded against the Department; and accommodation related liabilities where dilapidation clauses exist.

Health in Pregnancy Grant (HiPG) is a new provision and the opening balance for April 2009 reflects the establishment of the provision to cover the payments due to commence from 6 April 2009. The provision is based on the eligibility of those able to claim the grant.

<i>Provisions for liabilities and charges</i>	<i>HiPG</i>	<i>Early Departure</i>	<i>Child Trust Fund</i>	<i>Other</i>	<i>Total</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
<i>Position as at 1 April 2009</i>					
Balance at 1 April 2009	40,600	136,000	80,600	4,600	261,800
Provided in year in main estimate	14,300	4,000	148,700	500	167,500
Provision expected to be used in year	40,000	32,700	89,800	500	163,000
Expected unwinding of discount		2,000	—	—	2,000
Estimated closing balance	14,900	109,300	139,600	4,600	264,300

APPROVAL OF MEMORANDUM

This memorandum has been prepared with reference to guidance in the Estimates Manual provided by HM Treasury and that found on the House of Commons, Scrutiny Unit website. The information in this memorandum has been approved by the Chief Executive of HMRC, Lesley Strathie.

GLOSSARY OF KEY TERMS

Appropriations-in-aid—income received by a department which it is authorised to retain (rather than surrender to the Consolidated Fund) to finance related expenditure. Such income is voted by Parliament in Estimates and accounted for in departmental resource accounts.

Administration Budget—a Treasury control on the resources consumed directly by departments in providing those services which are not directly associated with frontline service delivery. Includes such things as: civil service pay, resource expenditure on accommodation, utilities and services. The Administration Budget is part of Resource DEL.

Annually Managed Expenditure (AME)—a Treasury budgetary control for spending that is generally difficult to control, large as a proportion of the department's budget, and volatile in nature

Departmental Expenditure Limit (DEL)—a Treasury budgetary control for spending that is within the department's direct control and which can therefore be planned over an extended (Spending Review) period (such as the costs of its own administration, payments to third parties, etc).

Departmental Unallocated Provision (DUP)—a part, usually between 1% and 1.5% of a department's total DEL that is not allocated to particular spending, but held back by the department to meet unforeseen pressures.

End Year Flexibility (EYF)—a mechanism whereby departments are allowed to carry forward unspent DEL provision into later years.

Estimates—a statement of how much money government needs in the coming financial year, and for what purposes, by which Parliamentary authority is sought for the planned level of expenditure and receipts in a department.

Estimates Memorandum—an explanation to the relevant departments select committee setting out the links to other spending controls and the contents of a department's Estimate.

Near-cash—resource expenditure that has a related cash implication, even though the timing of the cash payment may be slightly different. For example, expenditure on gas or electricity supply is incurred as the fuel is used, though the cash payment might be made in arrears on a quarterly basis.

Non-cash—costs where there are no cash transactions but which are included in the body's accounts (or taken into account in charging for a service to establish the true cost of all resources used).

Request for Resources (RfR)—a function based description of the organisational level of the department. These can vary between one or more RfR and should be objective—based, referring to the purpose for which the functions being carried out by the department are intended to meet.

Annex A

MAIN ESTIMATE 08/09 VS MAIN ESTIMATE 09/10 (RESOURCE ONLY)

<i>RfR and section References on changes¹</i>	<i>Main Estimate 2008–09</i>	<i>Main Estimate 2009–10</i>	<i>Variation</i>		<i>DSOs</i>	<i>Aims</i>
	<i>£m</i>	<i>£m</i>	<i>£m</i>	<i>%</i>		
RfR 1	4,075.0	3,978.4	(96.6)	(2.4)%	1,2,3	Administering the tax and customs control systems fairly and efficiently and making it as easy as possible for individuals and businesses to understand and comply with their obligations and receive their tax credit and other entitlements
RfR 2*	0.0	0.0	0.0	0.0%	–	Growing a contribution to the good management of property where the public interest is involved
RfR 3	144.0	158.0	14.0	9.7%	–	Providing payments in lieu of tax relief to certain bodies
RfR 4	31.9	32.9	1.0	3.0%	–	Making payments of rates to Local Authorities on behalf of certain bodies
RfR 5	11,240.0	12,285.0	1,045.0	9.3%	–	Payments of Child Benefit and Child Trust Fund endowments
Total	15,490.9	16,454.3	963.4	6.2%		

1. Section Letters refer to individual sections within Estimates and are included to assist in cross-referencing the Estimate Memorandum with the Estimate in line with the Best Practice Guidance Circulated by the clerk to the Select Committee.

2. Variances highlighted where greater than £50 million and 10%.

* This RfR relates to the Valuation Office agency, which has a token net subhead of £1k.

Annex B

SPRING SUP 08/09 VS MAIN ESTIMATE 09/10 (RESOURCE ONLY)

<i>RfR and section References on changes¹</i>	<i>Spring Supplementary 2008–09</i>	<i>Main Estimate 2009–10</i>	<i>Variation</i>		<i>DSOs</i>	<i>Aims</i>
	<i>£m</i>	<i>£m</i>	<i>£m</i>	<i>%</i>		
RfR 1	4,354.8	3,978.5	(376.3)	(8.6)%	1,2,3	Administering the tax and customs control systems fairly and efficiently and making it as easy as possible for individuals and businesses to understand and comply with their obligations and receive their tax credit and other entitlements
RfR 2	2.6	0.0	(2.6)	(100)%	–	Growing a contribution to the good management of property where the public interest is involved

<i>RfR and section References on changes¹</i>	<i>Spring Supplementary 2008–09</i>	<i>Main Estimate 2009–10</i>	<i>Variation</i>		<i>DSOs Aims</i>
	<i>£m</i>	<i>£m</i>	<i>£m</i>	<i>%</i>	
RfR 3	144.0	158.0	14.0	9.7%	– Providing payments in lieu of tax relief to certain bodies
RfR 4	31.9	32.9	1.0	3.0%	– Making payments of rates to Local Authorities on behalf of certain bodies
RfR 5	11,580.0	12,285.0	705.0	6.1%	– Payments of Child Benefit and Child Trust Fund endowments
Total	16,113.3	16,454.3	341.0	21.2%	

1. Section Letters refer to individual sections within Estimates and are included to assist in cross-referencing the Estimate Memorandum with the Estimate in line with the Best Practice Guidance Circulated by the clerk to the Select Committee.

2. Variances highlighted where greater than £50 million and 10%

<i>RfR and Section Reference on changes¹</i>	<i>Section Descriptions</i>	<i>Main Estimate</i>		<i>Main Estimate 2009–10</i>	<i>Variations from Spring Supplementary Estimate 2008–09 to Main Estimate 2009–10</i>		<i>Variations from Main Estimate 2008–09 to Main Estimate 2009–10</i>	
		<i>2008–09</i>	<i>Supplementary Estimate 2008–09</i>		<i>£m</i>	<i>£m</i>	<i>£m</i>	<i>%</i>
<i>RfR 1</i>								
A	Administration	3,975.0	4,144.8	3,868.4	(276.4)	(6.7)%	(106.6)	(2.7)%
B	E-filing incentive payments	100.0	190.0	110.0	(80.0)	(42.1)%	10.0	10.0%
C	Operational local clearance payments	0.0	0.0	0.0	0.0	0.0%	0.0	0.0%
D	Revaluations	0.0	20.0	0.0	(20.0)	(100)%	0.0	0.0%
<i>RfR 2</i>								
A	Administration	0.0	0.0	0.0	0.0	0.0	0.0	0.0%
B	Revaluations	0.0	2.6	0.0	(2.6)	(100)%	0.0	0.0%
<i>RfR 3</i>								
A	Payments in lieu of tax relief	144.0	144.0	158.0	14.0	9.7%	14.0	9.7%
<i>RfR 4</i>								
A	Payments of Local Authority rates	31.9	31.9	32.9	1.0	3.1%	1.0	3.1%
<i>RfR 5</i>								
A	Children's Benefit	10,950.0	11,265.0	11,770.0	505.0	4.5%	820.0	7.5%
B	Child Trust Fund Endowments	260.0	270.0	370.0	100.0	37.0%	110.0	42.3%
C	Health in Pregnancy Grant	30.0	45.0	145.0	100.0	222%	115.0	383%

<i>RfR & Section Reference</i>	<i>Resource</i>	<i>Capital</i>	<i>Objectives/Aims</i>	<i>Which supports DSO objective</i>
1	3,978.4	235.9	Administering the tax and customs control systems fairly and efficiently and making it as easy as possible for individuals and businesses to understand and comply with their obligations and receive their tax credit and other entitlements	DSO 1—Improve the extent to which individuals and businesses pay the tax due and receive the credits and payments to which they are entitled DSO 2—Improve customers' experiences of HMRC and improve the UK business environment DSO 3—Reduce the risk of the illicit import and export of material which might harm the UK's physical and social well-being
2	0.0	15.0	Undertaking rating and council tax valuation work in England and Wales and providing valuation and property management services to central government and other bodies where public funds are involved	Supports Valuation Office Agency's objectives
3	158.0	0.0	Providing payments in lieu of tax relief to certain bodies	DSO 1—Improve the extent to which individuals and businesses pay the tax due and receive the credits and payments to which they are entitled
4	32.9	0.0	Making payments of rates to Local Authorities on behalf of certain bodies	Supports Valuation Office Agency's objectives
5	12,285.0	0.0	Payments of Child Benefit, Health in Pregnancy Grants and Child Trust Fund endowments	DSO 1—Improve the extent to which individuals and businesses pay the tax due and receive the credits and payments to which they are entitled

Estimates Memorandum 2009–10 submitted by HM Treasury

INTRODUCTION

The Estimate covers the administration costs of the core Treasury, the Debt Management Office and the Office of Government Commerce. Programme spending on coinage and cost of capital charges for the Treasury's investments in the Bank of England and the Royal Mint are also included. These are continuing functions from previous years. The Estimate features a structural change involving the movement of the OGC spending from RfR 3 to RfR 1 and the creation of a new RfR 3 to cover Financial Stability spending including running costs of UKFI, TIFU and on the Asset Protection scheme; on Northern Rock, Bradford & Bingley (B&B) and any recapitalisations. An explanation of key terms used in the Memorandum is provided at Annex A.

SUMMARY OF RESOURCES SOUGHT IN THE MAIN ESTIMATE

Summary of the main indicators sought in the Estimate

The Main Estimate provides for a:

Net Resource Requirement (NRR) of £ 1,883,647,000 and;

a Net Cash Requirement (NCR) of £ 35,248,862,000.

RfR1 £ 325,797,000

RfR2 £ 52,500,000

RfR3 £ 1,505,350,000

 Budgetary data

The key budgetary figures are:

Resource Departmental Expenditure Limit (DEL)	£ 215,747,000
<i>of which:</i>	
<i>near cash is</i>	£ 216,662,000
<i>Administration budget is</i>	£ 165,145,000
<i>DEL Capital budget is</i>	£ 781,942,000
<i>Annually Managed Expenditure (AME)</i>	£ 1,692,375,000
<i>AME Capital budget</i>	£33,723,000,000

Detail by Section within the Part II table of the Main Estimate (Net resource spend in brackets)

Request for resources (RfR) 1, HM Treasury/Debt Management Office/Office of Government Commerce (£325,797,000)

Section A—funding covers the administrative costs of the Treasury’s core business, formulating and implementing the Government’s financial and economic policies, and Group shared services. It also covers core Treasury programme costs including the printing of Budgets and Estimates, cost of capital charges on the Treasury’s investment in Partnerships UK, conferences and spending in connection with a pilot scheme on the provision of generic financial advice. (Net resources for Section A: £130,409,000). Capital expenditure of £3,800,000 is principally on IT equipment.

Section B—covers running costs of the United Kingdom Debt Management Office (DMO). The DMO is an executive agency of the Treasury specialising in the provision of policy advice on and the delivery of the government’s financing needs and acts as a key gateway for government to the wholesale financial markets. It performs these functions primarily to support HM Treasury’s objective of maintaining sound public finances. The DMO also incorporates the Public Works Loan Board (PWLB) and the Commissioners for the Reduction of the National Debt (CRND), and provides operational services for the Treasury, other government departments and the Bank of England. (Net resources for Section B: £10,395,000). Capital expenditure of £1 million largely relates to IT infrastructure.

Section C—covers the running costs of the Office of Government Commerce—an independent office of the Treasury. Its role is to drive value for money improvements in public procurement and estates management in central government, improve delivery of programmes and projects across government and deliver sustainable procurement and sustainable operations on the government estate. Spending covers OGC administration costs and other current costs for the management and disposal of the surplus civil estate. (£24,993,000).

Section D—cost of capital charges (non-cash) on the Treasury’s investment in the Bank of England (£160,000,000). The actual charge will be calculated at a rate based on the target rate of return agreed between the Treasury and the Bank (6%), applied to the average value of the Bank’s net assets over the year.

RfR 2, UK coinage (£52,500,000)

Section A—for the manufacturing and distribution of UK coinage by the Royal Mint (£20,000,000).

Section B—cost of capital charges (non-cash) on the manufacturing element of the Treasury’s coinage stock held by the Royal Mint (£125,000).

Section C—cost of capital charges (non cash) on the Treasury’s investment in the Royal Mint (£2,800,000)

Section D—covers the cost of metals used in the production of UK coinage (£29,400,000).

Section E—cost of capital charges (non-cash) on the metal element of the Treasury’s coinage stock held by the Royal Mint (£175,000).

RfR 3, Financial Stability (£1,505,350,000)

Section A—covers the running costs of United Kingdom Financial Investments Limited (£5,350,000).

Section B—covers capital payments by the Infrastructure Finance Unit Limited in respect of PFI projects (£775,000,000).

Section C—covers the cost of capital charge (non-cash) on financial investments in financial organisations (£1,500,000,000).

Section D —Financial assistance to financial organisations other than Northern Rock, including payments in respect of Royal Bank of Scotland and working capital loans to B&B (£18,723,000,000).

Section E—Refinancing payments to Northern Rock, including loans and working capital loans (£15,000,000,000).

EXPLANATION OF SIGNIFICANT CHANGES MADE SINCE THE 2008–09 ESTIMATES

Net resource requirement:	2009–10	£1,883,647,000
	2008–09	£21,068,184,000

The main change since the presentation of the 2008–09 Main Estimate is the coverage of RfR 3. In previous years the RfR covered OGC spending but this has now been subsumed into RfR 1 bringing together all of the Treasury’s administration budget spending within one RfR. RfR 3 now covers financial stability including the running costs of United Kingdom Financial Investments, payments to Northern Rock and B&B and the costs of capital charge on investments in financial institutions.

The Main Estimate total is 91% lower than total provision for last year. This is principally due to last year’s Estimate including impairments on the department’s financial investments.

Forecast resource outturn for the 2008–09 Estimate shows an over spend of approximately £30 billion against the total provision voted in the Revised Spring Supplementary Estimate. This overspend arises from the inclusion of a provision for losses of approximately £30 billion in relation to financial stability measures consistent with the estimate given in Box 2.3 of the Economic and Fiscal Strategy Report. The accounting requirement to include this non-cash provision came to light too late for inclusion in the Treasury’s Revised Spring Supplementary Estimate.

The department has a Departmental Unallocated Provision (Resource DEL budget cover) of £3,631,000 for 2009–10.

Net cash requirement:	2009–10	£35,248,862,000
	2008–09	£89,236,052,000

The large decrease in 2009–10 in the cash requirement compared to 2008–09 is mainly due to the large financial stability interventions in 2008–09, including recapitalisations.

Resource DEL:	2009–10	£215,747,000
	2008–09	£221,624,000

The reduction in Resource DEL compared with the previous year reflects the CSR settlement, as adjusted for subsequent inter-departmental transfers.

Administration budget:	2009–10	£ 165,145,000
	2008–09	£ 169,543,000

The reduction in the administration budget reflects the impact of the CSR settlement, as adjusted for subsequent inter-departmental transfers.

Capital DEL:	2009–10	£781,942,000
	2008–09	£7,021,000

The increase in Capital DEL reflects the Infrastructure Finance Unit funding comprising a transfer of £5,250,000 to HM Treasury from DEFRA and DEL Reserve claims totalling £769,750,000, offset by a small reduction reflecting the CSR settlement. The capital DEL figure includes a DUP of £2,142,000.

Capital AME:	2009–10	£33,723,000,000
	2008–09	£89,902,455,000

The figures for 2009–10 reflect reduced costs of financial stability interventions compared to those made in 2008–09.

THE TREASURY GROUP’S 2004 SPENDING REVIEW (SR2004) PUBLIC SERVICE AGREEMENT (PSA)

A report on progress against the Treasury Group’s PSA targets will be published in the 2009 Annual Report and Accounts, due to be published before the summer Recess.

DEPARTMENTAL EXPENDITURE LIMIT (DEL)

The table below compares outturn from the last few years with planned DEL budgets for the future.

	<i>£'000s</i>			
	<i>OUTTURN</i>		<i>PLANS</i>	
	<i>2007-08</i>	<i>2008-09*</i>	<i>2009-10</i>	<i>2010-11</i>
Resource DEL	200,805	206,723	215,747	205,049
<i>o/w Near cash</i>	<i>199,195</i>	<i>209,974</i>	<i>216,662</i>	<i>205,159</i>
<i>o/w Non-cash</i>	<i>1,610</i>	<i>(3,251)</i>	<i>(915)</i>	<i>(905)</i>
Capital DEL	-904	3,783	781,942	6,700
less Depreciation**	(5,932)	(7,489)	(7,915)	(8,800)
TOTAL DEL	193,969	203,017	989,774	202,154

*Provisional outturn.

** Depreciation, which forms part of RDEL, is excluded from total DEL since CDEL includes capital spending and to include depreciation of those assets would lead to double counting.

The DEL plans figures are consistent with the 2007 CSR settlement after taking account of various inter-departmental transfers that have taken place since the settlement.

END YEAR FLEXIBILITY (EYF)

The 2008-09 EYF stock for HM Treasury was reported in the Public Expenditure Outturn White Paper 2007-08 (PEOWP) (Cm 7419). There has been no draw down of EYF or any other changes to the entitlements since publication of PEOWP.

	<i>£'000</i>					
	<i>Admin</i>	<i>Other resource</i>	<i>TOTAL Resource</i>	<i>of which: near cash</i>	<i>non-cash</i>	<i>Capital</i>
PEOWP Cm 7419 July 2008	70,110	131,526	201,636	<i>201,636</i>	-	72,616
Winter supp	-	-	-	-	-	-
Spring supp	-	-	-	-	-	-
Balance of EYF at 31 March 2009	70,110	131,526	201,636	<i>201,636</i>	-	72,616

The department's current 2008-09 provisional outturn indicates that EYF entitlements will be increased by underspends of £14.901 million resource DEL and £3.238 million capital DEL. It has been agreed that, provided the Treasury can demonstrate need, the department can access up to £20 million in resource EYF in 2009-10 to fund the increased workload brought about by financial stability issues. The need for EYF draw down in 2009-10 will be assessed later in the year in the light of forecasts of spending by the Treasury group as a whole.

ADMINISTRATION BUDGET

A comparison with earlier years (outturn) and plans is set out below.

	<i>£'000</i>			
	<i>OUTTURN</i>		<i>PLANS</i>	
	<i>2007-08</i>	<i>2008-09*</i>	<i>2009-10</i>	<i>2010-11</i>
Administration budget	159,870	158,286	165,145	161,335

*Provisional outturn.

2008-09 outturn is based on provisional figures net of £12 million of income paid to the Consolidated fund. Excluding this, outturn would be £168 million.

PROVISIONS

	<i>£'000</i>			
	<i>Early departures</i>	<i>Surplus leasehold property</i>	<i>Other</i>	<i>Total</i>
<i>Provisions for liabilities and charges</i>				
Estimated balance at 1 April 2009	7,300	6,900	30,000,000	30,014,200
Provided in year at Main Estimate	0.0	0.0	0.00	0.0
Provision expected to be used in year	2,400	400	0.00	2,800
Estimated balance at 31 March 2010	4,900	6,500	30,000,000	30,011,400

In addition to provisions there are liabilities arising from commitments to pay out fixed term depositors of Kaupthing Singer & Friedlander, Icesave and London Scottish bank that will be met in 2009–10. These are included in the “Use of provisions” figure shown in “Part II: Resource to cash reconciliation”.

CONTINGENT LIABILITIES

The contingent liabilities note in the Main Estimate covers contingent liabilities outstanding at the date of finalisation of the Estimate. The list includes the following changes and additions since the equivalent note in the Spring Supplementary Estimate:

- New liabilities in respect of Dunfermline Building Society covering Treasury guarantees to underwrite Bank of England losses in connection with the social housing portfolio and underwrite any losses the Bank might incur through managing the working capital facility;
- New liabilities concerning B&B continuing to operate above the minimum regulatory capital requirements and indemnities provided by B&B for its new directors against liabilities and losses incurred in the course of their actions;
- New liability to pay compensation in respect of Dunfermline Building Society in the event that an independent valuer determines that compensation is payable to certain parties;
- Changes to the levels of liabilities for the asset purchase scheme (up from £50 million to £150 million) and asset protection scheme (up from unquantifiable to £457 billion). The background to these changes were included in FSBR Box C4; and
- Small changes to the levels of liability in respect of Northern Rock’s back-up liquidity facility and the guarantee arrangements for certain wholesale borrowings and deposits with B&B.

APPROVAL OF MEMORANDUM

This Memorandum has been prepared with reference to guidance in the *Estimates Manual* provided by HM Treasury and that found on the House of Commons, Scrutiny Unit website. The information in this memorandum has been approved by the department’s Finance Committee.

GLOSSARY OF KEY TERMS

Departmental Expenditure Limit (DEL)

This is spending within the Department’s direct control and which can therefore be planned over an extended period, such as the costs of its own administration, payments to third parties, etc.

Annually Managed Expenditure (AME)

AME spending is generally less predictable and controllable than expenditure in DEL.

Request for Resources (RfR)

A Request for Resource is a function based description of the organisational level of the department. These can vary between one or more RfR and should be objective—based, referring to the purpose for which the functions being carried out by the department are intended to meet.

Subheads and Sections

Subheads and sections are lines within RfRs that detail the functions that the department is carrying out in pursuit of its objective. For example, subhead A1 is frequently “Administration” in many departmental Estimates.

Departmental Unallocated Provision (DUP)

A contingency reserve, which the department accesses, where necessary, by means of a Supplementary Estimate.

End of Year Flexibility (EYF)

A mechanism that enables the Department to plan the use of resources over Spending Review years and therefore carry forward unspent provision in the Departmental Expenditure Limit (DEL) in one year to subsequent years.

Voted and Non-Voted

Voted expenditure is that which has gone through the Supply Estimates process. Non-voted, as its description suggests, has not been through this process. It usually refers to expenditure that comes from another source eg consolidated fund standing services.

December 2009

Winter Supplementary Estimates Memorandum 2009–10 submitted by HM Treasury

This memorandum provides details of changes sought in the Treasury's Winter Supplementary Estimate for 2009–10 published in "Central Government Supply Estimates" 2009–10: Winter Supplementary Estimates' HC 24. Further details of the work of the Treasury and its finances can be found in the "HM Treasury Annual Report and Accounts 2008–09" HC 611. Supply Estimates and the Treasury's Departmental Report are available from <http://www.hm-treasury.gov.uk>

2. The purpose of this memorandum is to provide the select committee with an explanation of how the resources and cash sought in the Winter Supplementary Estimate will be applied to achieve departmental objectives and Public Service Agreement (PSA) targets. This includes information on comparisons with the resources provided in earlier years in Estimates and departmental budgets.

SUMMARY OF THE CHANGES SOUGHT IN THE ESTIMATE

3. The Estimate seeks an increase of £20,819,000 in net resources and an increase of £17,795,819,000 in the net cash requirement. The increase in resources is the net effect of take up of Administration Budget EYF, draw down of the balance of our administration Departmental Unallocated Provision (DUP) and programme DUP. The increase in the net cash requirement comprises the near cash consequences of the net resource increase above plus capital payments to RBS and Lloyds as a result of involvement in the Asset Protection Scheme, and the taking up of the Government's share of the rights issue respectively.

DETAILED EXPLANATION OF THE CHANGES BEING SOUGHT

Request for Resources 1: Maintain sound public finances and ensure high and sustainable growth, well being and prosperity for all.

4. The increase in resources is the net effect of the following:

Take up of DEL End Year Flexibility (EYF)

5. There is an increase of £15,000,000 in Section A covering the administrative and programme costs of the Treasury's core business. The increase is to fund the increased workload arising from financial stability work.

Movements between RfRs

6. There is an increase of £2,000,000 programme DEL in Section A. The increase is to finance increased costs associated with financial stability workload pressures and the Money Guidance pilot project. The increase is offset by a reduction in Section A of RfR 2 covering spending on the manufacture of coinage which is forecast to be lower than originally planned at the time of the Main Estimate.

Departmental Unallocated Provision

7. There is a draw down of administration DUP of £1,531,000 and £2,100,000 for programme DUP to fund increased spending in Section A in connection with financial stability (administration) and spending on financial inclusion (programme) for core Treasury.

Changes in forecasts—AME

8. The adoption of International Financial Reporting Standards means that employee benefits must now be accounted for in the Estimate. A new Section E has been introduced with provision of £2,188,000.

REQUEST FOR RESOURCES 2: COST-EFFECTIVE MANAGEMENT OF THE SUPPLY OF COINS AND ACTIONS TO PROTECT THE INTEGRITY OF COINAGE

9. The reduction in resources is the net effect of the following:

Changes due to revised forecasts of requirements—DEL

10. The forecast for the cost of the manufacturing element of coinage production is forecast to be in the region of £18,000,000. The resulting reduction in existing provision of £2,000,000 programme costs is being reallocated to RfR 1.

REQUEST FOR RESOURCES 3: PROMOTING A STABLE FINANCIAL SYSTEM AND OFFERING PROTECTION TO ORDINARY SAVERS, DEPOSITORS, BUSINESSES AND BORROWERS

11. The increase in capital AME of £17,775,000,000 is required for the following:

- (i) RBS has agreed to participate in the Asset Protection Scheme and as a result the Government has agreed to inject £25,500,000,000 in additional capital. The Treasury's Main Estimate already includes £13,000,000,000 for RBS recapitalisation and the Winter Supplementary Estimate includes the balance of £12,500,000,000.

- (ii) It was agreed that Lloyds would not participate in the APS but raise additional private sector capital through a rights issue and issuance of contingent convertibles (“cocos”). The Government, as a Lloyds shareholder, will take up its share of the rights issue resulting in a gross payment of £5,900,000,000.

12. There is a reduction in capital DEL in Section E covering capital payments by Infrastructure Finance Unit Limited in respect of PFI projects, PPP projects and other infrastructure projects approved by HM Treasury. Following a revised forecast of requirements for the remainder of the year, Estimate provision and the department’s capital DEL has been reduced by £625,000,000.

THE NET CASH REQUIREMENT

13. The increase in the net cash requirement amounts to £17,795,819,000 and arises from the changes outlined in paragraphs 6 to 12 above.

CONSOLIDATED FUND EXTRA RECEIPTS (CFERs)

14. The forecast of operating CFERs has been increased to reflect Lloyds obligation to pay an APS exit fee of £2,500,000,000 and estimated Credit Guarantee Scheme fees of £1,500,000,000.

IMPACT ON THE DEPARTMENT’S PUBLIC SERVICE AGREEMENTS

15. The increase in capital AME of £17,775,000,000 is to support stability in the financial services sector and is in line with Treasury DSO outcome DSO 2(e): “Supporting fair, stable and efficient financial markets” and with PSA 6: Deliver conditions for business success in the UK”.

DEPARTMENTAL EXPENDITURE LIMIT

16. The Resource DEL is increasing by £15,000,000 arising from the take up of Administration Budget EYF outlined in paragraph 5 above. There is a reduction of £625,000,000 in Capital DEL as set out in paragraph 12 above. The following table shows a comparison between DEL plans between 2005–06 and 2008–09 (after changes made via Supplementary Estimates) and the outturns for those years, and the DEL for 2009–10.

COMPARISON OF EXPENDITURE AGAINST DEPARTMENTAL EXPENDITURE LIMITS £M

<i>Year</i>	<i>Voted</i>	<i>Non-voted</i>	<i>Total DEL</i>	<i>Outturn</i>	<i>Variance</i>
<i>Resource</i>					
2005–06	227	29	256	215	– 41
2006–07	225	21	246	206	– 40
2007–08	212	20	232	201	– 31
2008–09	201	21	222	200	– 22
2009–10	210	21	231		
<i>Of which near cash</i>	<i>200</i>	<i>31</i>	<i>231</i>		
<i>Capital</i>					
2005–06	5	–	5	– 9	– 14
2006–07	7	–	7	– 1	– 8
2007–08	7	–	7	– 1	– 8
2008–09	6	1	7	3	
2009–10	155	2	157		

DEPARTMENTAL UNALLOCATED PROVISION (DUP)

17. The remaining DUP of £3,631,000 has been drawn down comprising £1,531,000 Administration Budget and £2,100,000 programme costs, both for RfR 1 Section A.

END YEAR FLEXIBILITY

18. Administration Budget EYF of £15,000,000 has been drawn down in the Winter Supplementary. The following table shows the remaining EYF entitlements for 2009–10.

					<i>£m</i>
<i>Administration</i>	<i>Other resources</i>	<i>Total resource EYF</i>	<i>Of which near cash</i>	<i>Capital</i>	<i>Total EYF</i>
65	137	202	202	77	279

ADMINISTRATION BUDGET

19. The Administration Budget is increasing by £15,000,000 through take up of EYF. The following table shows a comparison between administration budget plans between 2005–06 and 2008–09 (after changes made via Supplementary Estimates) and the outturns for those years, and the budget for 2009–10.

COMPARISON OF ADMINISTRATION COSTS AGAINST LIMIT

<i>Year</i>	<i>Voted</i>	<i>Non-voted</i>	<i>Total</i>	<i>Outturn</i>	<i>Variance</i>
2005–06	167	0	167	161	–7
2006–07	167	1	168	160	–8
2007–08	171	0	171	160	–11
2008–09	170	0	170	154	–16
2009–10	180	0	180		

CONTINGENT LIABILITIES

20. The following changes have been made to the list of contingent liabilities:

- (i) The exposure arising from the guarantee arrangements for certain retail and wholesale deposits in Northern Rock (NR) has been reduced to £18,600,000,000;
- (ii) The value of the liability arising from the back-up liquidity facility for NR has been increased to £5,700,000,000;
- (iii) The value of the liability guarantee arrangements safeguarding certain wholesale borrowings and deposits with Bradford & Bingley has been reduced to £10,000,000,000;
- (iv) As announced, the value of the Bank of England Asset Purchase Facility Fund has been increased to £200,000,000,000;
- (v) Amendment of the narrative for the Asset Backed Securities Scheme including the extension of the draw down period to 31 December 2009;
- (vi) Amendments to the narrative and the maximum liability of the Asset Protection scheme. The maximum liability falls to £199,440,000,000;
- (vii) Amendments to the narrative and value of the contingent capital liability for RBS. Liability increases to £8,000,000,000;
- (viii) A new unquantifiable liability in respect of the Equitable Life Ex Gratia payment Scheme. This liability is new to the Supply Estimate contingent liability note but was previously included in note 27.1.3 of the department's 2008–09 accounts ;
- (ix) A new unquantifiable liability arising from the guarantee for panel members who will appoint the independent valuer under article 4 of the Dunfermline Building Society Compensation Scheme, Resolution Fund and Third Party Compensation Order 2009;
- (x) Amendments to the narrative following the Dunfermline Building Society Compensation Scheme Order coming into force on 7 July.

November 2009

Winter Supplementary Estimate Memorandum 2009–10 submitted by HMRC

INTRODUCTION

The HMRC Winter Supplementary Estimate for 2009–10 seeks the necessary resources and cash to support the functions of the Department.

The purpose of this memorandum is to provide the select committee with an explanation of how the resources and cash sought in the Winter Supplementary Estimate will be applied to achieve Departmental Strategic Objectives (DSOs) targets. This includes information on comparisons with the resources provided in earlier years in Estimates and Departmental budgets. Details of changes in resources relative to original plans set out in the last Spending Review are provided.

During this winter round, the changes in provision sought in this Supplementary Estimate relate primarily to:

- £70,000,000 Resource DEL draw down from End Year Flexibility reserves
- £42,585,000 Resource DEL and £3,559,000 Capital DEL draw down of non-voted DUP (DEL neutral)

- Reduction of £303,166,000 Resource DEL and £13,081,000 Capital DEL due to the formal Machinery of Government transfer from HMRC to the Home Office in respect of the UK Border Agency (UKBA)

An explanation of key terms used in the memorandum is provided as an annex.

SUMMARY OF THE MAIN SPENDING CONTROL FIGURES CONTAINED IN THE ESTIMATE VOTED PROVISION

The Supplementary Estimate provides a 5.38% decrease in voted resource:

— Decrease in the Net Resource Requirement (NRR) of	£52,581,000
RfR1 – £192,581,000	
RfR5 £140,000,000	
— Decrease in the Net Cash Requirement (NCR) of	£51,375,000

BUDGETARY DATA

The changes to key budgetary figures are:

Resource Departmental Expenditure Limit <i>decreases</i> by	£228,968,000
Capital Departmental Expenditure Limit <i>decreases</i> by	£13,081,000

The net decreases above are caused by the Machinery of Government transfer from HMRC to the Home Office in respect of the UK Border Agency (UKBA), for which details are given further below.

Annually Managed Expenditure increases by	£138,000,000
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This is due to Child Benefit and Child Trust Fund increases offset by a small credit in respect of Accrued Employee Benefits (annual leave) under International Financial Reporting Standards.

DETAILED EXPLANATION OF CHANGES IN PROVISION SOUGHT IN THE SUPPLEMENTARY ESTIMATE, AND IMPLICATIONS FOR BUDGETS

<i>Amount</i>	<i>Description</i>
<i>Movements in provision related to DEL</i>	
Draw down of End Year Flexibility	
£70,000,000	Draw down of EYF near cash to fund the closure of various non-strategic sites delivering this through staff redeployments, departures and other efficiency measures. (RfR1: subhead A)
Transfer of budgetary cover from the Ministry of Justice	
£4,198,000	Transfer in from the Ministry of Justice of near cash programme expenditure in respect of work carried out in processing applications for leave to appeal and appeals on points of law from decisions of the Social Security and Child Support jurisdiction within the Tribunal Service in respect of National Insurance benefits. (Non-voted DEL)
Machinery of Government transfer from HMRC to the Home Office	
– £303,166,000	Machinery of Government transfer from HMRC to the Home Office as part of the establishment of the UK Border Agency (UKBA). Details are provided in a separate section further below
Resource	
– £13,081,000	
Capital	
– £242,049,000	Total change in provisions related to DEL
<i>Movements in provisions related to AME</i>	
Child Benefits	
£130,000,000	Increase in AME in relation to Child Benefit requirements due mainly to higher than expected number of 16–19 year olds staying in Full Time education. (RfR5: subhead A)
Child Trust Fund	
£10,000,000	Increase in AME in relation to Child Trust Fund requirements due to higher projected births and other qualifying children. (RfR5: subhead B)

<i>Amount</i>	<i>Description</i>
Tax Credits	
£289,763,000	Increase to AME non-voted funding in respect of Tax Credits due to higher spend on In Work claimants than anticipated. (Non-voted)
Accrued Employee Benefits	
– £2,000,000	Decrease in AME programme to record the movement in accrued employee annual leave as required under International Financial Reporting Standards. (RfR1: subhead C)
£427,763,000	Total change in provisions related to AME
<i>Movements in provisions neutral in budgets</i>	
Take up of Resource Departmental Unallocated Provision	
£42,585,000	Draw down of non-voted DUP as voted administration near cash costs to facilitate improvements to key operational activities. (RfR1: subhead A)
Take up of Capital Departmental Unallocated Provision	
£3,559,000	Draw down of non-voted DUP as voted capital costs to facilitate improvements to key operational activities. (RfR1: subhead A)
NAO Audit Fee	
£1,780,000	Auditors remuneration costs for work carried out on International Financial Reporting Standards and the UK Border Agency transfer, offset by a reduction to non cash provisions. (RfR1: subhead A)
£47,924,000	Total change in provisions neutral in budgets
<i>Changes in operating appropriations-in-aid (fully offset by changes in spending)</i>	
£11,000,000	To increase the levels of administration income by £11,000,000 mainly due to pension reform work resulting from the Government's undertaking to reform the UK pensions system to deliver increased financial security for an ageing population as part of the Pensions Act 2007. (RfR1: subhead a)
£37,021,000	To increase the levels of administration and programme income due to the UK Border Agency transitional Service Agreements. Details are provided in a separate section further below (RfR1: subhead a)
£48,021,000	Total change in operating appropriations-in-aid

IMPACT ON DEPARTMENTAL STRATEGIC OBJECTIVES

Objective I:—*Improve the extent to which individuals and businesses pay the amount of tax due and receive the credits and payments to which they are entitled.*

A proportion of £42,585,000 Resource Departmental Unallocated Provision

Draw down of non-voted DUP of £42,585,000 taken up as voted administration near cash costs to facilitate improvements to key operational activities.

A proportion of £3,559,000 Capital Departmental Unallocated Provision

Draw down of non-voted DUP of £3,559,000 taken up as voted capital costs to facilitate improvements to key operational activities.

£70,000,000 Administration Near Cash End Year Flexibility

Draw down of £70,000,000 EYF near cash to fund the closure of various non-strategic sites delivering this through staff redeployments, departures and other efficiency measures.

Objective II:—*Improve customers' experience of HMRC and improve the UK business environment.*

A proportion of £42,585,000 Resource Departmental Unallocated Provision

As detailed in Objective 1.

A proportion of £3,559,000 Capital Departmental Unallocated Provision

As detailed in Objective 1.

Objective III:—*Reduce the risk of the illicit import and export of material that might harm the UK's physical and social well being.*

—£303,166,000 *Resource Machinery of Government transfer*

Machinery of Government resource transfer of £303,166,000 from HMRC to the Home Office as part of the establishment of the UK Border Agency (UKBA).

—£13,081,000 *Capital Machinery of Government transfer*

Machinery of Government capital transfer of £13,081,000 from HMRC to the Home Office as part of the establishment of the UK Border Agency (UKBA).

DEPARTMENTAL EXPENDITURE LIMIT

This Supplementary Estimate will result in an overall reduction in resource DEL of £228,968,000 and an overall decrease in capital DEL of £13,081,000. The revised total DEL will decrease by £253,820,000. Details of DEL in Estimates are:

£'000s	Voted	Non-voted	TOTAL
<i>Resource DEL</i>			
Main Estimate	3,868,432	389,724	4,258,156
Winter Supplementary Estimate	3,677,851	351,337	4,029,188
<i>Capital DEL</i>			
Main Estimate	251,155	3,559	254,714
Winter Supplementary Estimate	241,633	—	241,633
Revised Total DEL*	3,712,513	351,337	4,063,850

**Depreciation, which forms part of RDEL, is excluded from total DEL since CDEL includes capital spending and to include depreciation of those assets would lead to double counting.*

The table below compares outturn from 2005–06 to 2008–09 with planned DEL.

Year	£ '000s				
	Voted	Non-voted	TOTAL*	Outturn*	Variance
<i>Resource</i>					
2005–06	3,960,974	349,051	4,310,025	4,116,918	– 4.48%
2006–07	3,987,148	347,939	4,335,087	4,293,297	– 0.96%
2007–08	3,872,277	372,813	4,245,090	4,068,552	– 4.16%
2008–09	3,845,404	347,739	4,193,143	4,129,998	– 1.50%
2009–10	3,677,851	351,337	4,029,188		
2010–11	3,765,429	388,074	3,851,918		
<i>Capital</i>					
2005–06	374,269	2,977	368,856	371,073	+ 0.60%
2006–07	338,331	0	330,322	296,789	– 10.15%
2007–08	288,230	3,739	283,728	248,593	– 12.38%
2008–09	284,866	3,648	293,071	289,777	– 1.12%
2009–10	241,633	0	241,633		
2010–11	244,642	3,472	237,549		

The Resource DEL outturn for 2008–09 of £4,129,998 represents an underspend of £63,145 compared to final provision of £4,193,143 (equivalent to—1.5% of Resource DEL). The main underspends relate to non-cash surpluses.

The Capital DEL Outturn for 2008–09 of £289,777 compares against a final provision of £293,071. The underspend of £3.3 million was achieved through a surplus by the Valuation Office Agency.

* *Removes baseline transfer and costs associated with two machinery of government changes: Serious Organised Crime Organisation (SOCA); and the United Kingdom Border Agency (UKBA) in 2006–07 and 2009–10 respectively.*

DEL END-YEAR FLEXIBILITY

The 2008–09 EYF stock for HMRC was reported in the Public Expenditure Outturn White Paper 2008–09 (PEOWP) (Cm 7606). The breakdown below reflects the latest EYF position at the Winter Supplementary.

<i>£'000</i>	<i>Admin Resource</i>	<i>Other Resource</i>	<i>Total</i>	<i>of which: Near-cash</i>	<i>Non-cash</i>	<i>Capital</i>
PEOWP (July 2007)	61,825	63,106	124,931	155,790	– 30,859	33,257
Take-up in WSE	–	1,400	1,400	1,400	–	–
Balance of EYF after Winter/ Spring Supplementaries	61,825	61,706	123,531	154,390	– 30,859	33,257
Changes to 2006–07 outturn	1,500	– 1,500	–	– 30,859	30,859	2,295
PEOWP (July 2008) to be added	63,325	60,206	123,531	123,531	–	33,257
2007–08 Underspend	144,432	– 18,050	126,382	62,289	–	31,202
Reductions for virement out of Admin budgets	– 18,050	18,050	–	–	–	–
Reductions for Reserve claims	– 30,000	–	– 30,000	– 30,000	–	–
Other Adjustments	299	–	299	299	–	–
2008–09 Entitlement	160,006	60,206	220,212	56,119	64,093	66,754
Changes to 2007–08 outturn	–	47,624	47,624	47,624	–	–
2008–09 Underspend	62,321	–	62,321	8,053	54,268	3,614
Other adjustments	473	4	477	477	–	–
2009–10 Entitlement PEOWP (July 2009)	222,800	107,834	330,634	212,273	118,361	70,368
Take up in WSE	– 70,000	–	– 70,000	– 70,000	–	–
Balance	152,800	107,834	260,634	142,273	118,361	70,368

ADMINISTRATION BUDGET

The administration budget is £3,957,886. A comparison with earlier years (outturn) and plans is set out below.

ADMINISTRATION BUDGET (PREVIOUS YEARS)*

<i>Year</i>	<i>Plans</i>	<i>Outturn</i>
2005–06	4,201,611	4,000,064
2006–07	4,269,918	4,245,702
2007–08	4,180,705	4,033,842
2008–09	4,124,749	4,055,160

During 2005–06 an underspend was generated mainly as a result of the de-scoping and deferral of some projects following a review of our change portfolio.

For 2006–07 there was a small voted underspend. An excess level of receipts was added to this, which led to the surplus.

The 2007–08 underspend relates mainly to Departmental Transformation and general administration underspends, including paybill.

For 2008–09 the underspend related mainly to non-cash surpluses generated by an imbalance between our near and non-cash splits created during CSR07.

*Removes baseline transfer and costs associated with two Machinery of Government changes: Serious Organised Crime Organisation (SOCA); and the United Kingdom Border Agency (UKBA) in 2006–07 and 2009–10 respectively.

The changes to the current year's Administration Budget are:

CHANGES TO ADMINISTRATION BUDGET IN 2008–09

1 April 2009 at Main Estimate	4,159,275
Change announced in winter supplementary	– 201,389
Revised Administration Budget	3,957,886

ADMINISTRATION BUDGET (REMAINING CSR YEARS)

<i>Year</i>	<i>Plans</i>
2010–11	4,056,226

MACHINERY OF GOVERNMENT CHANGES

<i>Description</i>	<i>RfR and section</i>	<i>Date of transfer</i>	<i>Amount £000</i>	<i>Transferring Dept</i>	<i>Receiving Dept</i>
Establishment of the UK Border Agency (UKBA)	RfR1 Subhead A	1st April 2009	£303,166,000 Resource £13,081,000 Capital	HMRC	Home Office

More details follow:

MACHINERY OF GOVERNMENT CHANGES

Legislation was passed on 21 July 2009 establishing the UK Border Agency (UKBA). As a result, staff and other assets are transferring from HMRC to the UKBA and funding as agreed between HMRC and the Home Office (the UKBA parent department) is being transferred via this Supplementary Estimate. Accounting Officer responsibility for the functions transferring passes from Mike Eland, Director General, HM Revenue and Customs, to the Home Office.

The funding transfers are as follows:

Administration: Staff and other running costs	£271,389,000
Programme: Other running costs	£31,777,000
Capital	£13,081,000

HMRC will also be continuing to bear costs on behalf of the UKBA for which charges will be levied. The value of these costs, **£37,021,000**, is included within the total fund transfer outlined above thereby providing cover to the Home Office for the charges. HMRC's appropriations-in-aid limit is therefore increasing by **£37,021,000** in this supplementary, wholly offset by an increase in expenditure which itself offsets the £37 million reduction in HMRC funding included within the total transfer of funds. The overall net effect is DEL neutral and can be summarised (ignoring Capital) as follows:

	<i>HMRC</i>	<i>Home Office</i>
Appropriations in Aid	– £37,021,000	
Funding for charges levied		+ £37,021,000
Funding for all other expenditure	– £266,145,000	+ £266,145,000
Net Resource DEL	– £303,166,000	+ £303,166,000

APPROVAL OF MEMORANDUM

This memorandum has been prepared with reference to guidance in the *Estimates Manual* provided by HM Treasury and that found on the House of Commons, Scrutiny Unit website. The information in this memorandum has been approved by the Principal Accounting Officer of HMRC Lesley Strathie.

GLOSSARY OF KEY TERMS

Appropriations-in-aid—income received by a department which it is authorised to retain (rather than surrender to the Consolidated Fund) to finance related expenditure. Such income is voted by Parliament in Estimates and accounted for in departmental resource accounts.

Administration Budget—a Treasury control on the resources consumed directly by departments in providing those services which are not directly associated with frontline service delivery. Includes such things as: civil service pay, resource expenditure on accommodation, utilities and services. The Administration Budget is part of Resource DEL.

Annually Managed Expenditure (AME)—a Treasury budgetary control for spending that is generally difficult to control, large as a proportion of the department's budget, and volatile in nature

Departmental Expenditure Limit (DEL)—a Treasury budgetary control for spending that is within the department's direct control and which can therefore be planned over an extended (Spending Review) period (such as the costs of its own administration, payments to third parties, etc).

Departmental Unallocated provision (DUP)—a part, usually between 1% and 1.5% of a department's total DEL that is not allocated to particular spending, but held back by the department to meet unforeseen pressures.

End Year Flexibility (EYF)—a mechanism whereby departments are allowed to carry forward unspent DEL provision into later years.

Estimates—a statement of how much money government needs in the coming financial year, and for what purposes, by which Parliamentary authority is sought for the planned level of expenditure and receipts in a department.

Estimates Memorandum—an explanation to the relevant departments select committee setting out the links to other spending controls and the contents of a department's Estimate.

Near-cash—resource expenditure that has a related cash implication, even though the timing of the cash payment may be slightly different. For example, expenditure on gas or electricity supply is incurred as the fuel is used, though the cash payment might be made in arrears on a quarterly basis.

Non-cash—costs where there are no cash transactions but which are included in the body's accounts (or taken into account in charging for a service to establish the true cost of all resources used).

Request for Resources (RfR)—a function based description of the organisational level of the department. These can vary between one or more RfR and should be objective—based, referring to the purpose for which the functions being carried out by the department are intended to meet.

Letter from Penny Ciniewicz, Chief Executive, Valuation Office Agency to the Chairman of the Sub-Committee

VALUATION OFFICE AGENCY—PORTS NON-DOMESTIC RATING

The Sub-Committee has requested a progress report on the actions taken this year to address concerns regarding the ports review, raised in their report on the Administration and expenditure of the Chancellor's departments 200708, First Report of Session 200809.

FAST TRACK ARRANGEMENTS

From 24 November 2008, the Valuation Office Agency (VOA) put in place special fast track arrangements for ratepayers affected by the review of ports who wished to question or challenge their new rating assessments. We have written to all the occupiers, explaining the process to them and are liaising with them, where necessary, to ensure we can reach a resolution as soon as possible.

Cases involving backdated rate liabilities in ports are given priority attention at all stages by the Agency, which:

Reviews all initial enquiries and responds within 5 working days, unless a site visit is requested or required in which case it may take up to 10 working days.

Gives an initial response to points raised in any appeal within 10 working days and aims to confirm a final decision shortly after that? in any event a decision will be issued within 2 months in all but the most complex cases.

Refers appeals to the independent Valuation Tribunal (VT), where agreement can't be reached and a ratepayer wants to pursue the case, requesting that the tribunal list the appeal for hearing as soon as possible.

Turning to the specific questions raised by the Committee:

How many formal appeals have you taken from port occupiers under the new fast track arrangements?

As at 4 November 2009, the VOA has applied the fasttrack arrangements to 758 proposals (appeals). 314 of these proposals were made prior to and were still outstanding on 24 November 2008 when the PreBudget Report (PBR) was made. The remaining 444 have been made since the PBR announcement.

Of these appeals, how many did you respond to within five days (10 days where an inspection is required)?

The undertaking to respond within 5 days (10 days where an inspection is required) is in respect of initial enquiries. The service standard for proposals (appeals) is to respond within 10 days. 314 ratepayers who had outstanding proposals prior to the PBR announcement were contacted in November 2008 informing them that their proposals would be dealt with under the new fasttrack arrangements. As at 4 November 2009, of the 444 received after PBR, 436 required a response within ten working days, of these 423 or 97% had received a response within time and for the remainder a response was provided shortly thereafter.

How many have been resolved?

At 4 November 2009, 464 of the 758 proposals have been resolved. In the remaining 294 cases, discussions are continuing to establish whether a settlement is possible. Where agreement clearly cannot be reached the matter will be determined by independent Valuation Tribunals.

How many of the appeals have resulted in a change to your assessment?

146 of the 464 proposals have been settled by agreement, well founded or heard at independent Valuation Tribunal resulting in a change to the assessments. The remaining 318 proposals have been withdrawn or dismissed at tribunal.

How many of the appeals have been referred to the independent Valuation Tribunal?

Of the 294 proposals still outstanding, 237 have been transmitted as appeals to the Valuation Tribunal following issue of the Valuation Officer's considered decision. The presumption is that early hearings will follow subject to the other parties' views on timing. In practice although ratepayers and their agents have been invited to support early listing dates, very few have taken this up. Of these 237 cases, 70 have a hearing date on or before 16 December 2009.

How many of the independent Valuation Tribunal hearings have upheld your assessment?

Fifteen cases have been heard before independent Valuation Tribunals. In each case the Tribunal has either upheld the assessment or case of the Valuation Officer or dismissed the proposal for lack of prosecution evidence. It is hoped that these decisions will provide clarity to enable resolution of other appeals made on similar grounds.

What are your legal costs for independent Valuation Tribunals involving port occupiers?

The total cost incurred by the VOA in obtaining legal advice and carrying out legal proceedings in connection with backdating business rates for some port companies through to 2 September 2009 was approximately £35,500. This includes Counsel's fees and other disbursements associated with Tribunal hearings, as well as the costs of time spent by HMRC's legal staff on behalf of the VOA.

Valuation Officers are required to maintain accurate rating lists. They are not responsible for calculation or collection of actual rate liability, which is the responsibility of the local (billing) authority. I have therefore taken the opinion of the Department for Communities and Local Government for the answers to the other questions raised by the committee:

BACKDATED LIABILITY

How many ports occupiers have agreed to spread their liability under this arrangement?

As at 8 October 2009, Local Authorities have reported that 200 business properties within ports in England had been granted a schedule of payments.

Has the Welsh Assembly introduced similar arrangements for Wales?

Yes—the Welsh Assembly brought in a similar scheme.

How many port occupiers have gone insolvent since being notified of their backdated liability?

We do not hold information on port occupiers that may have gone insolvent since being notified of their backdated liability.

How much backdated liability has now been paid, and what proportion is this of the total liable?

As at 8 October 2009, Local Authorities in England have reported that a total of £21,246,973 in backdated liabilities had been collected with a further £67,860,027 outstanding.

PAYMENTS BETWEEN PORTS OCCUPIERS AND OPERATORS

To what extent have port owners taken on backdated liability identified by the VOA as payable by port occupiers?

The backdated liability remains solely the responsibility of the occupying business that incurred the rates. We do not hold information on individual port owners that may have taken on backdated liability via an agreement.

Do negotiations between port owners and port occupiers remain ongoing and, if so, is the VOA prepared to await the outcome of such negotiations before requiring payments from port occupiers?

Valuation Officers are required to maintain accurate rating lists (they are not responsible for billing). When they become aware a change is needed, such as at the ports, they must make the alteration and also specify the date from which the change should be effective for rates charging purposes.

At the time of the Ports Review the requirement to backdate liabilities was set out in 14(2) of The NonDomestic Rating (Alteration of Lists and Appeals) (England) Regulations 2005. Regulation states that “where an alteration is made to correct any inaccuracy in the list or on after the day it is compiled, the alteration shall have effect from the day on which the circumstances giving rise to the alteration first occurred.”

The date of the change is now governed by regulations (The Non-Domestic Rating (Alteration of Lists and Appeals) (England) Regulations 2009) and where the correction is to insert property that existed at or prior to the compilation of the list, these require the alteration to be made from the start of the rating list (backdating), which in this case is 1 April 2005. Valuation Officers are not given any discretion on the effective date.

Once a hereditament is entered onto the rating list, it becomes incumbent on the relevant local authority to bill the relevant occupier. This is because local authorities are required under the rating legislation to collect the rates that fall due and have no discretion to vary or amend this liability. They must act diligently in collecting the rates, and to this end they have ultimately the power to pursue payment through the courts if the rates remain unpaid.

It is important to note here that where local authorities cannot demonstrate that they have pursued payment for any amounts diligently, the authority is required to make up the deficit.

The Department for Communities and Local Government has always advised local authorities that whilst the vigorous enforcement of debt recovery is important the rigid use of enforcement procedures may not always be appropriate, for example in cases of hardship. However, the ultimate decision on what action to take on each individual case rests with the local authority and neither the VOA nor any of the Government Departments have powers to intervene.

In order to avoid the standard system whereby, if a local authority did not take the steps currently available to collect the immediate payments from backdated liabilities in the current financial year it would be faced with paying that liability into the pool itself, the eight year schedule of payments was introduced.

13 November 2009

Supplementary written evidence submitted by HM Revenue and Customs

1. Q208: SALLY KEEBLE

The percentage of calls answered by Contact Centres during peak periods.

HMRC’s Departmental Report gives an average performance figure across the year (57%) and reports details of weekly performance outside peaks (75% in all but three weeks), but does not give more details of performance during peak periods.

The contact centres’ busiest months are April, May, June and July due to Tax Credit Renewals. July is a particularly busy month as a significant proportion of Tax Credit claimants renew close to the deadline of 31 July. There is a further peak in August and September when Child Benefit and Tax Credit claimants notify whether their 16 year olds will be continuing with their education and the claims of those Tax Credit claimants who have failed to renew are terminated. There is also a peak in January with the Self Assessment (SA) Online filing deadline.

The percentage of call attempts answered in these months in 2008–09 are highlighted in the table below alongside the monthly performance over the first six months of this year—2009–10. The table shows that performance has improved significantly this year. For example, in July 09/10 HMRC answered 68% of calls compared to 33% in July 08/09. In September 09/10 HMRC answered 74% of calls compared to 52% in September 08/09.

<i>Month</i>	<i>Peak Period (highlighted)</i>	<i>% Call Attempts Answered 08/09</i>	<i>% Call Attempts Answered 09/10</i>
Apr	New Tax Year—PAYE Coding/Tax Credit Renewals	56%	77%
May	PAYE Coding/Tax Credit Renewals	44%	68%
Jun	Tax Credit Renewals	50%	80%
Jul	Tax Credit Renewals	33%	68%
Aug	Tax Credit Terminations and Child Benefit Full Time Non Advanced Education (FTNAE) Notifications	66%	73%
Sep	Child Benefit FTNAE Notifications	52%	74%

<i>Month</i>	<i>Peak Period (highlighted)</i>	<i>% Call Attempts Answered 08/09</i>	<i>% Call Attempts Answered 09/10</i>
Oct			76%
Nov			86%
Dec			85%
Jan	Online Services/Taxes Helplines Final Filing date for SA Tax Returns		61%
Feb			84%
Mar			78%
Total			57%

2. Q218: SALLY KEEBLE

The statistics on take-up of the Childcare element attached to either the Child Tax Credit or the Working Tax Credit.

A take-up rate for the childcare element cannot be calculated in the same way as for Working Tax Credit or Child Tax Credit. This is because we do not have an estimate of the number of people who are eligible for the childcare element. The administrative and survey data we currently hold does not allow us to determine which tax credit recipients are entitled to, but not claiming the childcare element.

The table below gives estimates of the number of families benefiting from the childcare element at points in time based on our snapshot statistics for tax credits awards. This number has increased by 78% since New Tax Credits were introduced in 2003 and also there are over now twice as many families benefiting from it as from the childcare tax credit in the Working Families Tax Credit, the predecessor system. However during this time the number of families eligible for the child care element will also have grown, for example the Government has increased the amount of support in tax credits by increasing the proportion and maximum costs allowed for child care as well as increasing the child element above indexation.

FAMILIES BENEFITING FROM THE CHILDCARE ELEMENT

	<i>Numbers benefiting¹</i>	<i>Average weekly help</i>
July 2003	264,400	£43.20
October 2003	285,600	£43.43
April 2004	317,700	£43.67
December 2004	331,300	£45.75
April 2005	337,400	£45.60
December 2005	356,000	£48.97
April 2006 ²	374,300	£49.90
December 2006 ²	395,800	£60.13
April 2007	413,700	£61.26
December 2007	427,600	£64.19
April 2008	448,800	£65.30
December 2008	461,500	£68.37
April 2009	470,400	£68.69

Notes

1. Those claiming the childcare element and with CTC above the family element.
2. Proportion of childcare costs allowed increased from 70% to 80% on 6 April 2006. The higher rate would be reflected in the December 2006 snapshot onwards. The April 2006 snapshot was taken on 5 April 2006 so would be based on 70% of costs allowed.
3. Source: HMRC Provisional Statistics at snap shot dates available at <http://www.hmrc.gov.uk/stats/personal-tax-credits/cwtc-quarterly-stats.htm>

Further analysis of the number of families receiving the child care element of the Working Tax Credit can be found in the statistics published on our website at <http://www.hmrc.gov.uk/stats/personal-tax-credits/cwtc-quarterly-stats.htm>

3. Q233–Q235: MARK TODD

A summary of the status of HMRC IT resources.

Our IT systems have evolved over a number of years, and the IT estate has grown in size and complexity. The IT estate has changed to incorporate the merger of HM Customs and Excise and Inland Revenue, and as new policies have arisen, we have also made further additions to the IT estate.

There are 92 systems which are critical to HMRC's core processes. These have been subject to significant investment over the last two to three years; including programmes such as Carter and the new PAYE service. The availability of core systems remains in line with industry comparisons; with 99.74% availability. The remainder of the Departments systems differ and vary in terms of performance and quality. Our strategy is to consolidate systems, remove complexity and prioritise investment where it will make the greatest difference.

During 2008–09 HMRC have also invested in the IT infrastructure that supports the “core” systems, closing two old data centres, updating key infrastructure and improving security

The agreement with Aspire, announced on 29 October, will provide some of the investment to further standardise, simplify and modernise the IT estate.

4. Q239–Q240: MARK TODD

Information on HMRC plans to mitigate the IT disaster recovery risk.

113 of HMRC’s systems are considered as high priority for support within the Departmental Business Impact Assessment (DBIA). HMRC have 46 systems that have formal IT Disaster recovery (DR) in place. Three systems do not require IT DR, and all other systems, where appropriate, have regular back up and system documentation maintained.

During 2008–09 investment in DR has been targeted at firstly the high priority areas of SA online and Tax Credits payments and secondly at reducing the likelihood of incident by closing two old data centres and relocating key systems.

Further mitigation of this risk remains a priority for the department, with further measures being considered as part of the HMRC’s 2010–11 Business Planning round.

5. Q260: NICK AINGER

The pattern of Senior Civil Servant (SCS) departures over time.

In 2006–07 the rate of departures in the SCS was almost identical to the overall staff departure rate (10.15% of SCS population compared to 10.92% of overall staff population). In 2007–08 the number of SCS departures increased by 15 from the previous year to 55 as did the rate of departure when compared with overall staff leavers (14.03% for SCS compared with 8.81% overall). Although there was a slight reduction in the number of SCS departures in 2008–09 (49), the rate of SCS departures remained higher than the overall staff departure rate (12.34% for SCS compared with 8.48% for overall group).

Of all other grades, only clerical Grades (AA/AO) have a higher percentage rate of leavers. These are the grades which have seen the most change in type of work through automation of tasks and also tend to be the grade levels with the least established career.

The rate of SCS leaving as a result of early departure/release schemes has increased steadily each year, from 2.4% in 2006–07 to 5.4% in 2008–09. The only other grade groupings where there has also been a year-on-year increase is at AA/AO. Over the same three-year period the rate of resignations within the SCS has fluctuated from 3.1% in 2006–07, up to 3.8% in 2007–08, and down to 1% in 2008–09.

Retirement rate at SCS more than trebled between 06/07 and 07/08 (from 3 to 10) and in 2008–09 remained static at around 2.5% of the SCS population size.

SCS departures from mainline “tax professional” business areas have accounted for 28.5% of all SCS departures in 2006–07, 20% in 2007–08 and 31.5% in 2008–09.

SUMMARY OF DEPARTURES AS A % OF STAFF IN POST IN EACH CATEGORY:

<i>Leavers</i>	<i>SCS</i>	<i>G6</i>	<i>G7</i>	<i>FS</i>	<i>SO</i>	<i>HO</i>	<i>O</i>	<i>AO</i>	<i>AA</i>	Total
06/07	10.15%	12.58%	8.93%	5.29%	8.23%	6.40%	5.86%	11.41%	23.56%	10.92%
07/08	14.03%	7.06%	6.00%	7.12%	5.58%	6.00%	4.93%	9.93%	16.73%	8.81%
08/09	12.34%	6.12%	4.89%	7.81%	5.27%	5.73%	5.22%	9.87%	15.37%	8.48%

6. Q244: MARK TODD

How HMRC Value for Money commitments relate to each other.

There are three distinctive and separate HMRC initiatives mentioned in sections 4.4 and 4.5 of the 2009 Value for Money Update, published April 2009 (HM Treasury’s website). These are:

- new enhanced online services for Self assessment, PAYE, VAT and Corporation Tax to encourage online filing;
- steps to rationalise and develop a more strategically located estate to better meet customer service and operational requirements; and
- the simplification and consolidation of back office functions and activities.

All of these initiatives will deliver lasting efficiencies and other benefits. Processes, which were examined as part of the NAO’s 2008 review of the HMRC’s Departmental Transformation Programme, are in place to ensure that these efficiencies and benefits are all measured and reported separately. There is therefore no overlap or double counting in the reporting of these benefits.

7. Q264: NICK AINGER

The numbers of bankruptcy petitions sought by HMRC year on year.

The figures of HMRC Petitions filed in the UK are as follows:

	<i>Bankruptcy Petitions filed*</i>	<i>Winding up Petitions filed</i>
2006–07	10,982	6,954
2007–08	8,616	6,100
2008–09	8,784	4,397
2009–10 (to Sept)	3,999	2,056

* In Scotland these are Sequestration Petitions

Mr Ainger also requested assurance that the department is keeping its policy on supporting Voluntary Arrangements under review. A copy of the HMRC published guidance is attached at Annex 2.

8. Q253: MARK TODD

The relationship with Mapeley with regard to office reductions and the Department's flexibility under the STEPS Contract.

Under the terms of the STEPS Contract, Mapeley are responsible for the negotiation of rent, lease renewal, the disposal of surplus space, and other property related transactions.

In exchange for receipt of an annual facility price, Mapeley are responsible for ensuring that the Department's ongoing accommodation needs are met, at least until such time as HMRC has vacated, following appropriate service of notice. Facility specific vacation notices can be served by HMRC without direct reference to the underlying lease position.

HMRC's occupation of facilities is governed by STEPS leases and/or virtual assignments and each facility has a contractual designation of Core, Flexible or Intermediate. The ability of the Department to vacate any or all of these facilities during the life of the contract at nil cost was/is constrained as follows:

Core

Approximately 71% of the estate (969,000m²) had this designation at STEPS Contract award. The department had no vacation allowances for the first three years of the contract, but in each of years 4–18, HMRC was and is permitted to vacate 15,000m² per annum without a penalty payment to Mapeley. Any unused allowances roll forward into subsequent years to become the Aggregate Core Allowance and can be used at any time upon 12 months notice. Any underlying leases which continue remain the direct responsibility of Mapeley under the STEPS Contract risk transfer arrangements, which include ongoing costs (eg rent and vacant space rates) and liabilities (eg repairing covenants and dilapidations).

In each of the years 4–18 the department has a Further Core allowance of 15,000m² per annum, and can vacate on 12 months notice subject to, and upon payment of, overhead compensation only. Despite the payment of compensation, Mapeley continue to have direct responsibility for any underlying leases including costs and liabilities.

Flexible

Approximately 13% of the estate (175,000m²) had this designation at STEPS Contract award. In year 1 HMRC could vacate 2,500m², in each of years 2–5 5,000m², and in each of years 6–15 15,000m². Within these allowances and contract provisions, HMRC can exercise its vacation rights upon 12 months notice.

As with Core, any unused allowances are rolled forward into the following contract years and vacation is without penalty.

Intermediate

Approximately 16% of the estate (212,000m²) had this designation at STEPS Contract award. There are no vacation allowances as such, for Intermediate facilities, but each facility was given a Transition Date which determines flexibility. The Transition Dates are specific to each Intermediate facility and the Department has the right to vacate on the Transition Date at no penalty, providing that at least 13 months notice has been given and contract provisions satisfied. Once the Transition Date has passed, the Department can issue a minimum of 12 months notice to vacate two years after the Transition Date or at any time thereafter, also without penalty payment to Mapeley.

Qualifying Change

If at any time HMRC wishes to vacate properties in addition to the allowances and in any given year, then HMRC would have to issue a minimum of 12 months Qualifying Change notice and meet Mapeley's "Change in Costs". These costs might reasonably include ongoing rent, rates and LSC, and marketing/sub letting etc.

In making use of its allowances, HMRC is seeking to work as strategically as possible with Mapeley, while making use of the value for money flexibility which the Department has available.

November 2008

Written evidence submitted by the Office of Government Commerce

Under key goal 1 (delivering value for money from third party spend) did you, as promised in your Annual Statement 2008 document (P10), identify by end 2008 the target for value for money savings over the CSR07 years and, if so, what is it?

The CSR07 target for value for money from third party spend across common goods and services is £4 billion per annum by 2010–11 when compared to 2007–08 spend. Under the Operational Efficiency Programme (OEP), announced in the budget earlier this year, we anticipate that savings will be £7.7 billion per annum by 2013–14. This includes £1.6 billion savings on the collaborative procurement of IT. These savings were also identified in the OEP as part of the savings available from work to reform back office operations and IT.

Did you complete a further Public Sector Expenditure Survey in 2008–09 (P11) and, if so, what were the main findings?

The PSPES survey of procurement spend for 2008–09 was completed at the end of October and the results are currently being analysed. High level results for PSPES 2008, to category level, will be published in by March 2010.

To what extent are the top contracts within each procurement category fully compliant with the best value for money criteria (P12)?

Value for Money calculations for Collaborative Procurement are performed in strict accordance with Treasury VfM Guidelines which were published at the start of the CSR07 period. The way in which benefit is calculated for each deal is documented and quality assured by a central programme office in the Office of Government Commerce (OGC), and supported by third party management information.

Under key goal 2 (delivering projects to time, quality and cost, realising benefits) have you now rolled out the "starting gate assurance tool" you were piloting and appraising during 2008 for new high-risk policy initiatives (P16)?

OGC formally introduced Starting Gate reviews from April 2009 after successfully piloting the approach. To date, 13 Starting Gate reviews have been carried out for nine departments/agencies with a further six reviews in the immediate pipeline (ie to end March 10). The OEP recommended that Starting Gate reviews should be introduced for all major IT enabled projects. OGC has also introduced a radically different approach to Gateway Reviews based on delivery confidence rather than "urgency of recommendation". It now escalates to the Permanent Secretary and the National Audit Office (NAO) as soon as a project is reported as Red for delivery confidence rather than waiting for a second Red—often with over a year's gap. OGC has also introduced Assurance of Action Plans (AAP) to assure confidence in the plans for recovery on projects which are Amber/Red or Red. To date, 10 pilots have been undertaken. Latest feedback from Senior Responsible Officers (SROs) indicates extremely strong approval for the new processes and their impact on delivery confidence.

Under key goal 3 (getting the best from the Government estate) what progress have you made towards your goal of achieving savings of £1–£1.5 billion per year in the running of the civil estate (P21)?

The delivery of savings under the High Performing Property initiative is being calculated and monitored via the movement in the cost of the central Government estate each year.

This calculation was done for the first time for the *State of the Estate* in 2008 (SOFTE) report that was laid before Parliament on 1 June 2009. The calculation comprised of using as the first baseline, the cost of the estate in 2003–04 which was the year that the current drive to improve the central Government estate started (with Sir Michael Lyons' reviews of Government relocation and improvements on the management

of public sector assets), compared to the second baseline of 2007–08—the latest year for which costs were available. The difference between the two amounts is £532 million which is being scored as the actual savings achieved since HPP was introduced against the target of between £1 billion and £1.5 billion by 2013.

The estate cost exercise is being repeated for 2008–09 and the results will be reported in the SOFTE 2009 report.

Under key goal 4 (delivering sustainable procurement and sustainable operations on the Government estate) what progress have you made [during 2008–09] towards reducing Government carbon emissions, waste arising and water consumption from offices (P22 of the Annual Report)

The latest performance results, for the year 2008–09, for sustainable operations on the government estate (including carbon emissions, waste arisings and water consumption) are due to be published by the OGC in December 2009 (covering the period 2008–09).

The results for the year 2007–08 showed the Government receiving a “green” rating from the Sustainable Development Commission for its progress against four of the major targets, on carbon from travel, waste arisings and recycling and on water. However, future progress needed to be urgently made on carbon emissions from offices, which SDC rated as “amber”, at a total reduction of 6.5% against the 1999 baseline. The government’s delivery plan for sustainable development in government, last updated in July 2009 showed that plans are now in place to ensure that the target for a 12.5% reduction is exceeded when it falls due in 2010–11. A further update will be published in December 2008.

What hard evidence can you point to, to counter allegations that you lack the necessary clout to change Departmental culture?

The powers available to OGC to change departmental culture does include some mandation of process or delivery but also includes: influence through transparency; escalation such as Treasury’s MPRG; benchmarking; engagement with the Ministerial, Permanent Secretary and Professional communities; and importantly governance of collaborative processes. There are many examples in each of these categories ranging from the Procurement Capability Reviews (PCRs) process, through to Collaborative Procurement Category Boards, and personal objective setting for Commercial Director community, which I will be happy to discuss at my next committee hearing.

With respect to the specific example you quoted of the NAO report on complex procurement I would point out that the NAO identified a lack of systemic assessment of skills for projects outside those in the £200 bn portfolio of Government’s major projects. By definition it recognised that there is an assessment for these major projects. This is an important initiative which has been developed since the last time the Committee sat to review OGC. As a result of this process I can assure the Committee that it is not the case that all of these Major Projects are at risk through skills and capability gaps and indeed this was recognised by the NAO in the summary and main body of its report. It also clearly identified the Departments as having primary responsibility for skills and capability development, supported by OGC.

There is much to be done but progress is being made and I look forward to discussing areas for development with the Committee in the near future.

What are you doing to ensure that the relevant departments act to address these deficiencies (as identified by the PCRs)?

Each department has been required to publish, as part of the PCR process, an action plan which sets out how the departments will act to address the issues identified in the Review. I meet with Permanent Secretaries on a six monthly basis to review action against those plans.

Where the PCRs have identified issues that affect the government procurement service as a whole, OGC is now in the process of setting up cross-departmental best practice sharing groups on key cross-government issues—for example Supplier Relationship Management.

Has the ruling affected the conduct of subsequent Gateway Reviews and, if so, how?

The High Court hearing delivered its ruling in April 2008 following an Information Tribunal hearing in 2007. The High Court quashed the original Information Tribunal ruling on a point of parliamentary law and ordered that the case go back to a re-constituted Tribunal. This second Information Tribunal ruled in February 2009 that the ID cards reviews should be released since the public interest in the ID cards scheme, at the time of the initial FOI request, outweighed the public interest in protecting the Gateway process.

Both the Judge at High Court and the final Information Tribunal stated that they did not disagree with the Ministry of Justice working assumption that directs that Gateway reviews under two years old will, in most cases, have key information withheld when requested under FOI. The Information Tribunal also stated in its ruling that neither it nor the Information Commissioner believe that all Gateway reviews should be published.

The ruling has not, thus far, materially affected the conduct of Gateway reviews, nor has it necessitated a change in the way in which the OGC responds to FOI requests for Gateway reviews, which remains to follow the MOJ working assumption.

Have your staff cuts since 2007 left you with insufficient capacity?

I believe that OGC, which currently had a headcount of around 300 staff, has sufficient capacity to carry out its functions.

Whilst it is true that plans to enhance the efficiency of OGC were implemented in 2008, reducing staff by 20%, we have since the OEP created and are well advanced with plans to recruit teams to address two new collaborative procurement categories—facilities management and construction—and the implementation of the Glover report on Small and Medium Enterprises.

What actions have Buying Solutions taken to address the concerns expressed by the PAC Committee in June 2007?

Prior to the report, Buying Solutions were already undertaking a major consolidation of framework agreements as well as concluding that a number of uneconomical frameworks would not be renewed. During financial year 2008–09, Buying Solutions managed £5.35 billion of Public Sector expenditure through 80 framework agreements, whilst maintaining a customer-centric portfolio of goods and services. During financial year 2009–10, Buying Solution growth in managed spend to date is 25% higher than the previous year. Reviewing framework requirements is an ongoing part of our operating model and is also carried out in the context of the broader collaborative governance. We aim to balance customer requirements; operating efficiency and special needs.

Buying Solutions has continued to invest in both the Government Procurement Card and Memorandum of Understandings (MoUs) in line with its vision of Savings for the Nation. In 2009 a revised MoU was signed with Microsoft giving even greater savings to the UK public sector and work has commenced on a similar renewal with the Oracle MoU. In addition we have also embarked on a framework for supported workshops which will enable public sector organisations to acquire goods and services from this specialised sector.

How much did it cost to re-brand as Buying Solutions, and what has it achieved?

The cost of re-branding Buying Solutions was £28,000. The purpose of the re-branding was to enable the organisation to differentiate itself from the OGC thereby clarifying the respective roles of both bodies. In addition it enabled Buying Solutions to increase the organisation's relevance and support to the wider public sector and not be seen simply as part of central government. In terms of achievement, Buying Solutions is in the process of undertaking a brand tracking exercise designed to measure awareness and understanding across the public sector which will give evidence-based achievement data.

December 2009

Supplementary written evidence submitted by Royal Mint

I am writing in response to the letter I received from Mr Michael Fallon MP, Chairman of the Treasury Sub-Committee on 12 November 2009, requesting clarification on two points, following my appearance before the Treasury Sub-Committee. I set out below my response to the matters raised:

TRANSFER BETWEEN THE REVALUATION RESERVE AND THE PROFIT AND LOSS ACCOUNT

The vast majority of the £8 million transfer (£7.806 million to be more precise) between Revaluation Reserve and the Profit and Loss Account related to a change in accounting policy, to record what is referred to internally as our “Base Stock” of metals on a FIFO basis, as opposed to a historical cost basis, as was previously the case.

Prior to last year, the price movements in metal of our “Base Stock” were simply reflected by an increase or a decrease in the revaluation reserve. So, in accounting terms, an increase in the value was treated as:

Dr Inventory

Cr Revaluation Reserve

and vice versa in the case of a decrease in value.

The prior method was inconsistent with UKGAAP, which is the basis for Government Financial Reporting. To be clear, this adjustment did not impact the reported profitability of the Royal Mint. It was simply a transfer between two accounts within Government Funds, to reflect the fact that the prior treatment was no longer being adopted. There is no physical transfer of money either. This is simply a Financial Reporting Issue, and we do not anticipate any transfers of a similar nature next year.

FUTURE CONTRACTS WITH HM TREASURY

The Royal Mint and HMT have negotiated an arms length contract to supply UK coinage to HMT for a five year initial period followed by a three year termination period. The contract will therefore expire no earlier than 2018. The contract also provides for the production and sale of Commemorative coins, for which HMT are paid a Royalty.

The contract also provides for general service and advice on coinage and coinage related matters such as design, counterfeiting and security.

The value of the contract to the Royal Mint depends on the volume and mix of coins required by the UK economy over the life of the contract, and the value of metal prices over the period, as well as our ability to sell Commemorative Coins. In total this continues to be the most significant contract that the Royal Mint has, representing C.20% of the Circulating Coin business contribution and the vast majority of the Commemorative Coin business contribution.

20 November 2009

Written evidence submitted by the Crown Estate Commissioners

THE NATURE OF THE CROWN ESTATE'S RELATIONSHIP WITH THE TREASURY

In accordance with The Crown Estate Act 1961, The Crown Estate provides the Treasury with all the information about the Estate's activities which the Treasury requires. In practice, the Treasury is kept regularly informed of the Estate's business and any significant initiatives so as to enable the Treasury to satisfy itself that the Estate is performing its duties. There are two formal annual meetings; in the spring on the corporate plan and revenue targets; and in the autumn on the investment strategy. There are also less formal meetings and other collaborative contacts through the year as the flow of business requires. The Crown Estate Act also confers on the Treasury and the Secretary of State for Scotland, a power of direction over the discharge of the Estate's functions but this has never been exercised because of the arrangements described above.

1. *Can you go into more detail about your business strategy, business partners, and the proactive role The Crown Estate intends to play in these new initiatives [in the development of renewable energy]?*

Our Business Strategy

Our business strategy is to facilitate and participate in the development of the commercial opportunities in renewable energy on the Marine Estate, to play our part in helping the UK meet its renewable energy targets and to work in close conjunction with our stakeholders. As custodians of vitally important national assets, we have a clear responsibility to safeguard those assets and to manage them sustainably.

Our Proactive Role

- There is an opportunity to establish a considerable industrial sector within the UK to meet the investment needed for the development of offshore renewables in the UK. In order to help stimulate UK investment in this supply chain, we have invested in the development of wind turbine technology to be manufactured in the UK. We are currently investigating the potential to invest further in ports and logistics to support offshore construction, operations and maintenance over the next five years.
- We have committed capital funds of over £120 million—on, for example, scientific assessment, technical evaluation and project development—to help industry accelerate the deployment of offshore wind farms and wave and tidal technology.
- We are investing in the collection of data with a management information system tool (MaRS—Marine Resource System) to process this data to provide detailed knowledge of the physical, scientific and technical characteristics of the UK's coast, sea bed and seas. This highly advanced system is recognised as probably unique across the world's maritime nations. The Scottish Government and UK Marine Management Organisation are considering using it to assist with their marine spatial planning obligations.
- We have recruited and continue to recruit people with appropriate skills and experience.

Our Business Partners and Stakeholders

- Our business partners are commercial enterprises who are currently operating offshore renewable energy projects (including RWE, E.ON, Centrica, EDF, Dong, Scottish and Southern Energy, ScottishPower, Vattenfall) and those who have expressed an interest in doing so in the future.

- The Crown Estate has established strong relationships with the UK Government, the devolved administrations in Scotland, Wales and Northern Ireland, coastal communities, statutory bodies with marine interests, NGOs and other commercial sectors who have parallel commercial activities to The Crown Estate's.
- We work closely in conjunction with stakeholders with marine interests such as environmental interests, shipping, aviation, fishing, aquaculture, ports, harbours and marinas.

2. *Last year renewable energy brought in revenue of £1.8 million. What figure do you project to earn by 2020?*

Revenue rental income forecasts are based on three scenarios of energy generation and the projected revenue rental income is expressed in current energy prices. After defraying costs the surplus from this activity will of course be paid over to the Treasury for the benefit of the UK tax payer.

- Scenario 1—total operating capacity 14 GW: potential revenue rental income £66 million for the year 2019–20.
- Scenario 2—total operating capacity 28 GW: potential revenue rental income £143 million for the year 2019–20.
- Scenario 3—total operating capacity 42 GW: potential revenue rental income £221 million for the year 2019–20

3. *Are you now confident you have got sufficient expertise to ensure the successful development of the renewable energy sector?*

Yes. We have significantly increased the specialized expertise in our Marine Estate by recruiting some of the most qualified and experienced individuals from companies such as Merrill Lynch, RWE, NPower, BP, Royal Dutch Shell, E.ON, AGIP and British Aerospace and from consultancies such as Ove Arup and RPS. We have also recruited from other organisations such as the Met Office, Natural England, the Environment Agency and Greenpeace and from Glasgow, Newcastle and Southampton Universities. Contractors and consultants provide technical expertise and support to complement the knowledge, skills and abilities of our employees at various planned stages of projects. We also use professional advisors on commercial, legal and financial matters. Because of our expertise, we have been approached by the US and several European countries who want to know more about our initiatives in offshore renewable energy.

4. *Who is on the Offshore Energy Supervisory Committee and how will it benefit the Crown Estate?*

The Offshore Energy Supervisory Committee (OESC) was established in order to provide the Crown Estate Board with specialist advice on energy-related matters including wind, wave and tidal power together with CO₂ and natural gas storage. The OESC is chaired by Roger Bright, the Chief Executive of The Crown Estate. The other members are:

- John Burnham—formerly MD and Head of Infrastructure for Citigroup Global Markets Ltd.
- Matts Lundgren—currently the Managing Director of Allianz Capital Partners, a private equity company based in Germany.
- Dipesh J. Shah—formerly the Chairman of Viridian Group Plc and of Hg Capital Renewable Power Partners Llp; formerly Chief Economist of BP and Chief Executive of UKAEA; he is a non-executive director on several Boards, including Lloyd's of London Franchise Board, Thames Water, Babcock International Group Plc and JKC Oil and Gas Plc.
- Chris Geoghegan—formerly Chief Operating Officer of BAESystems, now Chairman of Hampson Industries Plc; he also holds several non-executive director posts including Kier Group Plc and Volex Plc.
- David Fursdon, Crown Estate Board member.

The members of the OESC draw on their experience and expertise in energy generation and transmission, economics and regulation, infrastructure investment and the energy supply chain.

5. *What is the reason for the delay in concluding the leasing stage of your plan [for wave and tidal power in the Pentland Firth]?*

We recognise that we should have made it clear in our September 2008 press release that the date of summer 2009 was indicative. We should have spelt out more clearly the uncertainties: that this is the first programme of its type in the world and highly complex and that the statutory and regulatory process was at that stage still being developed. In addition, there was an unexpectedly high level of interest expressed by the market and a number of challenges to the competition process. Nevertheless, we should emphasise that preparatory work is well underway and delivery of the target of 700 MW of installed capacity by 2020 remains on schedule.

6. *Are you confident that you have the expertise required to keep the UK at the forefront of the tidal power generation industry?*

In order to keep the UK at the forefront of this industry, there are essential roles not only for The Crown Estate but also for the UK Government, the devolved administrations, the investor community and the wider industry, with all of whom we are working closely. For our part we have recruited individuals into the Marine Estate who are recognised as being at the forefront of their fields. They are specialists with expertise in areas including: environmental management; renewable energy and transmission technology; commercial management of development projects; and project management. As the industry develops we will seek to recruit further suitably qualified individuals.

7. *What criteria do you take into account when setting rent levels for off shore wind farms?*

The objectives laid down by Parliament require The Crown Estate to earn a surplus which goes to the Treasury for the benefit of the UK taxpayer and to enhance the value of the estates we manage without exploiting any monopoly position. These considerations contribute to the determination of the appropriate rent levels for offshore wind farms.

The Crown Estate charges rent at 2% of the value of the electricity generated by a wind farm. Market rates for onshore wind farms are typically in the range of 4% to 10%, and in producing a rate for offshore wind farms these onshore rates have been discounted to take account of the additional capital cost, construction and operating risk of offshore wind farms and the additional complexity of working in an offshore environment.

Rental levels for Rounds 1 and 2 leases are linked to the Retail Price Index. Rental levels for Round 3 projects will be linked to a basket of indices, (some of which are recently established), which are more aligned to those specifically relating to renewable energy.

8. *How confident are you that leases for nine new offshore schemes will be awarded by the end of the year?*

The leases are currently on schedule to be signed by The Crown Estate and nine zone development partners by the end of December 2009. The preferred bidders were released from confidentiality to engage with third parties to take their projects forward and meet their target of 25 GW of installed capacity by 2020. Conclusion of this process is subject to negotiation with the preferred bidders and subject to compliance with statutory requirements for appropriate assessment.

9. *How does "The Business Deal" benefit your tenants?*

10. *How has it been implemented across the whole Crown Estate?*

"The Business Deal" is a Rural Estate initiative which we have developed with our tenants in order to enhance landlord:tenant partnerships.

Tenants will benefit from:

- improved clarity and transparency in the relationship;
- improved business efficiency;
- enhanced communications; and
- direct access to capital for new business opportunities, including the promotion and marketing of high quality products and services.

We have already found that this has created mutually beneficial business opportunities.

As a key component of our "Customer Focus Project", our Marine and Urban Estate teams are considering whether the Business Deal—in a suitably tailored form—has the potential to add value to their relationships with their tenants.

11. *What lessons have you learned from the financial crisis as regards property investment? Have you changed your approach to investing in property?*

The Crown Estate pursues a long term investment strategy with a view to weathering the vagaries of the market. While our portfolio has of course been affected by the financial crisis, it has been considerably more resilient than the market average as measured against recognised industry benchmarks. This has confirmed the robustness of our business model: a diverse property portfolio; high quality assets; active management of our assets; and measuring financial performance not just year on year but also over the long-term.

Our diverse portfolio includes central London offices and retail, residential, major retail schemes, business parks and industrial estates, rural land and marine holdings. With the advantage of being able to take a long term view, this diversity helps us withstand the vicissitudes of the property market.

So recent events have not caused us to change our overall approach. We will continue to focus on our core sectors. At the same time we aim to take tactical opportunities to trade between sectors and so to manage our scarce capital effectively to generate durable returns.

12. *Why did you not record progress against the Going for Gold targets?*

13. *What is your current progress against these targets?*

Our view was that readers of our 2009 Annual Report would find it more useful if we illustrated our progress against the Going for Gold targets through the achievements and case studies reported throughout the report. However, we do report progress during the year to our Management Board and Main Board. Our Going for Gold targets are designed to distil the essence of our corporate objectives into an easily understandable format. A summary of progress against each Going for Gold target is attached in the annex.

Annex

GOING FOR GOLD TARGETS

<i>Going for gold target</i>	<i>Current progress</i>																				
#1 Achieve a revenue contribution to the Treasury of £250 million	We anticipate achieving a revenue surplus target of £200 million in 2009–10; at the half year stage we were ahead of target. The investment strategy which underpins our financial strategy, both of which are reviewed annually, forecasts that £250 million may be achievable by 2014.																				
#2 Consistently outperform the IPD total return index	We now use an annual (IPD) Crown Estate bespoke benchmark at estate level which reflects the balance of The Crown Estate's assets. Also, the urban portfolios are revalued and analysed quarterly. Over the first half of this financial year they outperformed overall with the breakdown being as follows: <table border="1" data-bbox="561 814 1367 1002"> <thead> <tr> <th></th> <th><i>6 month total return</i></th> <th><i>IPD benchmark</i></th> <th><i>Relative</i></th> </tr> </thead> <tbody> <tr> <td>Regent St</td> <td>0.5%</td> <td>2.1%</td> <td>– 1.6%</td> </tr> <tr> <td>London</td> <td>3.9%</td> <td>0.8%</td> <td>3.1%</td> </tr> <tr> <td>Diversification</td> <td>3.2%</td> <td>1.1%</td> <td>2.1%</td> </tr> <tr> <td>Overall</td> <td>2.4%</td> <td>1.4%</td> <td>1%</td> </tr> </tbody> </table>		<i>6 month total return</i>	<i>IPD benchmark</i>	<i>Relative</i>	Regent St	0.5%	2.1%	– 1.6%	London	3.9%	0.8%	3.1%	Diversification	3.2%	1.1%	2.1%	Overall	2.4%	1.4%	1%
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#3 Achieve gold in the Business in the Community (BitC) Corporate Responsibility Index	We plan to make a formal submission to the BitC Corporate Responsibility Index in 2010. Having undertaken a gap analysis in consultation with BitC, we are working through the resulting actions as part of the implementation of our sustainability strategy. As a marker of progress we are working to achieve Silver in the 2010 Index. In September we appointed a Head of Sustainability to take our sustainability strategy forward under the guidance of our Sustainability Committee and embed it within the business. This strategy is based on four key pillars: tackling climate change and energy security, working together, sustaining communities and driving environmental value.																				
#4 Enter the Sunday Times' list of good employers	We are participating in the Best Companies Accreditation and <i>The Sunday Times</i> Top 100 Companies to Work For survey for the first time this year.																				
#5 Win more nationally recognised awards	Recent successes include: <ul style="list-style-type: none"> — Building Public Trust award for annual report and accounts <i>Recognition in the Public Sector for Excellence in Reporting</i> for our 2008–09 Annual Report; — Building Public Trust Award for <i>Sustainability Reporting in the Public Sector</i> for our 2008–09 Annual Report; — Estates Gazette award for National Property Company of the Year, Retail and Leisure; — the Green Award for our Glenlivet estate in the Highlands and Islands Tourism Awards 2009. 																				
#6 Establish a strong and respected customer brand, supported by excellent service from us and our service partners	An internal group has been exploring the means by which high standards of customer focus and management can enhance the business performance of The Crown Estate. We are now working on drawing conclusions from our pilot areas and at the same time we are looking at our internal customer culture—how we work together and with others.																				
#7 Establish partnerships with other property owners through a flexible approach to investment and disinvestment	Partnering remains a key tool for The Crown Estate to achieve its investment objectives. In addition to our already established relationships with Hercules/Aviva/Lend Lease we are working on further initiatives across our portfolio and hope to make further announcements on progress during the current financial year.																				

<i>Going for gold target</i>	<i>Current progress</i>
#8 Ensure Crown Estate employees and representatives actively embrace our core values	We use a variety of internal communication channels to highlight our core values, in particular we hold annual (six monthly in some parts of the business) sessions to share information about the achievements and direction of the business and invite questions in an informal setting. The key messages are taken out to our principal service partners at appropriate occasions such as estate conferences. Publications such as our Corporate Plan (internal) and Report and Accounts are also used to reinforce our key messages.
#9 Ensure we are regarded by our stakeholders as indispensable	We work to achieve this in all that we do but we place great emphasis on our relationships with stakeholders. We have developed a stakeholder management system linked to an external relations risk register and a public policy/regulator relations monitoring system. We are about to embark upon a reputational piece of research by Mori.

December 2009

Supplementary written evidence submitted by HM Treasury

FURTHER MATERIAL REQUESTED AT THE EVIDENCE SESSION ON 11 NOVEMBER 2009

Short notes are attached here on the following subjects. The committee questions referred to are in brackets.

- Accounting for the fall in net borrowing (Q. 296).
- HM Treasury's interaction with UK Financial Investments (Q. 304).
- Benchmarking procurement practice (Q. 306).
- Pensioners and tax allowances (Qs. 330–332).
- Child poverty (covering issues raised in Qs. 327, 329, 334, 339, 345–349, 378, 385).

HM TREASURY'S INTERACTION WITH UK FINANCIAL INVESTMENTS

This note clarifies the principles governing the exchange of information between HM Treasury and UK Financial Investments (UKFI) and, specifically, consultation with UKFI on due diligence information that was in the Treasury's possession.

UKFI was set up to manage Government's shares in financial institutions at arm's-length and on a commercial basis. UKFI's objective is to dispose of the investments in an orderly and active manner, within the context of an overarching objective of protecting and creating value for the taxpayer, paying due regard to financial stability and promoting competition.

The Treasury's relationship with UKFI is set out in more detail in UKFI's Framework Document and Investment Mandate.¹ In carrying out its functions, UKFI acts as an engaged and informed institutional shareholder.

As stated at the hearing, only the Treasury is in a position to take decisions from the perspectives of both fiscal and financial stability. In consulting with UKFI on the recent announcements, the Treasury sought to balance financial stability and value for money objectives with the need to avoid compromising UKFI's status as an engaged and informed shareholder in the banks.

Both UKFI and the Treasury take care at all times to respect their legal obligations in respect of the information they hold and share, including legislation on insider dealing and market abuse, and conditions which apply when confidential information provided for the purpose of the Asset Protection Scheme (APS) and financial stability is transferred between the two organisations. This includes confidentiality agreements signed with the banks, and FSA regulations on the disclosure of regulatory information.

Over the course of the APS negotiations, the Treasury sought UKFI's views on the market reaction to each bank's participation in the APS, Lloyds's alternative capital raising proposal and the implications for shareholder value. UKFI was also consulted on final advice to Ministers to ensure that UKFI's views were accurately reflected. Information discussed with UKFI included:

- Treasury's analysis of the banks' capital models;
- the structure of B shares and the contingent capital instruments;

¹ <http://www.ukfi.gov.uk/releases/Framework%20Document%20July%20Revised%20Version.pdf> and <http://www.ukfi.gov.uk/releases/UKFI%20Mandate.pdf>

- RBS strategy for raising capital and balance sheet structure, including liability management proposals; and
- State aid disposals.

Information provided by the banks, and seen by UKFI, has been reflected in public disclosures that have since been made by Lloyds and RBS.

Given the Treasury's wider responsibilities for financial stability, and its role as a member of the Tripartite, the Treasury is also in possession of information that was not provided by the banks, such as the results of its own due diligence. At UKFI's appearance before the TSC on 4 November, John Kingman correctly reported that no such due diligence information was shared between the Treasury and UKFI. Detailed information on the FSA's stress testing was not shared. This was because the Treasury judged that advice from UKFI was not required. In cases where further advice was needed, the Treasury sought that advice from Treasury's financial and legal advisers.

ACCOUNTING FOR THE FALL IN NET BORROWING FROM 2009–10 TO 2013–14

The 2009 Budget forecasts net borrowing to fall from 12.4% of GDP in 2009–10 to 5.5% of GDP in 2013–14. In cash terms, borrowing is projected to fall by £78 billion over that period, from £175 billion to £97 billion. The table below breaks down the annual fall in net borrowing relative to 2009–10 between cyclical changes and other factors, and discretionary measures.

<i>% of GDP</i>	<i>2009–10</i>	<i>2010–11</i>	<i>2011–12</i>	<i>2012–13</i>	<i>2013–14</i>
Net borrowing	12.4	11.9	9.1	7.2	5.5
Change in net borrowing since 2009–10	–	–0.5	–3.3	–5.2	–6.9
<i>of which</i>					
<i>Change in net borrowing due to cyclical and other factors</i>	–	1.4	–0.3	–1.2	–2.2
<i>Change in net borrowing due to measures (PBR 08 + BUD09)</i>	–	1.9	–3.0	–4.0	–4.7

Almost 70% of the fall in net borrowing between 2009–10 and 2013–14 reflects the impact of discretionary measures announced in the 2008 Pre-Budget Report and the 2009 Budget, including the reversal of the fiscal stimulus.

Just over 30% of the reduction is driven by cyclical and structural changes to borrowing largely driven by economic growth. Structural improvements include forecast recovery in the financial sector, supporting income tax and corporation tax receipts, and rises in asset prices, boosting receipts from stamp duties.

The change attributable to measures includes the reversal of the temporary VAT cut announced in the 2008 Pre-Budget Report. If the reduction in VAT is excluded from the 2009–10 baseline for net borrowing, discretionary measures would account for just over 60% of the fall in net borrowing between 2009–10 and 2013–14, and structural and cyclical factors almost 40%.

PENSIONERS AND TAX ALLOWANCES

The Committee asked why some pensioners do not claim tax allowances to which they are entitled, and asked what HMRC are doing to help pensioners to claim back tax they may have overpaid on their savings income.

On tax allowances for people aged 65 and over, the figure quoted by Mr Cousins appears to have come from the NAO report, "HM Revenue & Customs: Dealing with the tax obligations of older people", published on 23 October 2009. Most of the 3.2 million people who the NAO estimate do not claim their full age-related personal allowance already have a total income below this level. These people do not pay any tax (provided they register to receive their savings income tax-free) and are not required to inform HMRC of their tax situation. This group would derive no benefit from claiming a higher allowance, which is why their allowance may go "unclaimed".

Tax on savings income is collected automatically at source, at a rate of 20%, by banks and building societies. For most people this means they pay the right amount of tax, without having to worry about filling in a tax return. There are, however, some people who should pay no tax, or the lower 10p starting rate, on their savings income. Those individuals can claim back any tax that has been overpaid. Non-taxpayers can also instruct their banks or building societies to pay their interest tax-free. HMRC is currently contacting 3.4m pensioners as part of its latest "Taxback" campaign, which aims to ensure that pensioners do not overpay tax on their savings income and that they claim back any tax they have overpaid.

CHILD POVERTY

Child Poverty—performance to date and projections for the future

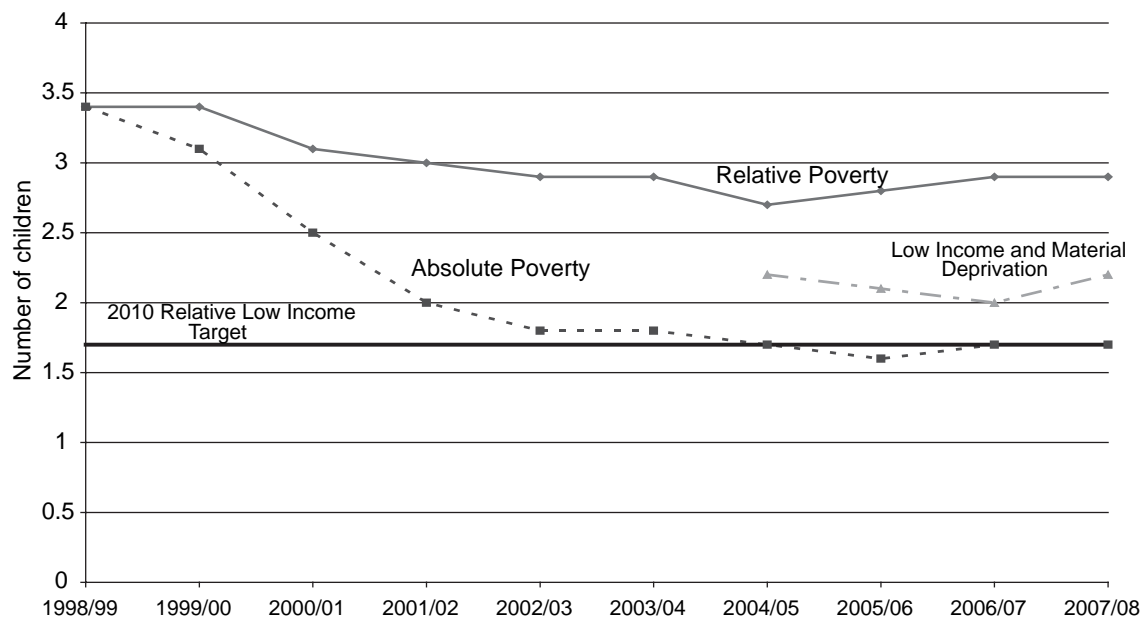
The Child Poverty PSA target uses the following three indicators to monitor performance. The data appears in the Households Below Average Income (HBAI) Report published by the Department for Work and Pensions.

- Absolute low income: this indicator measures whether the poorest families are seeing their income rise in real terms. The level is fixed as equal to the relative low-income threshold for the baseline year of 1998–99 expressed in today’s prices. Between 1998–99 and 2007–08 the number of children in absolute low income fell from 3.4 million to 1.7 million.
- Relative low income: this measures whether the poorest families are keeping pace with the growth of incomes in the economy as a whole. This indicator measures the number of children living in households below 60% of contemporary median equivalised household income. Some 500,000 children have been lifted out of relative poverty between 1998–99 and 2007–08 falling from 3.4 million to 2.9 million.
- Material deprivation: defined on the basis of those items that cannot be afforded. This indicator provides a wider measure of people’s living standards through a survey which asks respondents whether they have 21 goods and services, both child and household items. The 21 items were chosen following a thorough analysis of all existing UK material deprivation data to identify a set of questions which best discriminated between poor and non-poor families. They are designed to work together as a suite of items that combined present a picture of material deprivation rather than as individual indicators.

The Government’s target to halve child poverty requires it to reduce the number of children in relative low income poverty to 1.7 million by 2010. In 2007–08, the latest statistics available, there were 2.9 million children in relative poverty. Since, then the Government has introduced a number of additional measures targeted at reducing child poverty: the Government estimates that as a result of measures announced in and since Budget 2007 around a further 500,000 children will be lifted out of poverty. This analysis is based on estimates from HM Treasury’s tax and benefit simulation model which uses the Family Resources Survey and simulates the impact of changes in tax and benefits on household income and therefore poverty. This model focuses on simulating changes in relative poverty, the model has not been developed to accurately simulate the level of absolute poverty, or material deprivation, as requested by the Committee.

Child poverty is a result of a number of complex and varied factors and can be influenced by changes in economic circumstances, levels of employment and demographics. There is significant uncertainty about the impact on child poverty of the current economic circumstances and the Government faces additional pressures as a result of the extraordinary economic events. However, the Government remains committed to tackling child poverty and has taken further steps at Budgets and Pre-Budget Reports even in difficult times and is now taking forward the Child Poverty Bill which will enshrine in legislation its commitment to eradicate child poverty by 2020.

Graph 1
TIME SERIES ANALYSIS OF CHILD POVERTY INDICATORS



Take-up of Tax Credits

Child Tax Credit (CTC) is an income related payment for parents and carers of children or young people who are still in full-time non-advanced education or approved training. It is a single system of support for families, independent of parents' employment status, thus providing a stable source of income as parents move into work.

Work is the most effective route out of poverty. Working Tax Credits (WTC) "tops-up" income from low-paid work, improving incentives to work while also helping to ensure a decent income for families. For people who face a significant barrier to working full-time, such as those with children or a disability, Working Tax Credit is available if they work at least 16 hours a week. Other people who do not face these barriers and who work less than 30 hours a week are not generally entitled to Working Tax Credit, because working for less than 30 hours per week is less likely to create a strong attachment to the labour market and lead to sustained employment. Creating financial incentives to work part-time for people who could work full-time would therefore be counter-productive as a means of making work pay and tackling poverty. Nevertheless, to help people affected by the recession the Government announced in the Budget that from 31 July there will be a four-week run-on of entitlement to the Working Tax Credit for people who cease to qualify as a result of working shorter hours. This is worth up to £32 for a single person on the National Minimum Wage and £68 for a couple, and will help people with the transition to shorter working hours.

The WTC also contains a childcare element, which provides support with up to 80% of childcare costs, to a maximum eligible amount of £175 a week for one child or £300 per week for two or more children.

Take up of tax credits is higher than any previous system of income-related support for in-work families. In 2006–07 take-up of the child tax credit was 81% rising to 92% for those earning under £10,000. Take-up of the Working Tax Credit by people with children is 88% and 20% for those without children. In Budget 2009 the Government announced an ambitious target to raise take up of WTC among people without children by 100,000 by April 2011. HMRC will continue to expand its work with employers to increase take-up which is now reaching around 750,000 employees at over 50 organisations and its work with Jobcentre Plus to help those going in and out of work. Budget 09 also announced that HMRC will begin new research-driven marketing aimed at the half a million people who stand to gain the most from taking up WTC, and launch a pilot using data from Pay As You Earn records to identify and contact potentially eligible people.

Take-up of the childcare element of the Working Tax Credit

A take-up rate for the childcare element cannot be calculated in the same way as for Working Tax Credit or Child Tax Credit. This is because we do not have an estimate of the number of people who are eligible for the childcare element as this relies on use of formal childcare as well as work status. The administrative and survey data we currently hold does not allow us to determine which tax credit recipients are entitled to, but not claiming the childcare element.

The table below gives estimates of the number of families benefiting from the childcare element at points in time based on our snapshot statistics for tax credits awards. This number has increased by 78% since New Tax Credits were introduced in 2003, and also there are now over twice as many families benefiting from it as from the childcare tax credit in the Working Families Tax Credit, the predecessor system. However, during this time the number of families eligible for the child care element will also have grown, for example the Government has increased the amount of support in tax credits by increasing the proportion and maximum costs allowed for child care as well as increasing the child element above indexation.

Table 1
FAMILIES BENEFITING FROM THE CHILDCARE ELEMENT

	<i>Numbers benefiting¹</i>	<i>Average weekly help</i>
July 2003	264,400	£43.20
October 2003	285,600	£43.43
April 2004	317,700	£43.67
December 2004	331,300	£45.75
April 2005	337,400	£45.60
December 2005	356,000	£48.97
April 2006 ²	374,300	£49.90
December 2006 ²	395,800	£60.13
April 2007	413,700	£61.26
December 2007	427,600	£64.19
April 2008	448,800	£65.30
December 2008	461,500	£68.37
April 2009	470,400	£68.69

Notes

1. Those claiming the childcare element and with CTC above the family element.

2. Proportion of childcare costs allowed increased from 70% to 80% on 6 April 2006. The higher rate would be reflected in the December 2006 snapshot onwards. The April 2006 snapshot was taken on 5 April 2006 so would be based on 70% of costs allowed.
3. Source: HMRC Provisional Statistics at snapshot dates available at <http://www.hmrc.gov.uk/stats/personal-tax-credits/cwtc-quarterly-stats.htm>

Further analysis of the number of families receiving the child care element of the Working Tax Credit can be found in the statistics published on our website at <http://www.hmrc.gov.uk/stats/personal-tax-credits/cwtc-quarterly-stats.htm>

Employer Supported Childcare

The estimated costs of Employer Supported Childcare were published in the Tax Ready Reckoner and Tax Reliefs supplementary document at PBR 2008. In this document, the estimated costs to the Exchequer of Employer Supported Childcare was £400 million in 2007–08 and £500 million in 2008–09.

Most people claiming tax relief and National Insurance Contributions exemptions on Employer Supported Childcare have a household income that is too high for them to be eligible for childcare support through the tax credit system. Around one third of the funding for Employer Supported Childcare goes to the 6% of parents who pay tax at a higher rate.

Housing benefit

Budget 2008 announced that, from October 2009, Child Benefit would be disregarded for the purposes of calculating Housing Benefit (HB) and Council Tax Benefit (CTB). The implementation date was subsequently changed to 2 November 2009 to align with the changes to regulations which increased the HB and CTB capital thresholds for claimants of a pensionable age. This also allowed the local authorities more time to make the necessary changes to their software and instructions to staff. Given the timescale, involved, it is too early to say, but so far no local authorities have reported difficulties with its implementation.

As a result of this measure, around 200,000 working families will gain about £1,000 a year, making them an average of £20 a week better off. However, there is currently no reliable way of modelling the combined impact on child poverty of the Child Benefit disregard and the Local Housing Allowance (LHA) reforms announced in Budget 2009. This is because DWP does not currently hold quality assured data on the family breakdown of LHA customers. Although we are not able to say how many LHA customers have children, we estimate as a rough guide that around 45% of HB customers in the private rented sector have children (Family Resources Survey 06/07).

ALIGNMENT (CLEAR LINE OF SIGHT) PROJECT UPDATE

The Government published its proposals for a better aligned public spending framework in March 2009 (Cm 7567). The Liaison Committee responded to these proposals in its report *“Financial Scrutiny: Parliamentary Control over Government’s Budgets”* (HC 804) in July 2009. The Liaison Committee’s report accepted, on behalf of the Parliamentary Committees generally, all of the Government’s recommendations on alignment, as well as making a number of other recommendations about Parliament’s scrutiny of government expenditure. The Government has since responded to the Liaison Committee report. The Government’s response was published by the Committee on 2 November (HC 1074).

The Government is very grateful for Parliament’s support of the proposed alignment changes, which have enabled us to move towards phased implementation of the new spending framework, beginning in April 2010. At present, the necessary primary legislation is passing through Parliament as part of the Constitutional Reform and Governance Bill. The parts of the Bill relating to alignment passed their Committee stage in the House of Commons on 4 November.

The Government is also planning to put a further memorandum to the Liaison Committee, Treasury Committee and other interested Committees. This will cover a number of implementation issues on which the Committees have asked for further information, such as the format of Supply legislation and resolutions, as well as any new issues that have arisen since the Treasury’s memorandum in March 2009.

Subject to the passing of the legislation and any further comments received from the Parliamentary Committees, the Government is planning to implement the budgetary changes arising from alignment from April 2010 and the full changes to Estimates and resource accounts from April 2011.

OGC CONTRIBUTION TO THE RESPONSE TO THE TREASURY SUB COMMITTEE

The Office of Government Commerce (OGC) is currently piloting the second wave of Procurement Capability Reviews² (PCRs) which compare the procurement capability of the top 16 spending departments using a bespoke procurement capability model. This model uses a mixture of qualitative judgements and quantitative metrics to score departmental performance from nine perspectives (under broad headings such as leadership, governance and processes). Ratings have been published and a “Green” rating can equate to “world class”—as determined by OGC research and comparisons with a range

² http://www.ogc.gov.uk/procurement_capability_reviews_pcrs_update_about_procurement_capability_reviews_pcrs.asp

international procurement benchmarks which have been drawn from recognised international benchmarking organisations. The programme of reviews continues, with a greater focus on quantitative metrics, which naturally lend themselves to easier benchmarking—the results will continue to be made public.

On procurement outcomes, in pricing, for international markets such as energy we track against internationally recognised pricing indices, such as Platts (standard market energy index); and our collaborative approaches to certain categories are breaking new ground internationally. However, it will not always be possible to compare prices directly across international boundaries because the nature of consumption (ie customer behaviour) and the supply side (structure of markets, strength of competition) varies from country to country. Within the collaborative programme, OGC will continue to support the strengthening of Government's relationship with its top suppliers (most of who are international players).

The UK is a good exporter of Procurement practices; over 20 countries follow the Office of Government Commerce's (OGC) GatewayTM procurement assurance process. International standards have been set by our PRINCE2 and MSP products for project and programme management and ITIL processes for IT service management. This work will continue because since these standards are regularly updated and maintained through consultation and peer review by a pool of international experts.

It should be noted that the imminent publication of the first Operational Efficiency Programme "back office" benchmarking report will enable all public bodies employing more than 250 people to compare their performance across a number of metrics relating to back office costs, which includes procurement measures of efficiency and effectiveness. The metrics against which benchmarked performance is assessed were developed and agreed by the Audit Agencies (NAO, Audit Commission, etc) after an extensive period of research, which included a comparison with international standards.

The above are just a few example of the ways in which OGC will continue to make use of international comparisons. OGC seeks to continue to support the UK's leadership in this field and extend it through programmes of collaborative procurement, PPM and capability further into the Public Sector.

Supplementary written evidence submitted by HM Treasury

FURTHER MATERIAL REQUESTED AT THE EVIDENCE SESSION ON 8 DECEMBER 2009

Do large minority shareholders attend the quarterly meetings with UKFI? (Q401–Q402)

The Committee asked about UKFI's relationships with large minority shareholders.

Quarterly meetings are held between the UKFI CEO and senior Treasury officials, to allow Treasury to assess UKFI's performance. These meetings are weighted towards a forward-looking, risk-based analysis of progress against the UKFI Business Plan and Investment Mandate. Large minority shareholders in the relevant banks do not attend these meetings.

UKFI recognises that rebuilding the confidence of existing and potential shareholders will be essential if the banks are to attain a full market valuation for their shares. This is especially important given the Government's intention not to be a permanent shareholder.

Since the publication of *UKFI Strategy: Market Investments and Annual Report and Accounts* in July 2009, UKFI has held over 130 meetings with UK-based and global institutional shareholders, including current and potential shareholders in RBS and Lloyds.

The aims of these meetings are:

- to canvas other investors' views on the issues facing the banks, and what steps the banks should be taking to address these. Given the relative size of the Government's shareholdings in the two banks it is important that UKFI's views are well-informed;
- to explain the arm's length nature of UKFI's relationship with Government, and to explain the objective of protecting and enhancing the value of Government's stakes with a view to an exit from the shareholdings. This is intended to address any misunderstandings or fears about possible non-shareholder-oriented goals that UKFI, as a Government-related entity, might be perceived to have; and
- to demonstrate the UKFI is a responsible and responsive steward of the taxpayer's investment. UKFI aims to promote the development of a broad group of investors who are comfortable with the direction that the banks are taking, and who would be willing to enter into transactions with the Government over time.

UKFI continues to build relationships with other investors, and is committed to continuing its policy of engagement with them around major business issues and in deliberation on matters brought to vote at the banks' Annual General Meetings and all other meetings of shareholders.

What was the reasoning behind the targets that were given to RBS and to Lloyds for additional lending? (Q403–Q406)

The lending commitments agreed with RBS and Lloyds Banking Group are the result of careful, detailed negotiations between the institutions concerned and HM Government.

The lending agreements were negotiated individually with the banks, taking account of their specific circumstances, expertise and capacity.

Could you share the work on risk management of the Mapeley contract? (Q427)

HM Revenue & Customs (HMRC) has been very conscious of the potential impact of the economic downturn and its own vacation plans on Mapeley's financial position. To that end, it has carried out a detailed analysis of Mapeley's financial viability. Ongoing monitoring activity takes place, by intelligent review of published information. Two-way dialogue at senior stakeholder level in the partnership augments this analysis.

A financial model has been constructed which shows the impact of a variety of factors on Mapeley's financial viability; these include external economic factors (eg inflation, borrowing interest rates) and contractual (particularly the extent and timing of HMRC exiting buildings under the flexibility provisions). Mapeley were fully consulted during the development of the model and provided property specific data and management information relating to their own cash flows. These inputs are fed in to the model so that it can be used for robust decision-making, rather than HMRC relying upon scenario assumptions when determining its tactical and strategic estate plans. The model can be updated and continues to be used to inform vacation plans as well as allowing a number of economic scenarios to be run.

HMRC has discussed the results of the initial modelling with Mapeley with a view to identifying the options for maximizing HMRC's capacity to use the STEPS contract to generate financial efficiencies, whilst ensuring the ongoing financial viability of the partnership arrangement. HMRC has drawn on the modelling work as vacation plans have become clearer and both partners have discussed where it may be possible to amend plans in order to reduce the financial pressure on Mapeley whilst enabling the Department to vacate surplus space. We are in discussion with Mapeley based on those planned vacations.

HMRC is refining this modelling to enable it to undertake comparative analysis of the impacts of a range of service and portfolio related contractual strategies and actions, both on its own financial position and on Mapeley's financial viability. The model, once fully constructed, will form a platform to inform ongoing measurement of value for money from the STEPS contract.

Whilst the Department has prioritised the discussions and supporting modelling work intended to help Mapeley manage its financial pressures, HMRC has also refreshed and enhanced previous work done on business continuity planning in the event of Mapeley default. Through this planning and the work on Mapeley's financial viability, HMRC's Executive Committee is confident in its ability to manage any risks to its estates management plans effectively.

Why is outcome 2(a) "Supporting low inflation" described as "met-ongoing"? (Q433–Q435)

The rationale behind the "met-ongoing" assessment is that consumer price inflation (CPI) hasn't been more than 1% above or below the 2% target since February, but also that the monetary policy framework allows the Monetary Policy Committee (MPC) to look through short-term fluctuations to keep inflation at target over the medium term. As the latest MPC remit states:

"The framework takes into account that any economy at some point can suffer from external events or temporary difficulties. The framework is based on the recognition that the actual inflation rate will on occasions depart from its target as a result of shocks and disturbances. Attempts to keep inflation at the inflation target in these circumstances may cause undesirable volatility in output."

If CPI does move more than 1% above or below the 2% target, the remit states that the Governor of the Bank of England must explain in an open letter the reasons for the deviation from target, the action the MPC proposes to take, the expected duration of the deviation and how the proposed action meets the remit of the MPC.

Can you confirm the number of families that were supposed to be helped by the Housing Benefit change? (Q458–Q459)

Our latest estimate is that around 200,000 working families will gain about £1,000 a year following the disregard of Child Benefit from the calculation of their Housing Benefit and/or Council Tax Benefit award. These customers are already in receipt of Housing Benefit and/or Council Tax Benefit and so we can be confident they will gain.

In addition to those families who are already in receipt of Housing Benefit and/or Council Tax Benefit, the introduction of the disregard will also bring a further set of families onto entitlement for these benefits. Because of uncertainty about the extent to which this group will take up the benefits they are entitled to, reference to them is not included in the press notice issued by DWP in November when the change came into effect.

Our current estimate is that around a further 200,000 working families who become newly entitled to Housing Benefit and/or Council Tax Benefit because of the disregard will need to make a claim. We have not included this group in our media strategy because of the dependency upon them to make a claim.

The estimate for AME cost of the disregard announced at Budget 2008 was £330 million per annum. This estimate took a cautious approach for costing purposes (the potential maximum cost to the exchequer) by including both existing customers who will gain and assuming full take-up by those who become newly entitled to Housing Benefit and/or Council Tax Benefit.

The disregard of Child Benefit from the calculation of the Housing Benefit and/or Council Tax Benefit award applies to all customers in the Social and Private Rented Sectors.

What discussions has Treasury had with the Crown Estate regarding seabed leasing for renewable energy offshore? (Q520)

The Crown Estate operates at arm's length from the Treasury and enjoys a substantial degree of independence in its commercial activity. The Treasury's main focus of interest is in the commercial activity of the Estate as an integral corporate entity. The Crown Estate has shown itself capable of delivering successful financial results, while contributing to sustainable development, over a number of years and in a variety of property fields.

In the offshore energy field—both wave power and wind power—the Crown Estate is working constructively with the expert departments, notably DECC and the Scottish Government. It meets relevant people both in formal committees and ad hoc as issues arise.

How are you monitoring NS&I's performance now that they have suspended the value-add indicator? (Q534–Q536)

NS&I's performance

NS&I's performance is measured against three main financial targets: Value Added (measure of cost effectiveness against comparable (ie similar maturity) alternative wholesale sources of financing), Net Finance (the net flow of customer deposits), and the cost of administering funds (which benchmarks NS&I's efficiency against the industry). The minister sets annual targets for these measures.

Last year, NS&I was affected by a series of unexpected events, and was operating in a volatile environment. It saw the flight to safety, followed by falling base rates, and the dislocation between base rate and LIBOR.

NS&I did not benefit from the market instability. It kept rates within the pricing corridor and stopped all discretionary marketing, such as TV and press advertising for instance, and adopted—as best as it could—a low profile. However, in the interest of financial stability it remained open to new customers and focused on maintaining its usual service standards, in spite of the additional unsolicited inflows. At each stage it was quick to point out the effect of the changing environment on the dynamics of its business, presenting the options to stay on track (to reduce net financing and keep value added on track). It recommended and we agreed to an approach, which preserves the brand and Net Financing, at the expense of short term Value Added. Net Financing in 2008–09 was £12.5 billion against a remit of £4.6 billion.

For 2009–10, HMT agreed a net financing target of zero, with a range of –£2 billion to +£2 billion. NS&I's focus in 2009–10 is on delivering its modernisation programme for the benefit of customers, preserving net financing for the government and supporting financial stability in terms of maintaining an appropriate competitive position.

Value Added (VA)

The cost effectiveness of NS&I in the form of VA is measured against the cost of the most directly comparable form of alternative wholesale financing. For variable rate products we compare the cost of funding to the Bank of England base rate, and for fixed rate products, the comparator is the yield on fixed rate gilts.

In the current unprecedented economic environment, the comparators NS&I previously used to measure NS&I's cost-effectiveness and set its interest rates are no longer as meaningful. The base rate is now at a historically low level and financial markets have been unusually volatile over the last year. It is worth noting that the distorted Value Add comparators could have resulted in NS&I's Value Add figures being artificially depressed or flattered.

Under the circumstances and the actions agreed on pricing, NS&I agreed with HMT that NS&I's Service Delivery Measure target for value added would be temporarily suspended from Quarter 4 2008–09 and no target set for 2009–10.

Alternative indicators

Over the last two years, NS&I has proved itself to be a reliable, secure and trusted cornerstone of the savings market. NS&I remain committed to delivering Value Add over the longer term; however, there are other measures that illustrate its effectiveness as a cost-effective way of raising funding for the government: a good example is the efficiency ratio [this compares NS&I's administrative costs to the average funds invested by customers]. This currently stands at 20 basis points, which compares extremely well to those of comparable financial services providers and below the target agreed with HMT.

While Value Added is temporarily suspended due to market conditions, NS&I has developed a proxy value indicator, which has more validity in current circumstances. This is useful for pricing and planning purposes. It is not designed to replace Value Add but to give NS&I a tool to see whether it is delivering cost effective financing while the Value Add comparators are distorted and therefore misleading.

The alternative value indicator is still calculated in the same way for the fixed book; however, for the variable book it has looked at the average length of time people hold their investment with NS&I. It has compared this average figure to current gilt yields with equivalent maturity dates [ie, the cost to the DMO of raising the money now]. It estimates that, in the current financial year, this has so far delivered a figure of circa £750 million.

What assessment have you made of the impact on the Government's net debt figure of full compliance with IFRS? (Q541)

None of the existing PFIs coming on balance sheet under International Financial Reporting Standards (IFRS) will be counted against net debt. Any new PFIs will be assessed against both IFRS and National Accounting rules (ONS). If they satisfy IFRS criteria, they will come on balance sheet for resource accounts (and local authority accounts), and if they satisfy National Accounts criteria, they would be counted against net debt. We expect that very few PFIs will remain off balance sheet under IFRS, but the existing off balance sheet schemes and new ones are likely to be outside national accounts and thus outside net debt. The actual position for the first year of IFRS will not be known until the accounting for the 2009–10 financial year has been completed and audited by the NAO.

What proportion of the assets covered by the Asset Protection Scheme, which now and in the future will only apply to RBS, represented assets outside the UK? (Q548)

HM Treasury does not intend to publish detailed information about individual assets within the Scheme given the commercial sensitivity of such information and the risk that releasing such information would hinder the effective operation of the Scheme. However, now that the accession agreement is signed and all details are finalised, Treasury has published more detail on the asset pool and the due diligence and loss estimation process. This has been deposited in the libraries of both Houses of Parliament and includes information on the location of the Obligor incorporation (extract from Table 3.B, page 18 below). This can be accessed via the following link: http://www.hm-treasury.gov.uk/d/rbs_aps_apr.pdf

If RBS had not been able to include foreign assets and assets denominated in foreign currencies the scheme would not deliver its objectives. The RBS balance sheet includes assets denominated in foreign currencies and assets that were issued or purchased by foreign subsidiaries of RBS. Where these assets meet the criteria for entry, it is right that they are included in the APS pool. Failing to do so would not solve RBS' problems and allow it to increase its lending to customers. Some international assets have been excluded from the scheme since it was announced in January 2009. This is because the Government has concluded that specific assets are incompatible with the scheme rules.

Table 3.B
LOCATION OF OBLIGOR INCORPORATION

<i>Location of obligor incorporation</i>	<i>Covered assets (£bn)</i>
United Kingdom	114.5
Other EU	75.4
United States of America	43.6
Other	48.4
Total	281.9

How will HM Treasury report a change in value of the Government's investments in financial institutions in its Resource Accounts? (Q562)

In accordance with International Accounting Standard 39 (Financial Instruments: Recognition and Measurement), where HM Treasury acquires share capital in a financial institution, it is initially held on the Department's balance sheet as an "Available For Sale Financial Instrument", at the fair value of the consideration paid. Subsequently, the fair value of the investment is reassessed either—in the case of

“ordinary shares” capital—by reference to the publicly quoted share price, or—in the case of “B shares” capital—with reference to a valuation model. Any movement in this fair value assessment whilst the investment is held is shown in the “Available For Sale Reserve” in the bottom of the balance sheet.

Where HM Treasury sells any such Financial Instrument, the fair value of the investment is removed from the balance sheet, with the fair value of the consideration received recorded in the balance sheet; any difference in these two values is then recognised in the Operating Cost Statement, alongside the release of any related “Available For Sale Reserve”.

Under this accounting standard, where the fair value of the investment suffers a significant or prolonged decrease in a given financial year, this loss in value, is recognised in the Operating Cost Statement in the period in question, and not deferred until any future sale date; this treatment does not apply to any significant or prolonged increase in value.

Financial instruments held by HM Treasury during 2008–09 are reported in the Operating Cost Statement on page 176 of HM Treasury Group’s Annual Report and Accounts 2008–09 (HC 611), and in the Balance Sheet on page 177, along with the associated Notes 8 and 13a to those Accounts.

Written evidence submitted by the Government Actuary’s Department (GAD)

Thank you for your letter of 12 November 2009 asking us a set of questions on which you would like answers in order to prepare your annual report.

I am delighted to respond to your questions. As background, understanding the answers to a lot of what you are asking will, I believe, be helped by an understanding of the overall strategy and business plans of the Department and how things have changed since I started. So I shall start by setting the scene in this regard.

COMMENTS ON GAD’S STRATEGY/BUSINESS PLANS ETC

When I took on the role of Government Actuary on 1 May 2008, I instigated a strategic review which forced us to address the questions:

- what does success for GAD look like?; and
- what is failure of GAD?

Without addressing these questions it is impossible to know what risks to control (of which more later) or how to motivate the department to a common objective.

For GAD we decided that failure would be a sale of the Department caused by our own action/errors (as opposed to a Government inspired sale which would be subject to other considerations).

Success, in the absence of a single metric such as profits as one gets in private sector, was set as a balanced scorecard of various metrics (see the key objectives described in the summary business plan attached; the objectives include delivery of the plan, improving sustainability and brand, complete HR initiatives etc).

In addition, I have set myself three personal success measures:

- to ensure GAD is a success;
- to be truly the Government Actuary (ie providing all types of actuarial support to Government and not just pensions support as has generally been the case for some years); and
- to improve the “brand” of GAD, and actuaries generally, in Government.

In order to deliver on this, we had a structured set of initial objectives as follows:

- determine a descriptor of GAD; which we have set as “Government Actuary’s Department—the actuarial consultancy—in the public sector—for the public sector”;
- determine, through client and employee surveys and an interactive SWOT analysis, the values to which we need to aspire (not just what we think we are);
- a total overhaul of the HR approach (new job descriptions, career maps, competencies, appraisal system, pay and reward etc);
- quality management information on a monthly basis;
- establishment of half-yearly employee attitude surveys (we have now finished three) and annual client surveys (the second is now just finished);
- segmenting our business into three strands and setting goals for each (ie to be principal provider of services on policy work, to be best in class for our regular work for public service pension schemes and to provide a valued service to other work suppliers). The key is that clients judge us on a scale of 1–10 and we achieve our goals if we secure target marks on client perception;
- to shift to a client-centric organisation which means (a) that clients decide whether they receive a quality service rather than as previously, we form our own view on quality and (b) we need to significantly change our culture with regard to client service, sales and marketing;

- restructure the management of the Department into functions with clear allocated responsibilities;
- to overhaul our training programme in line with the new culture, the new competencies etc; and
- determine the big risks which can lead to “failure” (seven in all). Interestingly of the 70 items on the GAD risk register when I started only three of the big risks were present—a proportion which we understand is not untypical. The big risks are getting sued, loss of any of our key clients, valuation software, personal data loss and three client specific risks.

In summary, these objectives recognise that the two big things that matter for GAD are our people and our clients.

As you have noticed we got off to a very successful start in 2008–09. After two years’ previous decline, income was up 19%, staff numbers up some 30% at 30 June 2009, morale up significantly and indeed all the metrics turned very positive.

As well as the summary business plan which is attached to this letter, I also attach our “user-friendly” annual report for 2008–09 which lists all of the things we do, our values etc which I believe will fill in many gaps. It also summarises on page two our achievements for last year and plans for this year.

A key part of our plan is investment in developing two new areas for us:

- investment and risk consulting (this started in February this year); and
- opening a second office, in Scotland, to serve Scottish Government and Local Authorities (early next year).

To finish this introduction, I will share with you my own approach to my own bonus which, sensibly, is different to that elsewhere in civil service given that GAD receives income broadly comparable to our expenditure so we can easily look at private sector analogies. The principles are:

- there should be no reward for failure;
- there should be the potential for a sizeable reduction if the risk of failure is higher at the end of the bonus period than the beginning (this I see as critical since it has more effect on behaviour than the previous principle);
- the maximum bonus should be set in advance with a realistic chance of achievement;
- if I am to advise others on risk and reward mechanisms (as I do), I should put my money where my mouth is and try out mechanisms on myself first to see what works; and
- there should be a real range of possible outcomes from zero to 100% rather than the more common narrow range which in practice could well be in the 66%–80% band.

A proforma to the approach I adopt is attached. Note that this approach is only applicable to me at present. It may get extended to the Executive on the Board but it is not appropriate beyond that level. Note also that the proforma approach is designed to avoid “shutting the stable door after the horse is bolted” as is the intention of bonus deferral elsewhere. Quite which of the two approaches turns out best is too early to say but the approach I am adopting is not tried and tested elsewhere but is a novel and worthwhile alternative to understand as the years go by.

Turning now to the questions:

Q1. *How has GAD’s business changed in response to the economic crisis*

A1. To date very little. Our income for 2009–10 should again be some 20% higher than last year. 80% of our work is UK public sector which has been and will be secure until 1 April 2010. Beyond that we expect:

- more pressure on fees;
- extra work for any new government, whoever is in power, at the start of an administration;
- growing our two “investment areas”; and
- some risks to some overseas insurance contract renewals (although we are investing much time in protecting our position and have very good relationships).

On balance we expect the second and third to be more significant than the first but this is by no means certain. So we are now into a theme of consolidation for 2010/11 and have contingencies prepared.

Q2. *To what extent is the new Investment and Risk team a response to the changing economic environment over the last year?*

A2. In principle the answer is none but there was an indirect influence.

When I started, the Department had very limited expertise on investment or risk. Elsewhere, in the private sector, investment is now mainstream actuarial work. Risk is upcoming. I looked round Government and quickly came to the view that there is a big need for quality mathematical and actuarial support in both these areas so we launched the initiative of setting up this team with a view to “marketing” our services. There is no doubt that the credit crunch supported us in the analysis but it wasn’t a direct driver.

To date, the core team has grown from one person to four in under a year. As well as investment risk, we are also chairing a cross-Government group on project risk, we are aiming to link with NAO/Internal Audit to establish a joint audit/actuarial approach to managing and controlling risk and, are working with APA, UKFI and Treasury.

Q3. *How much of the (Investment and Risk) team's work has been on the modeling of the Asset Protection Scheme for HM Treasury?*

A3. The short answer is not much. The work of designing the APS was already under way when the team was formed. That said, GAD were able to review the proposed terms of the APS and comment on some risk-related aspects of the design. We also reviewed an illustrative cashflow model that was used to help with the scheme design, commented on its suitability for analysing risk on an ongoing basis and proposed an alternative approach to the modeling which would enable more of the potential risks to be captured. In addition, members of our insurance team worked with the investment and risk team given that the infrastructure of the APS bears some resemblance to an insurance company. Now that the APA has appointed its new head and new head of risk, we are actively liaising with them regarding monitoring and evaluating risks going forwards where we believe a combination of actuaries with the APA's credit experts can deliver better than either expertise in isolation.

Q4. *What skills and expertise does the (Investment and Risk) team possess to be able successfully to advise on investment risk management strategies and approaches to hedging risk?*

A4. Members of the team have extensive experience of working with pension funds, insurance companies, asset managers and investment banks in designing and implementing risk management and hedging strategies. Specific expertise includes:

- financial and demographic risk assessment;
- stochastic asset liability modeling;
- investment strategy implementation and asset allocation optimisation;
- critique of any investment strategy and hedging;
- risk mitigation strategies eg interest and inflation swaps, longevity hedging, insurance to effect a risk transfer etc; and
- strong communication skills.

It is also worth recording that we are actively exploring with other parts of Government (including NAO, Internal Audit, Treasury, Cabinet Office and departmental risk Managers) ways in which we can bring our skills on quantifying/managing risk from a mathematical/financial perspective into a coordinated framework with other relevant risk skills for the better control of risk across Government. This proper professional mathematical modeling expertise has been conspicuous by its absence to date.

Q5. *(In relation to Solvency II) what additional work will GAD be required to undertake?*

A5. The work that our insurance team will do on Solvency II needs to be considered under three headings:

- (i) who is our client base;
- (ii) the ongoing work for existing clients; and
- (iii) other work (training and development, new project for new and existing clients).

It should also be remembered that Solvency II does not come into force until 2012.

Taking each in turn:

- (i) Our insurance client base is primarily regulatory support work for non-UK regulators. In other words, we have the equivalent role for certain overseas regulators that actuaries at the FSA have for the FSA in respect of the UK but, naturally, the work we do is commensurate with the state of development of the relevant local market. We also perform a small (but growing) amount of consultancy work for Governmental Departments in the UK.
- (ii) In relation to ongoing regulatory support work, much of this arises from September, through March. There is no increase for October 2009–May 2010 on account of Solvency II regulation. The first year when this is expected to arise is 2010–11 when we are likely to offer an internal model review service (but whether clients defer until 2012 is unknown). We are planning that in 2010–11, our workload will be some 50% higher on existing EU clients. However, this estimate represents a very wide range between 10% and 100% and only in six months' time will this become clearer. Further, it should be realised that EU work represents just some 25% of our insurance team's business.
- (iii) We are already seeing new work arise in terms of training sessions for regulators and for certain UK Government Departments. We also expect our expertise will create real opportunities to win new overseas clients. We recently secured a new client with the Bahamas regulators.

Q6. *What is GAD's strategy for coping with this increased (Solvency II) workload*

A6. At present, we are keeping a watching brief and indulging in very low cost marketing exercises. This is because there is so much uncertainty of whether there will be much extra work and when it will arise, coupled with the constraints imposed under Parliament's spending rules. As a Government Department, we are constrained to not go below budget of a £588,000 net cost for 2009–10 (based on £13.5 million income) nor to make any profit. This makes it almost impossible to staff up in advance for work that will not arise for at least a year and potentially never. Further, the potential growth relates to non-UK work which is outside our core strategy. (The rationale for having a public sector GAD is to support UK central government; if we become a profit-centre for non-core work we would likely suffer in our ability to deliver to this core strategy). Against this background (and the earlier mentioned risks with some of our overseas contracts) "our wait and prepare" strategy is:

- monitor and report quarterly on Solvency II activity/developments;
- build relations with the actuaries in FSA for purposes of sharing knowledge, joint training etc with a view to determining if there are any future possibilities of secondments either way to create a more flexible pool of labour to respond quickly to demand;
- attend the key international insurance regulator conference each year; and
- develop a 2010–11 Solvency II strategy in May 2010.

Q7. *Does the estimation of numbers of staff needed next year include those required to complete the increasing Solvency II work?*

A7. Our estimation of 130 average staff for 2009–10 does not include any specific Solvency II extra staff but it does effectively make an allowance. We just applied an overall increase to 2008–09. Already the estimate looks like it might be too low independent of Solvency II. Regardless, any increased workload, if it comes, will not be big relative to the Department as a whole. We do not know if much will arise in 2010–11 and we have to manage relative to some very tight financial "caps and collars"!

Q8. *How many man hours do you envisage being spent on this area in 2009–10 and 2010–11?*

A8. For 2009–10, the client-training fee based work (some to UK departments, some overseas) will comprise some 50–150 man-hours. For internal awareness and training, we do not specifically itemise or budget our pure Solvency II elements but we started internal training in the summer of 2009 and envisage some 100–150 total man hours for our 15 insurance team members on awareness and training in 2009–10. We will not come to a view on 2010–11 until May 2010 (see A6 above) for all the reasons given. Things are too uncertain at present.

Q9. *To what do you attribute GAD's success?*

A9.

- Absolute clarity on meaning of success/failure and the big risks to failure.
- Clear recognition that our strategy focuses on our people and our clients.
- Leadership and Drive. I will do everything I ask others to do and not afraid of taking personal risks.
- Combining private sector focus and techniques with the strong ethics and service culture of public sector.
- It would be wrong to totally ignore the recession! Although not a major contribution, the recession has, when combined with all the positive messages and our changed reputation, helped us recruit and retain quality staff. But I would not wish you to overplay this aspect.

Q10. *To what extent is the increased income the result of increased charges for your services rather than increased business?*

A.10 The increase in fee income for the year (allowing for the increase in work-in-progress which is shown as a credit against expenditure in the accounts rather than income) is about 21%. This comprises an increase in chargeable hours worked of 15% and an increase in average fee per hour of 6%. So, roughly, just under one-third is increased charges and two-thirds is increased business. It is worth considering, conceptually, where the increased business has come from which is:

- a catch-up of work (backlog), that had slipped behind expected timescales in the previous year, arising from the recruitment of extra staff;
- being given extra work from ongoing clients by being more on top of our workload; and
- new clients.

Of these, the last only made a small contribution in 2008–09 but 2009–10 year to date is already showing significant wins in new clients; some against strong competition.

Q11. *What are your projections for income for 2009–10?*

A11. Although difficult to predict we anticipate income could be between £13.5 million and £14.5 million which would represent another year of close to 20% growth depending on the precise turn-out.

Q12. *Why did you waive this year's bonus when GAD has had "real and genuine success" (Annual Report and Resource Account, p 22) over the last year under your stewardship?*

A12. On a factual basis, I did not waive the bonus in full. I took £15,000 and waived the potential excess of up to £25,000. Although a final nominal figure was never agreed, it was accepted that it would have been in excess of £20,000 without the waiver. So how did we arrive at this position? It was a combination of two factors:

- (i) I want to make GAD a success. This means we need to build and preserve good relations with all parts of Government in order to get work and more work from them. I was advised that to push for more than £15,000 would create serious difficulties to the Civil Service given their desire to achieve more cost control over the pay bill.
- (ii) I felt that a full waiver would be quite wrong since it would create a message generally in the Department that the Department had been a failure meaning that success would be seen by all as being no better than failure—which would create the perverse behaviour of rewarding failure! To explain, the message to senior people of no bonus after a successful year would have been "it doesn't matter whether you do poor work; you're not going to lose out relative to doing good work, since you end up with the same pay—so why do more than the minimum"—hence the reward for failure consequence of a full bonus waiver.

So it was pretty straightforward. My big objective of "GAD success" meant it would be stupid to push for more than £15,000. Note that in line with my drive for transparency/disclosure, we positively disclosed and accounted for my 2008–09 bonus in the 2008–09 accounts notwithstanding the cash not being paid until 2009–10. If you would like more details of my 2009–10 bonus arrangement over and above the proforma attached please let me know.

Q13. *How is GAD going to measure performance against these aims, and how will GAD report this to stakeholders?*

A13. Against each of the three aims we take measurements:

- firstly on the client's perception of "preferred provider", "best in class", "highly valued";
- secondly on income growth for each category.

We have targets for the perception measures (85% for preferred provider, 60% for best in class, by summer 2010. These are stretch targets given a base of 76%, and 36% respectively in August 2008.

Our growth targets for each category are 20%, 7% and 10% per annum. The last two are being beaten. We are behind on the first.

In early 2009 we did a full report to stakeholders of the results (good and not good) of the summer 2008 exercise. We will do the same again in early 2010 in respect of this year's exercise. If you would like to see the report we issued earlier this year, please let me know.

Q14. *Will GAD be repeating the client survey conducted in 2008–09 on an annual basis in order to gain stakeholders' views on GAD's performance?*

A14. Absolutely yes. We conducted an equivalent survey in September/October 2009. The results are not fully analysed. Initial indications suggest not much change over the year. So we need to understand why this is the case and do better.

Q15. *GAD's Annual Report records great success in recruitment with staff numbers up accordingly. Does the fact that "Consultancy" costs and "Agency and other temporary staff" costs have increased dramatically suggest that GAD has nevertheless been working this year without the full time permanent staff it needs?*

A15. There is a sizeable increase in Consultancy and Agency costs as you rightly point out. The increase in agency costs reflects our great success in recruitment and represents the agency commissions for each new recruit we take on through agency introductions.

The increase in commissions is caused by us taking on a handful of staff to cope with our workload where:

- (a) some did not actually wish to become permanent members of GAD;
- (b) given our rapid expansion, it suited us to have some flexibility to easily reduce numbers if for example the increased workload did prove to come just from catching up on the backlog.

As of the present, we still have two such individuals on a staffing level now of 134 so we believe we are managing this well at present.

Q16. *Has GAD recruited the right staff?*

A16. There is no doubt that with the changed direction and the recession, GAD has been able to recruit some real quality actuarial staff at all levels. In a year's time, might we look back and say "we could have done better there" or "we missed an opportunity on that issue" or "we misjudged"? I expect so. But that's always the way of things and at present I have no omissions or regrets.

Q17. *Are GAD's pay levels sufficiently competitive to attract the senior staff and specialists that you need?*

A17. At present the answer is yes. But we need to monitor very closely since, once there is real growth in the economy, there is a significant risk of losses of good staff. Positive adherence to our key values and exposure to plenty of interesting work will be a great help.

Q18. *How many staff will you be recruiting in the next financial year?*

A18. We expect our staff numbers at 31 March 2010 to be broadly as they are today (ie 134) plus two or three new staff to set up our Glasgow office.

Q19. *Is GAD still on course to move into a new office in "early 2010"? Do you have a more precise date for the move?*

A19. No. GAD will be unable to move into a new office as planned.

Although we had received OGC and Treasury approval in April 2009, and had a firm commitment of new better, cheaper premises and had a new tenant for the whole of Finlaison House, we hit problems due to our sub-tenants. One of our sub-tenants is the Baha Mousa Inquiry. They had originally expected to vacate in April 2010 but this is now likely to be extended to late 2010. So the new tenant for Finlaison House, quite reasonably, pulled out needing full immediate occupancy. It will be difficult to find new tenants in the current climate so we are focused on staying in Finlaison House for the foreseeable future and delivering quality service to our clients.

We are being more efficient in our use of space—Finlaison House is 2,874 sq metres with GAD occupying 1,376 sq metres (a reduction from 1,515 sq metres on 1 May 2008 when I took on the role notwithstanding the higher staff numbers).

The committee should be aware that, as a result of our failure to move, our finances are very vulnerable to sub-tenants leaving. We could in the next year or two face a hit to our net costs of over £1 million based on what may or may not happen. We are in discussions with Treasury and OGC about managing this potential exposure.

Q20. *What benefits do VIP events bring to GAD and its business?*

A20. Ultimately, our aim is to have greater penetration of Government so that Government makes best use of its in-house actuarial services wherever this is appropriate. There are lots of areas of Government where our expertise could be of real benefit and currently is not, due to lack of knowledge and lack of sponsorship. So our first aim is to spread the word amongst senior key participants and influencers that we're back in business.

Our second aim is to act as a facilitator between key government/public sector individuals and the external financial world where there are often misunderstandings. If all parties can better understand each other then policy implementation will work better for all parties (in the non-party political sense) for the good of the country. And if we can do this, then this will also support our first objective.

To date we have held four breakfasts—two in January on gilts issuance (with Treasury/DMO), one in June on Longevity (with ONS and Cass Business School) and one in October on the Walker review (with Sir David Walker speaking).

Q21. *What was the cost of holding these events?*

A21. The total cost of the four events to date was £1,572.

Q22. *What progress has been made on the valuation of the miners' pension scheme?*

A22. The September 2008 valuation for the Mineworkers Pension Scheme has been completed and signed in September 2009. Copies were circulated to the trustees, DECC, HM treasury shortly afterwards. A copy is enclosed. The statement on risk requested by the committee is included as Appendix B of the report. Members of the scheme were briefed on the outcome by a newsletter issued in late October. There is no formal publication of the report other than as described above.

The valuation for the British Coal Staff Superannuation Scheme has nearly concluded its consultation phase and we hope to sign the report in the next month or two.

CONCLUDING REMARKS

My aim in the above has been to answer the questions fully and honestly with the hope that you can see the tremendous progress the whole Department has achieved and takes pride in, along with the challenges we face. We are on a journey to even greater things for the good of Government and the country. But as stated there are many challenges ahead and potential minefields to navigate. So if you would like any more information about the past or the future, whether in writing or face to face, please do not hesitate to get in touch and I would be delighted to assist further.

Attachments:³

- Business plan.
- Short form Annual Review.
- Proforma bonus approach.
- MPS valuation.

Trevor Llanwarne
Government Actuary

5 January 2010

³ Not printed.