



House of Commons  
Committee of Public Accounts

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# Managing the defence budget and estate

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Tenth Report of session 2010–11

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

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## The Committee of Public Accounts

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The following member was also a member of the committee during the parliament:

Eric Joyce (*Labour, Falkirk*)

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Powers of the Committee of Public Accounts are set out in House of Commons Standing Orders, principally in SO No 148. These are available on the Internet via [www.parliament.uk](http://www.parliament.uk).

### Publication

The Reports and evidence of the Committee are published by The Stationery Office by Order of the House. All publications of the Committee (including press notices) are on the Internet at <http://www.parliament.uk/pac>. A list of Reports of the Committee in the present Session is at the back of this volume.

### Committee staff

The current staff of the Committee is Philip Aylett (Clerk), Lori Verwaerde (Senior Committee Assistant), Ian Blair and Michelle Garratty (Committee Assistants) and Alex Paterson (Media Officer).

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## Summary

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### *On managing the defence budget*

The Ministry of Defence (the Department) is responsible for over £42 billion of annual expenditure. While it has managed to stay within budget each year, it has failed to exercise the robust financial management necessary to control its resources effectively in the long term. It has also failed to match its future plans to a realistic assessment of the resources available. There is a shortfall in planned expenditure against likely funding of up to £36 billion over the next ten years. The Strategic Defence and Security Review did not explicitly set out how this long-standing gap between defence spending and funding would be resolved. It is imperative that the Department should now do so.

The Department's consistent pattern of planned overspend demonstrates serious organisational failings and a dangerous culture of optimism. The underlying reasons for the systemic failings in budgetary controls are the tendency towards financial over-commitment, weaknesses in the financial planning processes and a division in responsibilities and accountability for financial stewardship. The failure to integrate financial planning and control into decision making means that cuts in programmes and delays in expenditure on defence equipment are made very late in the day, leading to inefficiency, poor value for money and longer term additional costs.

The Accounting Officer has not discharged his responsibility to ensure that planned and committed expenditure across the defence budget represents value for money. For example, in 2008 the Department signed a contract to buy new aircraft carriers which was unaffordable, without having identified compensating savings. Because these savings were not subsequently found, it was necessary within a year to delay the project, resulting in an enormous cost increase and poor value for money.

We were astonished to learn that the Department has not had an explicit financial strategy linking its funding to its priorities. Without a clear strategy, it is difficult to resolve funding conflicts or to reallocate resources when priorities change. The Department does not have the tools to help it to revisit assumptions underlying its plans, ensure plans are realistic and make provision for unexpected events and managing risk.

Furthermore, the Department does not prioritise individual elements of the defence programme against its strategic priorities. When financial savings have to be found there is then no clear basis for determining where cuts should be made. So in-year decisions on budget cuts are made on an ad hoc basis, without proper consideration of relevant priorities and needs.

The Department has made some inroads into improving its financial management; however, it has yet to give financial management the serious consideration that it deserves. The Department has now appointed a professionally qualified Finance Director, and has undertaken to provide him with the full authority he needs to do the job.

### *On managing the defence estate*

The defence estate covers 1.5% of the UK land mass, is valued at over £20 billion, and costs an estimated £2.9 billion per year to run. The Department has reduced the amount of built estate in the UK by 4.3% between 1998 and 2008, and achieved £3.4 billion in sale receipts. However, staffing over the same period was cut by 13%, so more of the estate could and should have been released.

The Department does not assess its estate against clear objective criteria, such as the cost of running a site or the intensity of usage. The bias always appears to lie with keeping a site rather than disposing of it.

The Department does not collect centrally the information and data that would allow it to manage its estate in an effective way. It appears to lack urgency in its plans to improve its information base.

On the basis of reports by the Comptroller and Auditor General,<sup>1</sup> we took evidence from the Ministry of Defence and Defence Estates on managing the defence budget and estate.

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<sup>1</sup> C&AG's report, *Strategic financial management of the defence budget*, HC (2010-2011) 290; C&AG's report, *A defence estate of the right size to meet operational needs*, HC (2010-2011) 70

# Conclusions and Recommendations

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## On managing the defence budget

- 1. The Department's poor financial management has led to a severe funding shortfall of up to £36 billion in defence spending over the next ten years.** Weaknesses in financial planning and management have resulted in poor value for money from delays, changes to project specifications and costly contract renegotiations. There is a culture of over-optimism about the ability to meet financial commitments and senior officials do not challenge unaffordable decisions about equipment procurement. All of these factors have contributed to serious budgetary pressures year after year, with consequent budget cuts being made mid-year in an unsystematic and ad hoc way, leading to greater costs in the longer term. We believe this situation is entirely unacceptable. The Department needs to take immediate steps to sort out its financial management, and we make several recommendations below directed at this.
- 2. The Department has failed to develop a financial strategy identifying core spending priorities.** This should have been a fundamental part of the Department's business planning processes. The Department's inability to prioritise individual elements of the defence programme on a strategic basis means it cannot easily identify where in-year budget cuts should be made. As a matter of urgency, the Finance Director should lead the creation of a realistic financial strategy which identifies and reviews spending priorities on an annual basis.
- 3. The Department's senior officials did not seek ministerial directions to proceed when they had major concerns about decisions threatening the value for money of defence spending.** In response to a recognition that the overall defence programme was unaffordable, a series of decisions to delay and change the scope of defence projects were made which offered poor value for money. The Accounting Officer did not, however, consider it appropriate to seek a direction from Ministers to proceed on any of these individual decisions or in respect of their cumulative effect. Whilst respecting his view, we recommend that HM Treasury and the Cabinet Office revisit the issue on seeking ministerial directions and strongly reiterate to Accounting Officers the importance of seeking such directions in appropriate circumstances.
- 4. The Finance Director's role has been undermined by giving responsibility for long-term financial planning to the Strategy Director.** We welcome the Department's commitment to give the Finance Director the full range of powers he needs to perform his job effectively. We urge the Department to make sure the Finance Director has immediate responsibility for all financial matters, including strategic financial planning.
- 5. The recent Strategic Defence and Security Review was an opportunity to set out how defence spending could be brought into line with available funding.** However, in the absence of an explicit statement of how the Department will balance

its budgets in the future, it is even more imperative that the Department gets a firm grip on its strategic financial management.

### On managing the defence estate

6. **The Department's decision making about its estate has been driven almost entirely by a loose judgement on operational need, with a bias toward keeping sites rather than releasing them.** The Department must develop a more robust decision making process, which balances perceived operational need with the cost of holding and running major assets. It should change the way it takes decisions on the future of the estate so that it can challenge more robustly whether the use of the estate is cost effective and efficient in the light of changing operational needs and reductions in personnel numbers.
7. **The Department has not defined high level criteria or metrics to judge whether it is using its estate efficiently.** It has not set any high level targets for estate size and cost, nor has it developed appropriate indicators of its efficiency. The Department should define the size and type of estate needed to fulfil the tasks required of it. Within six months, it should develop a small suite of measures to assess whether it is successfully reducing the size and cost of its estate, in line with changes to the size of the armed forces and equipment fleets. Whilst it should have regard to the views expressed by operational staff, it needs to establish clear, objective, and value for money criteria in determining the future of its estate.
8. **The Department does not have good central data to inform decision making about its estate.** The Department recognises it needs to collect better information but has not set out a timeline to achieve this, and previous attempts to develop data systems have failed. We recommend the Department should immediately identify the key data it needs to manage its estate assets effectively, including data on relative operational importance, potential sale value, running cost, utilisation and condition. The Department should have systems in place to collect this data within 12 months, and certainly well before signing its next generation of major estates contracts. We expect the Department to report back to us on the progress it has made within six months.



# 1 Managing the defence budget

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1. The Department needs effective financial management to direct and control the £42 billion of resources for which it is responsible and to ensure successful delivery of its aims and objectives within budget.<sup>2</sup> Without good financial management, the Department has struggled to deliver an affordable plan and live within its means.

2. Consequently, the Department has found itself facing a budgetary black hole of up to £36 billion over the next ten years.<sup>3</sup> This has resulted in short-term decisions which have delivered poor value for money. For example, in 2008 contractual commitments were made to procure new aircraft carriers without identifying compensating savings across the whole programme. Because these savings were not identified, within a year it was necessary to delay the project, resulting in an enormous cost increase.<sup>4</sup>

3. Although the size of the budget shortfall is highly susceptible to assumptions regarding future Spending Review settlements, further cuts in funding without associated cuts to outputs will cause the deficit to increase.<sup>5</sup> The recent Strategic Defence and Security Review highlights the importance of bringing the budget back into balance.<sup>6</sup>

4. To ensure that its spending plans are both sustainable and affordable, the Department must set out a financial strategy.<sup>7</sup> The financial strategy should articulate and review, on an annual basis, the spending priorities across the Department.<sup>8</sup> The lack of such prioritisation to date has meant that every time savings need to be made, the entire organisation has to be reviewed to determine where cuts would have the least impact on capability.<sup>9</sup> The result has been short-term decisions to delay, de-scope, and reduce equipment numbers after contracts have been signed with industry.<sup>10</sup> Such decisions are extremely poor value for money.<sup>11</sup> A defence programme which has been mapped to strategic priorities would mean that there is a clear basis for determining where savings should take place when funding falls short.

5. The financial strategy should contain within it an unallocated reserve of funds to allow the Department to respond to unexpected events.<sup>12</sup> For example, the Department's decision to reprioritise £300 million per annum to Afghanistan meant that tough decisions

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2 Q 2; C&AG's report on the defence budget, para 1

3 Q 2

4 Qq 58-67

5 Q 6

6 HM Government, *Securing Britain in an Age of Uncertainty: The Strategic Defence and Security Review*, Cm 7948, October 2010

7 Q 18

8 Q 40

9 C&AG's report on the defence budget, para 10

10 Qq 49, 56-69

11 Q 66

12 C&AG's report on the defence budget, para 2.17

had to be made to close air bases and reduce training, as there was not enough flexibility in the budget to enable this to happen otherwise.<sup>13</sup>

6. Budget flexibility would also help to deal with the effects of optimism bias and poor risk management.<sup>14</sup> The Department has a tendency to be over-optimistic about the cost and likely delivery dates of major projects.<sup>15</sup> In such instances, setting aside an unallocated contingency would mean that cost increases on major projects would not lead to cuts being made elsewhere, as has previously been the case.<sup>16</sup> Similarly, the Department does not have a good track record in identifying and budgeting for financial risks.<sup>17</sup> An unallocated reserve would enable the effects of risk to be managed without removing funding from other areas.

7. The financial strategy should be regularly updated with an annual review of the assumptions which underpin it.<sup>18</sup> This would help ensure that decisions based on the strategy are relevant to current defence needs and the financial position of the Department – rather than being hamstrung by the absence of a strategic defence review, as has been the case over the past twelve years.

8. The recently published Strategic Defence and Security Review provides the Department with an opportunity to “reset” its budgets in line with expectations of likely funding.<sup>19</sup> However, the greater challenge will be for the Department to maintain that balance in the long term, between strategic reviews.<sup>20</sup> The development of a financial strategy would put the Department in a better position to balance expected funding and significant changes to capability.<sup>21</sup>

9. The Accounting Officer’s responsibilities, as set out in *Managing Public Money*, include taking personal responsibility for value for money.<sup>22</sup> If value for money is placed at risk, then the Accounting Officer should seek a ministerial direction where Ministers decide to continue with a specific course of action that the Accounting Officer has advised against.<sup>23</sup>

10. There should be no doubt that ministerial directions should be sought when projects which would make the overall programme unaffordable are approved without corresponding cuts being identified elsewhere in the defence budget.<sup>24</sup> They should also be required when decisions are taken to delay or otherwise alter existing projects in a way which would jeopardise value for money for the taxpayer.<sup>25</sup> The Department’s Accounting

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13 Qq 81-82

14 Q 7

15 Q 7

16 Q 43

17 Q 43

18 Q 40

19 Qq 6-7, 14

20 Qq 6, 14; C&AG’s report on the defence budget, para 19

21 Qq 31-41

22 HM Treasury, *Managing Public Money*, October 2007, para 3.3.3

23 HM Treasury, *Managing Public Money*, box 3.2

24 Q 59

25 Qq 10-11, 39, 42, 90

Officer told us that, in the case of the aircraft carriers, he did not seek a direction because in his view there were no issues of regularity or propriety and the concerns about affordability in themselves did not warrant a formal direction.<sup>26</sup>

11. Under present arrangements in the Department, the Finance Director leads the search for in-year savings but is not responsible for the long term management of the defence budget.<sup>27</sup> This contradicts the guidance laid out for Departments in *Managing Public Money*, which explicitly states that the Finance Director should:

- Maintain a long term financial strategy to underpin the organisation's financial viability within the agreed framework; and
- Develop and maintain an effective resource allocation model to optimise outputs.<sup>28</sup>

12. Currently, it is the Director General for Strategy who manages the long term plans for the Department.<sup>29</sup> The Finance Director's role in long term planning has been limited to providing advice on the financial aspects of plans.<sup>30</sup> This has eroded the authority of the Finance Director and contributed to a pattern of over commitment in future spending plans.<sup>31</sup> Mrs Brennan told us she would make sure the Department complies with the requirements in *Managing Public Money* that relate to the Finance Director's role.<sup>32</sup> We welcome this commitment to ensuring that the Finance Director has primary responsibility for strategic financial planning in the Department.

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26 Ev 22

27 Qq 15-18, 86-89

28 HM Treasury, *Managing Public Money*, box A.4.1B; Q 16; C&AG's report on the defence budget, para 3.29

29 Q 16

30 Q 18

31 C&AG's report on the defence budget, para 3.27

32 Qq 88, 92

## 2 Managing the defence estate

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13. The defence estate covers 1.5% of the UK.<sup>33</sup> It includes 370,000 hectares across 4,000 sites, while the Department also manages a further 200,000 hectares overseas.<sup>34</sup> This estate, valued at over £20 billion, exists to support operations and defence capabilities across the Royal Navy, Army and Royal Air Force.<sup>35</sup>

14. The Department was unable to say whether an estate that covers 1.5% of the UK is too large, too small or the right size.<sup>36</sup> It has few, if any, metrics to determine what an estate of the right size should look like.<sup>37</sup> We noted that, while the built estate has reduced by 4.3% over the last ten years, personnel numbers have reduced by 13.4% – three times more – over the same period.<sup>38</sup>

15. The Department has developed a Defence Estates Development Plan, which was published for the first time in 2008.<sup>39</sup> This plan lists the Department's 571 main sites and how long it plans to keep them for, but it lacks measures or quantifiable targets regarding the cost and size of the estate.<sup>40</sup> Nor does it have information on key measures including condition, operational importance, running costs, value and utilisation.<sup>41</sup>

16. Without this essential information, Defence Estates is not in a position to challenge the armed forces about the need to retain sites or balance the cost of the estate against operational need. Currently, the questions asked to determine whether a site can be disposed of concentrate on whether it has defined use or not – which most sites do. The Department does not ask how heavily the sites are used, how much they cost to run or how much they would be worth if sold.<sup>42</sup> It is therefore unsurprising that little progress has been made on reducing the size of the estate; the RAF, for instance, has only reduced its airfields by 800 hectares (3%) over the last ten years.<sup>43</sup>

17. In part, the reason for the absence of any performance measures or quantified targets is that the Department lacks centrally collected data to assess them.<sup>44</sup> For example, on utilisation, there is no suite of measures to assess the intensity with which airfields are used.<sup>45</sup> Previous efforts to establish a data system have failed. The Department initiated the Estates Performance Measurement System in 2005, and began populating it with data in

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33 Q 108

34 C&AG's report on the defence estate, para 1

35 Qq 163-169; C&AG's report on the defence estate, para 2

36 Qq 98-99

37 Qq 93, 104

38 Q 93; C&AG's report on the defence estate, para 1.16

39 C&AG's report on the defence estate, para 6

40 Q 126; C&AG's report on the defence estate, para 7

41 Qq 100-101

42 Qq 100-101

43 Qq 110-114

44 Qq 126-127, 130-138

45 Qq 103-104

2007.<sup>46</sup> This system has since been abandoned, as the broad scope of the database led to concerns over data consistency.<sup>47</sup>

18. We are astounded that five years of effort and expense have apparently produced no tangible data we can examine to assess how well the defence estate is being used.<sup>48</sup> In our view, managing a £20 billion asset with virtually no understanding of its cost or efficiency is entirely unacceptable.<sup>49</sup>

**Figure 1: Essential data to manage the estate**

Information required	Are data collected locally	Are the data comprehensive?	Are data available centrally?
Operational importance	<input checked="" type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>
Potential sale value	<input checked="" type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>
Running cost	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>
Utilisation data	<input checked="" type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>
Condition	<input checked="" type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>

Yes   
 Partly   
 No

Source: C&AG's report on the defence estate, Figure 15

19. The Department is developing a new system to record data on the estate, including costs and utilisation rates.<sup>50</sup> However, the Department believes that it will take over a year to populate the system with data and could not give a date by which all the data needed to manage its estate would be available.<sup>51</sup> We believe the Department should, within six months, collect sufficient data to allow it to start managing its estate efficiently (such as those outlined in Figure 1). This process would not require a perfect system to be developed, nor should it involve placing an undue burden on the Department.<sup>52</sup> Once this data has been collected to an acceptable degree, it could then be enhanced further to help the Department manage the next generation of major estate contracts.<sup>53</sup> We would also

46 Q 127; C&AG's report, *Managing the defence estate: quality and sustainability*, HC (2006-2007) 154, para 2.16

47 Q 127

48 Q 129

49 Q 163

50 Q 130

51 Qq 131-147

52 Qq 134-136, 143-144, 163-165

53 Qq 141, 144

expect the Department to use improved central data to reassess more rigorously its estate holdings and costs in line with the findings of the Strategic Defence and Security Review.

# Formal Minutes

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**Wednesday 8 December 2010**

Members present:

Rt Hon Margaret Hodge, in the Chair

Mr Richard Bacon  
Mr Stephen Barclay  
Jackie Doyle-Price

Rt Hon Mrs Anne McGuire  
Nick Smith  
Ian Swales

Draft Report (*Managing the defence estate and budget*), proposed by the Chair, brought up and read.

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

Paragraphs 1 to 19 read and agreed to.

Conclusions and recommendations 1 to 8 read and agreed to.

*Resolved*, That the Report be the Tenth Report of the Committee to the House.

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

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

Written evidence was ordered to be reported to the House for printing with the Report.

[Adjourned till Tuesday 14 December at 10.00 am

## Witnesses

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**Wednesday 13 October 2010**

*Page*

**Sir Bill Jeffrey KCB**, Permanent Under Secretary of State, **Mrs Ursula Brennan**,  
2<sup>nd</sup> Permanent Under Secretary, **Jon Thompson**, Director General Finance, and  
**David Olney**, Acting Chief Executive, Defence Estates, Ministry of Defence

Ev 1

## List of printed written evidence

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1 Ministry of Defence

Ev 22



# List of Reports from the Committee during the current Parliament

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The reference number of the Government's response to each Report is printed in brackets after the HC printing number.

## Session 2010–11

First Report	Support to incapacity benefits claimants through Pathways to Work	HC 404
Second Report	Delivering Multi-Role Tanker Aircraft Capability	HC 425
Third Report	Tackling inequalities in life expectancy in areas with the worst health and deprivation	HC 470
Fourth Report	Progress with VFM savings and lessons for cost reduction programmes	HC 440
Fifth Report	Increasing Passenger Rail Capacity	HC 471
Sixth Report	Cafcass's response to increased demand for its services	HC 439
Seventh Report	Funding the development of renewable energy technologies	HC 538
Eighth Report	Customer First Programme: Delivery of Student Finance	HC 424
Ninth Report	Financing PFI projects in the credit crisis and the Treasury's response	HC 553
Tenth Report	Managing the defence budget and estate	HC 503



# Oral evidence

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## Taken before the Public Accounts Committee

on Wednesday 13 October 2010

Members present:

Margaret Hodge (Chair)

Stephen Barclay  
Richard Bacon  
Matthew Hancock  
Austin Mitchell

Nick Smith  
Anne McGuire  
Ian Swales

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### Examination of Witnesses

*Witnesses:* **Sir Bill Jeffrey**, Permanent Under Secretary of State, Ministry of Defence, **Mrs Ursula Brennan**, 2nd Permanent Under Secretary, Ministry of Defence, **Jon Thompson**, Director General, Finance, Ministry of Defence, **David Olney**, Acting Chief Executive, Defence Estates, gave evidence.

**Q1 Chair:** Welcome. Before we start we should that this is Sir Bill's last appearance before the Public Accounts Committee.

**Sir Bill Jeffrey:** Unless you decide to summon me in the next week.

**Mr Bacon:** That can be arranged!

**Q2 Chair:** We will summon you immediately after the CSR—that will be an interesting one. We wish you well in the future. You have only given evidence to this Committee once before but I know from Richard Bacon and from Austin Mitchell that you have given evidence innumerable times before, so thank you for your forbearance in answering our questions. Welcome and congratulations to Ursula Brennan, who I understand has been confirmed as the new Permanent Secretary. Therefore, we look forward to not having to do quite so much business as we have done in the past with you. Nevertheless, if we do have to do business with you, we look forward to those exchanges.

I will start with Sir Bill because you are responsible for a budget of about £42 billion. You are also responsible for ensuring that that budget is spent in a way that ensures the safety of our nation and of our people. The budget itself provides support for the livelihood of some 360,000 to 370,000 individuals whom you employ directly, and probably hundreds of thousands of individuals who work for the Defence industry in Britain. Yet year on year on year, it is not just that you overspend, which is bad enough, but that you deliberately set out and plan to overspend. Right at the beginning of the NAO Report, which you have agreed, there is an assumption that overspend could be in the region of £6 billion to £36 billion—a crazily wide sum—over the next 10 years. Every Department of Government—certainly every Department with which I have been associated—always has plans beyond its means. However, most Departments of Government and most people learn to make do with less. You consistently plan to spend more than you have. Why?

**Sir Bill Jeffrey:** Chair, thank you for your introductory remarks. A preliminary comment is that we have not overspent, in the sense that we have

consistently kept within the money voted by Parliament for Defence. Last year, we had a significant in-year financial management problem. We managed it as well as we could. We came in very close to the spending limit that the Treasury imposed on us and significantly within the money that Parliament had voted. Sometimes in government, I have observed overspending that needed to be addressed by supplementary estimates. We have not been in that territory. We have had a persistent problem of pressure in the budget which probably goes back to the last Spending Review in 2007. Since then, we have been trying, in conditions that I would argue are ones that make it particularly hard, to control that and find ways of taking cost out of the programme. Year by year, we have succeeded in taking some cost out of the programme. However, the fact that we have failed to do so completely has meant that we have entered the year of spend already with a job to do in terms of managing overspends. I don't think that is satisfactory, but it has been a feature of our lives in recent times.

**Q3 Chair:** Mr Thompson, how long have you been in the Department for as Finance Director?

**Jon Thompson:** Since January 2009.

**Q4 Chair:** So you have done a year and a bit. Why have you allowed the Department to overspend? To plan to overspend?

**Jon Thompson:** I am not sure we do have a plan to overspend. The opening paragraph of the NAO Report estimates the projected overspend in the next 10 years and is highly sensitive to four factors, which the Report sets out: what you assume about forward defence inflation, forward pay rates, and forward funding for the Defence budget, as well as the sensitivity of the equipment programme for future decisions, which have yet to be on contract. That is why you end up with a significant difference. £6 billion over 10 years in which you might spend something of the order of £400 billion seems to me to be a number that would be controllable if you balanced the overall strategy for Defence and your financial plan.

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13 October 2010 Sir Bill Jeffrey, Mrs Ursula Brennan, Jon Thompson and David Olney

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**Q5 Chair:** It might be in the circumstances where there wasn't a record and a history of every year having to then implement in-year cuts, which we will come back to; in-year cuts which are always more difficult or more damaging than planning proper spending to live within your budget. The history of the MoD, as I read the Report, is one of consistently having to play around with in-year cuts while at the same time as planning next year's spending in quite a dysfunctional way.

**Sir Bill Jeffrey:** It is true that we had to do that in the last couple of years. Before that we did not have in-year problems of that nature. I reinforce what Jon Thompson says, which is about a 10-year estimate of how much our budget falls short of our then plan.

**Q6 Chair:** With the greatest respect, you have chosen to take the £6 billion. If you take the £36 billion, that is one heck of a lot.

**Sir Bill Jeffrey:** Yes. I was about to take the £36 billion. Firstly, if you look over a 10 year period, you are looking over a very long period. Secondly, as Mr Thompson says, the assessment that you make—and I think the NAO would acknowledge this, as it originally put this figure in the public domain—is extremely sensitive to the assumptions you make about Defence inflation and, more particularly, what subsequent spending reviews end up producing. One of the things that most inhibits us in a business that is principally about long-term investments and operates long-term is that Government spending plans are only set for three years ahead, or in this case, four. Therefore, when the NAO made their estimate, they assumed that the budget would remain constant in cash terms for 10 years. I do not know if that is a fair assumption or not. However, it illustrates the fact that if one had made even slightly different assumptions one would have reached a different figure. Having said that, I do not deny that the inheritance of the recent period is very significant financial pressure and we are having to use the strategic Defence Review that is going on now to try to address that pressure so we can get into a more balanced position in the future.

**Q7 Chair:** The other issue the Report goes on about is that the NAO have found what they called a "culture of optimism". I call it something else: recklessness and irresponsibility, I have to say, Bill. I am not surprised that George Osborne felt that the MoD budget was chaotic and disorganised. Therefore we have some reference to optimism bias. Paragraph 3.18 might be the most sensible one, where you talk about "overcommitted assumptions". That sort of a culture and that approach to budget-making leaves you in a mess. I do not know how you feel about leaving the Ministry with the Defence budget in such a mess.

**Sir Bill Jeffrey:** Firstly, on optimism, I think it is true that there is a tendency to be over-optimistic about the cost of a particular project. That is something we are addressing. We are doing a lot of work to improve cost estimation and to ensure that what is known as optimism bias is driven out from our initial estimates in the first place. I do not think it is the case that we have been over-optimistic in the last few years. Ever

since the 2007 Spending Review, we have been making, year by year, our best assessment of the cost of the programme, comparing that with the budget and then considering what measures we can take to reduce costs. We have been doing so, first, during a period when the Department has been greatly stretched by the operational commitments in Iraq and Afghanistan, and secondly without the cover of a recent Strategic Defence Review. In the last few years we have found that although it is possible to agree within Government cuts and reductions of the kind we have made in our recent planning which get the position closer to being in balance on a clear headed, not over-optimistic view, it has been very hard to take decisions which impact greatly on Defence capabilities, because the natural reaction of Ministers and others has been to say we have not had a Defence Review for while, therefore we cannot take decisions that involve cuts of that nature.

**Q8 Chair:** Are you telling us that Ministers refuse to take the necessary financial decisions, which would have brought you within budget?

**Sir Bill Jeffrey:** I am saying that, at each stage, our best assessment of the shortfall was drawn to Ministers' attention. They did take decisions that took very significant costs out, but they and we were operating in an environment in which the most impactful decisions were ones which one might naturally expect to be taken after a Defence Review, rather than before one.

**Q9 Chair:** I am trying to get some clarity from you on this. Were you suggesting to Ministers that they should cut expenditure on new or existing projects, or on staffing, more than they were prepared to do?

**Sir Bill Jeffrey:** In each planning round, we assessed the difference between the budget line we had and our then estimate of the cost of the programme over the succeeding few years. We drew attention to options and measures that could be taken. Some were taken and some were not.

**Q10 Chair:** As Accounting Officer, why did you not use Letters of Direction if you felt they were not being tough enough on the decisions they were taking?

**Sir Bill Jeffrey:** The view I took was that although we had to draw attention to the financial pressures, which we did, this was not something that was in the territory of seeking formal directions. At each stage, we did ensure Ministers were clear about the position.

**Q11 Chair:** And why did the Director of Finance not? This is a joint issue for Sir Bill and Jon Thompson. It strikes me that if you know you are heading for an overspend you have to draw a Letter of Direction.

**Sir Bill Jeffrey:** We did not know we were heading for an overspend. We knew we had significant financial pressure and the closer we got to the point, the harder we had to work to manage that pressure.

**Q12 Chair:** So the decisions that you took, for example, to cut £800 million out of the 09/10 budget—were they damaging decisions? What

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decisions were they? What did you decide to cut? As I understand it, you took those decisions in about October- November of 09/10 of the financial year.

**Jon Thompson:** I am not sure that is quite right. We took a series of decisions throughout the course of the year, on the basis of the budget information that we had available in that year.

**Q13 Chair:** Not very good long-term planning.

**Jon Thompson:** Indeed. If I might return to the strategic point that you are making, which is the recommendation 21a of the National Audit Office Report, we do actually agree with that. The Department needs to rebalance its strategy with its financial plan. That is absolutely the fundamental point in terms of addressing the so-called deficit.

**Q14 Chair:** It seems to be a very basic point that you do not have your financial strategy aligned with your policy and programmes. When I read that, I just could not believe it.

**Jon Thompson:** Indeed. So we agreed with the recommendations. If I might just say, given that the Government had made a public commitment that it would conduct a Strategic Defence Review after the election, and the previous one was in 1997, the judgment that Sir Bill and I had to make was whether we thought we could survive the interim period for the final two years in the run up to the SDSR and then fundamentally reset the strategy and the financial plan. In other words, make all the big decisions that needed to be made in the SDSR, because they could not be made, in our opinion, before the SDSR. They were sensibly to be made in a redrawn strategy. That's the judgment we had to make.

**Q15 Mr Bacon:** I would like to pursue this point, because paragraph 21b says: 'The financial strategy should be reflected in financial plans prepared by the Department.' It is an extraordinary truism but it is mind-blowing that the NAO needs to make that recommendation. We first saw you on this Committee when you were at the Department for Children, Schools and Families as it was then called. I was mildly disappointed that in your CV you did not mention your excellent start at Norfolk County Council Finance Department. To us in Norfolk, it is therefore no surprise that you have risen to your present eminence. When you were at the Department for Children, Schools and Families, the report we were looking at was about estates management, and there was a huge contrast between the different Departments and how they run their property. The Department for Education was right at the top of that. One believed that this was partly because there was a holistic approach to the use of all the assets, management and financial planning by you as the Finance Director—the finance function, you. It all seemed rather good.

You have now moved over and it is welcome to see you at the MoD as a professionally qualified accountant, because the MoD was one of the last to move across. Furthermore, you are now, and have been for some years, the Head of the Profession. What would you expect the Finance Director of a major

organisation like the MoD or indeed any Government Department to have within his or her purview as responsibilities? For example, would you expect it to include strategic financial planning, because the report says that is not one of your responsibilities at the moment?

**Jon Thompson:** That is correct. I would expect it to be within my remit. I think Sir Bill should respond to the question about what the rationale was for the vision between my post and the Strategy Director. The judgment I had to make as the Head of the Finance Profession with the Permanent Secretary of the Treasury was whether it was better to have a Finance Director within the Ministry of Defence with a slightly narrower remit than that which was in accordance with Managing Public Money, or none at all. Therefore, we made a decision that it was better to establish the post of Finance Director. We discussed it with Sir Bill in the run up to the appointment of a Finance Director, in the knowledge that there were special circumstances in the run up to the SDSR, and then post the SDSR the position would be revisited.

**Q16 Mr Bacon:** When we, as a Committee, visited the Pentagon, we met the Under Secretary (Comptroller)—spelt the same way as the CAG. It was very clear who had responsibility for financial management inside the Pentagon. Why do you not give Mr Thompson the authority to do his job? You have finally got yourself a decent Finance Director. I am not saying your predecessor was not a decent Finance Director but he was not financially qualified. He did tell us that when he appeared in front of this Committee. You finally have somebody who has the appropriate background. Is it not obvious that you align the strategic management of your resources with what it is you are trying to do with them, and give the responsibility of that to one person? Why have you not done that?

**Sir Bill Jeffrey:** I have thought hard about that, Mr Bacon. I take responsibility for that decision and I will do my best to explain it to the Committee. The key to it lies in the other post we are talking about. When I arrived in the MoD I felt that strategy was being dealt with in a large number of different parts of the Department. At one level it was being seen as policy and defence strategy, the kind of issues that the Strategic Review like the one we are doing now goes into. At another, there was business strategy, which was in the hands of a different Director General at the time. Then there was industrial strategy. There were very significant strategic, financial and resource issues involved as well.

Knowing that we would be facing a Strategic Defence Review before long, I created a Director General-level post responsible for strategy within the Department. It is he who has led the major activity on the SDSR. We could only have done it that way because leading the Defence contribution to the SDSR has required the full-time attention of a very senior person. My conclusion was that in this period as we ran up to the Defence Review, the right thing to do was to ask the Strategy Director to lead on the strategic aspects of our financial planning with the strongest possible input from the Finance Director on the strategic

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financial aspects. We received that. Jon Thompson has played into our discussions important assessments of the risks that have been built into our plans on strategic financial considerations that arise.

**Q17 Mr Bacon:** Strategy without money is castles in the air.

**Sir Bill Jeffrey:** I accept that.

**Q18 Mr Bacon:** Years ago, I used to represent the management consulting industry. After the fall of the Berlin Wall there was a long period of consultants flying in to places in Eastern Europe, producing enormous fat reports and then hurling them to the governments concerned from the steps of the aeroplane with a big invoice as they headed back home. That understandably became very unattractive to many Eastern European governments and there was a big shift in consulting, where clients began to say that what they wanted—I'll use the word again—was a holistic approach where at the end they have something that they need. The way to do that is to have integrated management, where the people responsible for the strategy are also responsible for delivering it. Mr Thompson has just said, as the Head of the Finance Profession, that he would expect to have that responsibility and it seems to me perfectly obvious that that is what you would expect, never mind whether it is Defence, in the management of any large Government organisation—you would expect the Finance Director to have those responsibilities. Are you now moving towards that?

**Sir Bill Jeffrey:** Firstly, can I say that I entirely accept that finance and strategy must be completely connected. For the reasons I have given, I thought this was the right way to handle things over that year or so. In practice, because we have had a single team supporting both the Strategy Director and the Finance Director within the finance function, the activity has been well informed by financial considerations and the two individuals have worked extremely closely together. Jon Thompson will agree with that. His own contribution has been huge because as you have observed, he is a very experienced and capable Finance Director. Where we go after the SDSR will be for my successor to decide. However, personally I had always envisaged that we would move back onto a more conventional arrangement.

**Ursula Brennan:** It is interesting to look at the NAO Report, paragraph 3.29 where it says: 'The role of the Finance Director and his responsibilities...is set out... in Managing Public Money.' One of the roles is to coordinate the planning and budgeting processes, and it talks about the long-term financial strategy as part of that. I am clear that the financial strategy is the business of the Finance Director, in our case, the Finance DG. The planning process should be the process by which, having set our affordable strategy, we check that we are on track with it and we make the adjustments necessary in order to deliver it. That should be the responsibility of the Finance Director. Like Sir Bill, I recognise that this Department has been in a position where it has been such a long time since it set its strategy. Most Departments refresh their

strategy more often than the Ministry of Defence has done in recent years.

As a result of that, the planning round, instead of being a planning round where you can plan against a reasonably recent strategy, where you could work on the expectation that the resources in the strategy were directed in the right place and you use the planning round to make adjustments, we were having to use the planning round to surface decisions that are really strategic decisions. It is the SDSR that gets us that opportunity to get that—

**Chair:** I have to say that it is complete nonsense to suggest that because you have not had an overall Strategic Review that you do not do your financial planning in the context of a policy.

**Q19 Mr Bacon:** This is what I do not understand. The report says that the last time there was a Strategic Defence Review was in 1998, which is perfectly true. Any large organisation ought to be refreshing its strategic planning anyway, on a regular basis. I actually wrote the first ever corporate strategic plan for an investment bank I used to work for that was the merger of various different entities, a stock broking firm, a jobbing firm, and a merchant bank. It is a process that has developed hugely over the last 20 years but it has never stopped. It has always been refreshed. You are not really saying you needed Ministers to say that you need an SDR before you can get round to the serious business of having a proper strategic planning function that regularly refreshes itself, are you?

**Ursula Brennan:** Forgive me. Strategy is indeed the business of Ministers. It would not be the business of the MoD to say, "Here is an SDR; we are going to invent a strategy of our own".

**Q20 Mrs McGuire:** With the greatest respect, I am inclined to think that the MoD is slightly different from an investment bank in terms of how it manages its financial strategy because you do not have chiefs of staff sitting on your shoulder, for a kick-off. We need to be realistic about some of the challenges. Mr Thompson, do you have the authority to say no?

**Jon Thompson:** It depends what the question is, sorry.

**Q21 Mrs McGuire:** "I need two aircraft carriers." Do you say, "Sorry, no, we just do not have the money"?

**Jon Thompson:** The decision about the exact nature of capability developed by the Department is clearly a matter for Ministers. My advice is sought on any financial commitment of more than £10 million. I give my advice and then it is for Ministers to make their decisions. That is the standard arrangement around Whitehall.

**Q22 Mrs McGuire:** Returning to the Chair's point, in any other Whitehall Department, if you as the Finance Officer felt that Ministers were asking you to do something—and I just use the aircraft carriers because they're topical—that you feel the Department cannot afford, you would then have a course of action that you or Sir Bill or the Permanent Secretary would need to take?

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*Jon Thompson:* Correct.

**Q23 Mrs McGuire:** Do you have the authority, Sir Bill, to say no?

*Sir Bill Jeffrey:* I have the authority to do as I would do, which is to draw Ministers' attention to issues of affordability in the programme and also, as they decide on particular investments, issues of propriety, value for money, regularity and if they are in relation to the things covered by the Accounting Officer guidance. I would seek directions on things that do not meet that guidance—that in some way involve irregularity or if there is a poorly founded business case; that kind of thing. I will say that this can only go ahead if they give me a written instruction. That is the procedure that the Committee know very well. As I said earlier, at no point through this process have I felt we have reached this point. I have at various stages given Ministers very clear advice about the budgetary position in which the Department found itself and the implications of that for individual projects.

**Q24 Mrs McGuire:** Do you then think there is an inconsistency between the process by which a Defence capability is arrived at and rational financial planning?

*Sir Bill Jeffrey:* Not necessarily. The process in the MoD for generating projects is more elaborate than some Departments because they typically involve equipments, they arise from analysis within the capability area in the Department, principally staffed by military officers, of what capability is required and what equipment will fulfil that capability. Once that has been settled on, the process of project management, accountability, and the putting of project proposals to Ministers and then to the Treasury operates in the same way as other Departments.

**Q25 Mrs McGuire:** And then out of the blue comes Afghanistan?

*Sir Bill Jeffrey:* Out of the blue comes Afghanistan.

**Q26 Mrs McGuire:** So there is a difficulty about rational financial planning and Defence capability that may have to change, almost at a moment's notice?

*Sir Bill Jeffrey:* The significance of Afghanistan is firstly the Afghan campaign, and the Iraqi one before it, not only stretched our brave forces on the ground, but also stretched the Department quite significantly. Some of the financial pressure we have been trying to manage has been a side product of that campaign, even though its marginal costs are met directly by the Treasury. The other significance of it is that, very naturally, when we are committed to the extent that we have been, Ministers want, so far as they can, to divert resources from existing planned projects onto things that are more relevant to the immediate operation. As the Report brings out, in December last year, the previous Government decided to commit about £300 million a year more to operationally relevant priorities. That arguably added to our pressures. We found substantially greater savings at that point. Nonetheless it meant that the conditions in which we were operating were not just affected by

all the normal things, but they were affected by an understandable desire to switch some of our efforts, to the extent that we could, to capabilities that were extremely relevant to the Afghan operation, like Chinook helicopters.

**Q27 Matthew Hancock:** Taking that point a bit further, you were arguing then that the extra £300 million due to the cost of the war in Iraq and Afghanistan was at first taken from savings elsewhere in the budget? Is that correct?

*Sir Bill Jeffrey:* What we did at that point last year, through our annual planning round, and acknowledging that we still had significant pressures in the programme, not just in the year that was about to begin but beyond that, was to search for savings and identify a number of measures.

**Q28 Chair:** Hang on a minute, let me just stop this, because I think this is a rewriting of history. How much extra money did you get from the Treasury on top of your budget in 08/09 for Afghanistan and Iraq? How much extra? You were asked to find £300 million, but how much extra money?

*Sir Bill Jeffrey:* The additional cost of the operations themselves was paid for from the reserve.

**Chair:** Quite.

**Q29 Matthew Hancock:** You had to find £300 million from the savings?

**Chair:** A contribution. But how much extra did you get?

**Matthew Hancock:** Okay, but this is just to get to the key part of my question. You described earlier how you had to survive for two years in the run up to the election because there was not a Strategic Defence Review, is that right?

*Sir Bill Jeffrey:* That was Jon Thompson's phrase, not mine.

**Q30 Matthew Hancock:** Would you recognise that description?

*Sir Bill Jeffrey:* We were managing a difficult situation as well as we could.

**Q31 Matthew Hancock:** What was the impact of not having a SDR in that period when you had to survive on not having that strategy?

*Sir Bill Jeffrey:* The main impact was the one I referred to earlier which is that as we attempted in successive years to address the budgetary shortfall and the financial pressures that we have been discussing. Options which, through our Strategic Review might have been uncovered but which would have had long-term impact on defence capabilities were much harder to take and our Ministers quite understandably felt that they needed to wait for a Defence Review.

**Q32 Matthew Hancock:** Did you think there should have been a Defence Review?

*Sir Bill Jeffrey:* I personally think it would have been better if there had been one part way through the lifetime of the last Government.

**Q33 Matthew Hancock:** Why wasn't there one?

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*Sir Bill Jeffrey:* I do not know.

**Q34 Matthew Hancock:** Is that not something that you as the PUS should have a material input into? If you think that the problem and the reason for your requirements and your budget splitting is because you have not been able to assess the strategy, as you very eloquently described, would you not therefore recommend that there was an SDR?

*Sir Bill Jeffrey:* What I am principally talking about is the year or so before the election.

**Q35 Matthew Hancock:** Sorry, Mr Thompson described it as surviving two years before the election.

*Sir Bill Jeffrey:* The previous Government could have decided to have a Strategic Review during that period but in the event did not. To do it very close to the election would have been extremely difficult. All I am really saying is that, absent a recent Defence Review, there are some types of decision that are genuinely harder to take.

**Q36 Matthew Hancock:** Therefore it is reasonable to say that because of the absence of a Defence Review, that made this problem that we now face in the Defence budget more difficult?

*Sir Bill Jeffrey:* I think it is, yes.

**Q37 Mr Bacon:** Have you ever sought a direction on a major procurement decision?

*Sir Bill Jeffrey:* I have sought a number of directions in my time. Each of them in the normal way have been copied to the Comptroller and Auditor General and thence to your Committee. I need to check whether there is anything related to what you might describe as a major project. They have tended to be other issues of financial irregularity, whether particular payments appeared to be within the scope—

**Q38 Mr Bacon:** I can remember one which was whether the mother of a British soldier killed in the former Yugoslavia could be flown at MoD expense to attend a murder trial. That is the sort of thing you would expect to get a direction on and for the Minister to take the decision. I am talking about procurement decisions.

*Sir Bill Jeffrey:* Procurement decisions—I cannot recall any occasion.

**Q39 Mr Bacon:** If there are projects that are plainly not going to be value for money because of the way in which they are put together is it not one of the jobs of the Accounting Officer at some point to say, “Hang on a minute. I cannot defend this before Parliament as value for money”.

*Sir Bill Jeffrey:* At the point at which we have invested in each of the major projects over the last period, in themselves they have been properly put together, well-supported by business cases. Therefore the normal criteria that one would use to judge whether to seek direction had not been there. The question is whether, with what one might call an affordability challenge, we are in the territory of asking for formal direction. My view is that we were not, but we were in the territory of explaining very

clearly to Ministers what the nature of that challenge was, so that they were well aware of it.

**Q40 Chair:** Returning to this Defence Review, I think it is an easy excuse. Maybe one ought to have had an earlier Defence Review, but it just seems to me reading the way in which you run your budget, you have no mechanism for determining priorities within that overall budget. That does not require a Defence Review. That requires an understanding of your day-to-day business, updating it annually with a three-year perspective every year. I think hiding behind the failure of having a Defence Review absolves you of that responsibility of determining relative priorities within your budget so that you can take budgetary decisions year on year to live within your means.

*Sir Bill Jeffrey:* To be clear, I am not hiding behind the Defence Review. I am saying that the absence of a recent Defence Review was obviously a factor. It was not the case certainly that we systematically prioritised defence capabilities so that one can say this was at the bottom and then therefore drops off. However, the strategic guidance that we published across the Department last year set defence priorities at the highest level. Our planning rounds are intended to be the means by which we can do exactly what you describe, which is to prioritise one capability against another. I don't know whether you want to add to that, Jon.

*Jon Thompson:* No.

**Q41 Stephen Barclay:** Could any of the major projects in your view have been stopped earlier than the Defence Review? It is clear that there was inaction because everyone was waiting for that; given that part of your duties is to find value for money, could you not have acted in other areas sooner?

*Sir Bill Jeffrey:* In theory, major projects can be terminated at any time and it would have been open to Ministers to decide to do so. The fact is, most of the cost reductions that were decided on did not relate to whole capabilities or big projects. In some cases, they were quite significant in their impact.

**Q42 Stephen Barclay:** You said earlier that you would draw issues of affordability to Ministers' attention, but at no point did you feel you had reached that point. What would the point have been at which you would have felt that you had reached the point?

*Sir Bill Jeffrey:* It is a hard question to answer, to be frank. All one can do is make a judgment at the time on the basis of the facts as they are. It is an issue we have discussed within Government and with other colleagues, including in the Treasury. There is an issue about the extent to which the affordability issue, which does not really get mentioned in the existing Accounting Officer Guidance at all, ought to be one that can give rise to directions. My view at the time was that although we were facing significant issues regarding the affordability of the programme, as long as we were taking active steps to address them, we certainly were not in the territory of conventional Accounting Officer directions, propriety, etc. It is an



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interesting issue and it is one that I have discussed with a number of my Permanent Secretary colleagues.

**Q43 Ian Swales:** By any standard you are running a huge organisation here, which must require tremendously robust systems to make it work. I note that from the Report that the last set of accounts that you published were qualified for various reasons. It is mentioned in the summary in section four. Also when we saw you, Sir Bill, on the tanker aircraft project a few weeks ago, the recommendations were made there about improvements in financial and performance management systems. Given that we are now talking about the whole of the Ministry, what are your comments about the state of the systems and in particular how that enables you to control all the aspects we are talking about here?

**Sir Bill Jeffrey:** Firstly on the Accounts qualifications, they do affect the business significantly. There is a specific story attached to each which we can go into if the Committee wishes. In each of them, we have taken rapid action to address them. In one case, a qualification attached to the accounts in 2008/2009 was withdrawn in 2009/2010. In others there are more systemic problems to do with stock control and how we track stocks, for example, which I think the NAO feels we are addressing as vigorously as we can, but it will take more time. On the general systems issue, we have been strengthening our financial systems. A weakness that the NAO report draws attention to is that some years ago we were less good than we needed to be at identifying financial risks and budgeting them in. In particular issues like the amounts we assumed we would be spending on pay. We have moved quite a long way on that in the last few years.

**Q44 Ian Swales:** Mr Thompson, what do you think of the state of systems under your command?

**Jon Thompson:** The state of financial systems in the Department is variable. Some of them are very good—the core general ledger systems are very good—but some of the financial feeder systems, for example the stock system, have clearly been built up over a significant period of time. To scale it, we run 845,000 lines of stock spread across 78 IT systems, which are then brought together in a single number on a balance sheet. That is £6.3 billion—the gross number is £9.1 billion. Therefore, the scale of the operation is really significant. We received the qualification in 2008/2009. The Chief of Defence Materiel was charged with resolving that situation and the further we got into it the more complex the situation has become. The limitation of scope this year is even more complicated than it was the year before, which I think demonstrates the fact that we understand the problem more. The Chief of Defence Materiel is trying to sort that issue out. That is probably the worst example but equally there are some very good financial systems in the Department.

**Q45 Ian Swales:** What about the high level of systems that enable people to have their hands on the levers, as it were, in terms of financial spending, early warning and such like?

**Jon Thompson:** The in-year financial management system, called the Planning Budgeting and Forecasting system—PB and F, as we call it—we have substantially improved in the last 18 months. Therefore, the Department has moved from a situation where it received a financial report once a quarter, approximately two and a half months behind, to now receiving monthly data within five days of month close. We have therefore significantly speeded up reporting on the basis of that system, which I think colleagues in the NAO would support. I could now tell you at any point in the financial year where we are. We have made some significant strides forward in that respect.

**Sir Bill Jeffrey:** Additionally, as the Report brings out, both this year and last, we have inside the year had to manage budget very closely to keep it within the totals. Having quicker and more reliable systems has made that much easier.

**Q46 Austin Mitchell:** In February 2010, the Defence Board recommended the plan for 2010 to 2011 for spending £185 million above its known funding. By May, when the assumptions behind that were tested, the shortfall increased to £500 million. Why did that happen? Why does it happen? And why does the MoD plan to spend more than it can ever realistically receive?

**Sir Bill Jeffrey:** Firstly, the growth from £185 million or £186 million—I cannot remember which—to £500 million is almost exactly 1% of the budget. This is not, in a budget as large as the Defence budget, hugely material. It is not uncommon.

**Q47 Austin Mitchell:** So it is peanuts?

**Sir Bill Jeffrey:** I am not saying that, of course I am not saying that. In Government as a whole, you rely on two things. One is the top-down estimate of what the spend will be, which emerges from our planning round. As you approach the spend you rely on the budget holders' estimates of what they will spend. It is not uncommon for these to come in higher, and as the year goes by for them to shade down towards the original total. This year, we have certainly had to work quite hard, to put it mildly, to ensure that we do in fact keep within our budget. Without in any way describing it as peanuts, the increase from £185 million to £500 million—

**Q48 Chair:** It then became £800 million.

**Sir Bill Jeffrey:** I am talking about this year. It is not that unusual. It certainly presents us with a challenge in-year.

**Q49 Austin Mitchell:** Let me try another tack. I do not know whether Jon Thompson is a trained accountant but I do not think you have necessarily benefitted from your experience at Ernst & Young because accountants normally sit there straight-faced, and impassive and show no emotion. When our Chair said this was a mess, you nodded. That is incredible for an accountant. That makes me worried, because I wonder if, for the last year or so, Sir Bill, you have not been training as a juggler perhaps, for a post-retirement career. You have been spinning out

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contracts, haven't you, and spinning out the life of equipment and helicopters in Afghanistan? You have been overspending what you can afford and been trying to cut out £800 million of economies in the course of the year. Is it fair to describe your last year as juggling?

**Sir Bill Jeffrey:** You once accused me, Mr Mitchell, of being a betting man in a previous Committee. This is a new one.

**Q50 Austin Mitchell:** This is the last time I will be able to sling these accusations at you. While you are here, I might as well.

**Sir Bill Jeffrey:** I don't think this is juggling. It is a phrase like "peanuts". What I would admit readily is that the last few years, under the various pressures that I have tried to describe as dispassionately as I can, have involved us managing a difficult situation as best we can and sometimes taking decisions that are sub-optimal, to put it mildly. In that sense, I plead guilty. However, there are some mitigating circumstances to do with the way Government plans its expenditure, the inflationary pressures we face, the commitment in Afghanistan and the lack of an immediate or recent strategic review.

**Q51 Austin Mitchell:** There are certainly mitigating circumstances, but we are ordering a lot of equipment for a Cold War that is dead, including huge aircraft carriers that must tie up a lot of guts to protect, like the Euro-fighter, Typhoon or whatever it is called, like the Trident renewal, all stuff for dead wars when we are actually fighting wars in primitive situations that are testing our equipment to the limit. You have to order new equipment and string out the life of existing equipment. Can we do these two things—can we buy all this technical stuff and heavy equipment, and fight two wars at the same time? It is not possible, is it?

**Sir Bill Jeffrey:** I won't say it is impossible, but you have just illustrated very well the nature of the strategic challenge we have faced in recent years. One of the dilemmas that Defence faces is that major investments in big platforms, like aircraft carriers and submarines and fast jets, are on a long-term basis. You must make judgments about what the longer-term future will look like. We are going through a review now which is attempting to make exactly these kinds of judgments. There is no doubt that to set alongside that the intense expectations that have been placed on us and our Armed Forces in the last few years does create tensions. They are illustrated by the episode that we discussed earlier, where for very understandable reasons, even though the majority of the Afghanistan costs are met from the reserve, our Ministers wanted to shift the cursor a little towards equipment and capabilities that were more directly relevant to the things we are doing now.

**Chair:** As you would say, that was less than 1%.

**Q52 Ian Swales:** A supplementary on Mr Mitchell's juggling comments, if you like. Under pressure, how does one save £800 million out of this budget? What did you actually do? How easy was it and how much more was there to go at?

**Sir Bill Jeffrey:** I do not want to make this sound too easy. The point I made earlier about the extent to which in any internal monitoring system, as you go through the year, some projected overspend tends to disappear is valid. That helped us a bit. Furthermore, internally we have been taking quite severe measures on overtime, recruitment, travel and all the expenses that one can bear down on at short notice.

**Q53 Ian Swales:** 'Some projected overspends disappear'—what does that mean?

**Jon Thompson:** Perhaps I could illustrate. If you fully cost the number of people you employ at the beginning of the year then you have a projection of how much that will cost for the full year. We have had a brake on recruitment, which has reduced inward recruitment by 80% in the current financial year as against the previous year. The overall headcount is also fairly rapidly reducing. In the course of the current year, the headcount in the MoD, its civilians will have reduced by nearly 5% year on year.

**Q54 Chair:** That was an imperative put on every Department by the centre and therefore should have appeared within your budget. Every Department had this imperative to reduce its central administrative costs.

**Jon Thompson:** I am not sure that is quite true. When the Department set its budget, it was not the situation. The situation changed. The Department predicted how much it was going to spend, then they put the brake on. You can save money in-year.

**Q55 Chair:** My understanding is that every Department across Government has been reducing its central admin costs year on year as part of the budget making process.

**Sir Bill Jeffrey:** We have been doing that. I think what Jon Thompson is saying is that in addition in-year we have this year and last acquired—

**Q56 Chair:** I want to ask about your £800 million in 09/10, and then your £500 million, as I understand it in 10/11. I understand that quite a lot of it was saved in deferring schemes. Every time you defer a scheme, all you do is massively add to the cost. Is this a sensible way of doing your business?

**Sir Bill Jeffrey:** No, it isn't.

**Q57 Chair:** Then why do it?

**Sir Bill Jeffrey:** That is why I accept the burden of the Report's recommendations. To some extent, in managing these in-year pressures, we have managed to do so through a more parsimonious approach to running costs through the extent to which projected overspends sometimes do disappear. We have also had to shift some things to the right. I do not pretend that is anything other than a sub-optimal thing to do because normally it does add to costs in the end.

**Chair:** Massively

**Q58 Matthew Hancock:** Coming back to a point made by Austin about some of the consequences of the strategic financial management, the decision on the aircraft carriers, which was one of the biggest

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items of future expenditure, could you remind me when the go ahead was made to cut the aircraft carriers?

*Sir Bill Jeffrey:* In 2007.

**Q59 Matthew Hancock:** You mentioned before sometimes that you brought to Ministers' attention that this would not fit within the plans, or would heighten the financial difficulties; did you do it on that occasion as well?

*Sir Bill Jeffrey:* This was at the end of the 2007 Spending Review. We took stock of the position in which the outcome of the Spending Review left us. Shortly afterwards, the commitment to the aircraft carriers was made. The advice that was given to Ministers was that, as current plans stood, they would only be affordable if we revisited the equipment programme and identified some savings from elsewhere, including some quite significant capability.

**Q60 Matthew Hancock:** For example?

*Sir Bill Jeffrey:* We did not identify them at that stage.

**Q61 Matthew Hancock:** So you identified the size of the hole it would leave elsewhere?

*Sir Bill Jeffrey:* We said, in effect, that the carriers would be affordable only if steps were taken to reduce the cost of other significant capabilities.

**Q62 Matthew Hancock:** And were those steps taken?

*Sir Bill Jeffrey:* As we got into 2008, the then Ministers on advice decided that it would be right to have a thorough examination of the equipment.

**Q63 Matthew Hancock:** So they went ahead with the decision on the aircraft carriers without the consequent decisions to reduce costs elsewhere?

*Sir Bill Jeffrey:* They went ahead but they then, in the ensuing period, undertook an examination of the equipment programme with the view to taking significant costs out, among other things, to ensure the carriers were affordable.

**Q64 Matthew Hancock:** Shortly after these contracts were signed, am I correct in my recollection that a delay introduced into the carrier programme?

*Sir Bill Jeffrey:* Later, in early 2009, partly as a consequence of the equipment examination, it was decided-

**Q65 Matthew Hancock:** What was the cost of that delay?

*Sir Bill Jeffrey:* The then estimated cost of it was £674 million.

**Q66 Matthew Hancock:** Do you think that represents good value for money? Taking a decision and then within 18 months adding £674 million due to a delay?

*Sir Bill Jeffrey:* I do not think it does.

**Q67 Matthew Hancock:** And therefore did you ask for a Letter of Direction?

*Sir Bill Jeffrey:* Not in relation to that.

**Q68 Matthew Hancock:** Who took the decision?

*Sir Bill Jeffrey:* The Secretary State for Defence.

**Q69 Matthew Hancock:** Do you regret that whole chain of events?

*Sir Bill Jeffrey:* Clearly I do. I think that at the point that we were at when the decisions on the equipment examination were taken, either late 2008 or early 2009, among the range of options that were available, deferring the in-service dates of the carriers in order to save some hundreds of millions in the early years was available in the way that others were not. Therefore that decision was taken.

**Q70 Matthew Hancock:** Has that whole chain of events made the current SDR more difficult?

*Sir Bill Jeffrey:* It has, but I like to think we have learnt from that experience.

**Q71 Matthew Hancock:** I would hope so.

*Sir Bill Jeffrey:* In the SDSR we are being as clear as we can be about what would constitute an affordable programme. To my mind, if I may in my last appearance before this Committee, one of the most important things about the SDSR is that it should generate some Defence plans that match the budget that is likely to be available to pay for them.

**Q72 Matthew Hancock:** Do you think that will happen?

*Sir Bill Jeffrey:* I hope so.

**Q73 Mrs McGuire:** Is that possible, given the long history of the MoD and the tension that there is between the civilian civil service, the politicians and the Chiefs of Defence staff? Or is that just the hope of a civil servant who is leaving?

*Sir Bill Jeffrey:* Firstly I would not describe the relationship as a tense one. There are respects in which—

**Q74 Mrs McGuire:** I meant tension, as opposed to tense.

*Sir Bill Jeffrey:* In the last few years there has been quite a good appreciation on the part of the Chiefs of Staff that, although individually they would be protective of the things they care most about, collectively it would be better if we have a programme that is not overheated and is capable of being managed more readily within the resources we are given.

**Q75 Mrs McGuire:** Will Mrs Brennan travel in hope or in expectation?

*Ursula Brennan:* I will travel on the basis of continuing with the work we are doing now, to do the professional business with Jon Thompson to ensure that we have the information that enables Ministers and the Defence Boards to take informed decisions.

**Q76 Stephen Barclay:** How much is the discretionary element in your budget?

*Jon Thompson:* What do you mean by "discretionary"

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**Q77 Stephen Barclay:** A large part of your budget is pre-spent, personnel, capital—that sort of thing. What sort of discretionary element do you have?

**Jon Thompson:** We do not really recognise the term, but to try to respond to your question, when you enter into any particular financial year, approximately 20% of the budget is uncommitted, and you have the ability to slow that expenditure or stop it.

**Q78 Stephen Barclay:** What I am driving at is there was paralysis because there was no SDSR. So you were saying you couldn't because that had not taken place. Yet we had an £800 million adjustment required that clearly had an effect. I would like to get a sense of the flexibility you have in terms of your budget allocation.

**Jon Thompson:** The flexibility is approximately 20% in any year. This includes items that are scalable such as how much fuel will be used, flying hours; training in any particular year.

**Q79 Stephen Barclay:** So that would not conditional on operational requirements in Afghanistan?

**Jon Thompson:** No, the operational requirements in Afghanistan are dealt with separately in terms of the claim on the reserve. If I might answer your question, the answer was, for the last financial year, £3 billion, £820 million was the—.

**Q80 Chair:** £3 billion?

**Jon Thompson:** £3 billion, £820 million was the claim on the reserve.

**Q81 Chair:** Right. You were asked to find £300 million from your own budget as a contribution to the operation in Afghanistan.

**Jon Thompson:** We weren't asked to. We chose to reprioritise in order to do some activities that do not fall within the scope of the claim that you can make against the reserve. There are some very tight rules about what you can and cannot claim against the reserve. We chose to reprioritise £300 million to do some activities which were pre-deployment and so on, which you could not claim against the reserve.

**Q82 Stephen Barclay:** And when you say 20%, that is not including reserves in terms of your flexibility?

**Sir Bill Jeffrey:** No, the Report deals with this somewhere round about paragraph 2.8 or 2.10 and makes the point that with approximately 75% of the budget allocated in advance, the ability of the Defence budget to respond to unexpected events in the short term is limited.

**Q83 Chair:** I read that, Sir Bill, and I have to question that. All public services are people. To the extent that if you went to any Department of Government, 75% of its expenditure is tied up in people. The difference with you is probably quite a lot of it is also tied up in capital expenditure and capital equipment. I do not think any other Department of Government would say that because they were spending money on people, that was a fixed cost that they could not shift. I do not understand why the MoD chooses to say that is an inflexibility with which they

cannot cope, whereas presumably when you were in DCSF or in any other Department of Government, you were able to think about teachers in schools or nurses in hospitals, anything like that, when budget constraints emerged.

**Jon Thompson:** Yes, I do not think I indicated that people were fixed costs. I indicated very clearly that we took in-year action because I do not think they are fixed. You can change the level of people over a period of time, they are not fixed.

**Q84 Chair:** So why is 75% considered fixed, including your personnel costs?

**Sir Bill Jeffrey:** I was quoting from the Report. There is a certain extent to which reducing people numbers quickly tends to be more rather than less expensive. Frankly, there are also some issues in the Armed Forces, which is that there is an understandable reluctance to scale down opportunistically in the course of a year. Within that, we have been reducing civilian numbers, for example, quite rapidly.

**Q85 Chair:** But even if we were to accept it, there are 8,000 people at any time in Afghanistan and 40,000 committed to that in a force overall of 180,000. There is flexibility there which any other Department of Government including Education, with teachers, and Health, with nurses and doctors, would not see themselves constrained in the way the MoD tries to see itself.

**Sir Bill Jeffrey:** All I would say is that the size of the Armed Forces is one of the issues that the SDSR is looking at.

**Q86 Mr Bacon:** Mrs Brennan, may I ask you about paragraph 3.30, the last paragraph of the Report, on page 27, which says, "By introducing the arrangements described in paragraph 3.27, in our view"—the National Audit Office's view—"the Department is running the risk that the next planning round will not have a sufficiently well-articulated strategy underpinning it." Do you agree with that?

**Ursula Brennan:** I suppose it slightly depends on what you think of as the next planning round. Sir Bill has explained the approach we have taken in relation to planning our business in the context of the run up to and through the SDSR. I think we have stated already that it is our intention to develop a financial strategy and that in relation to the next planning round—in other words, the one that comes after the SDSR—we do expect to have a clearly articulated strategy and a planning round operated by the Finance Officer which delivers that.

**Q87 Mr Bacon:** What this paragraph is talking about is the architecture which is described in paragraph 3.27, where the Director General for Strategy reports directly to the Permanent Secretary but is not a member of the Board, and the Director General of Finance, who is a member of the Board, provides advice on the financial coherence of the emerging plans, risks and the contingency? And what this paragraph is saying is that this structure and architecture increases the risk that the planning round will not have the sufficiently well articulated strategy

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underpinning it. Are you going to change that structure?

**Ursula Brennan:** It is our intention to change the planning round process for the future.

**Chair:** That is not what you are being asked.

**Q88 Mr Bacon:** Are you planning to keep the Director of Strategy in the way that Sir Bill has created it, where Mr Thompson as Director of Finance does not have the full responsibility, or will you change it so that Mr Thompson as Finance Director does have the full responsibility in a way which, as Head of the Government Finance Profession, he said he would expect a finance director in a Department to have?

**Ursula Brennan:** I am sorry, I was going to come on to explain that. We do wish to change our planning round, which we think at the moment is over-complex and over-burdensome on the business. As part of that, we also intend, as part of the SDSR, to reduce the size of our head office and to change and slim down the roles within head office. As part of that, Lord Levene is leading a Defence Reform Review for the Secretary of State about the organisation and structure of the Department, which is precisely looking at the relationships between the different roles within the Department, which includes strategy and planning. However, as I said previously, it is our intention that, having established our strategy in the SDSR, we should be able to move to a position where the Finance Director is able to conduct the planning round in the manner described in *Managing Public Money*.

**Q89 Mrs McGuire:** I can't get a feel of where the ultimate authority lies. Who says, "Sorry, we cannot do this. We cannot afford it?" Who says no?

**Ursula Brennan:** We ought to be clear on that. The Accounting Officer is the accounting officer in the Department. The relationship is between the Accounting Officer and the Secretary of State. Ultimately it is the Secretary of State who takes decisions on the advice of the Accounting Officer. The Finance Director provides the financial advice but, forgive me, I have not yet taken over this responsibility, but I think Sir Bill will confirm that is the division.

**Q90 Mrs McGuire:** Sir Bill, I think you said you'd never said no?

**Sir Bill Jeffrey:** I don't think I said that. I never asked for a direction. I do not think the Committee would expect me to go into the details of advice to Ministers. Ministers decide on advice, but sometimes that advice is quite strong.

**Chair:** We haven't got a yes or no to Richard's question. Is it possible?

**Q91 Mr Bacon:** Mr Thompson, what further changes would you like to see to strengthen the internal financial management of the Department

**Jon Thompson:** My role is set out in my job description. It is for the Accounting Officer to make the decision and clearly I am sympathetic to what the Report says between paragraphs 3.27 and 3.30. Obviously my line manager will indicate what tasks—

**Q92 Mr Bacon:** You are also the Head of the Profession so you have some standing in the industry so to speak in terms of Government finance. You are a very welcome addition to the MoD as a qualified accountant—from Norfolk. There was a glaring omission that such an enormous budget had a Finance Director in charge of it who was not a qualified accountant. We will come on to whether Mr Olney is a qualified chartered surveyor later, I expect. From my point of view as a Norfolk MP, and a Member of this Committee, you are very welcome in the Department. It is therefore interesting to hear your views as Head of the Profession on what you think can be done to strengthen the internal management of the Department.

**Jon Thompson:** Clearly as Head of the Finance Profession in the Treasury I would expect the Department to comply with *Managing Public Money*.

**Ursula Brennan:** I am sorry if I was not clear; I thought I had made that commitment.

**Mr Bacon:** You did, Mrs Brennan; we just like to have it with your name signed in blood. That is very helpful, thank you.

**Q93 Chair:** I am now going to move us—Mr Olney has been waiting patiently, to some consideration of the other Report we have from the NAO and the question of whether the defence estate is of the right size to meet the operational needs. The most obvious first question that hits you when you read this Report is that in the last 10 years you have reduced your personnel by 13.4%. You have only reduced your built estate by 4.3%. Whilst that reduction has led to some very welcome financial income for Government, it is not enough. Why have you not reduced the estate in line with the reduction in personnel?

**David Olney:** Chair, it is a metric that has some credence but it is not the only metric you can look at in terms of comparing the size of the estate against a reduction in personnel. It was one that the NAO in the report said in the absence of others, this is the one we will use. And we may no doubt come on to that later. You have to look at two thirds of the estate as training estate. Indeed, in the NAO report they recognise that that estate has increased. Therefore you have an increase in training estate which is offsetting a decrease in the built estate. The built estate includes airfields, barracks, and we have made demolitions and changes to assets within the estate that clearly would not have been in this Report. The point is that it is not an easy comparison to make.

**Q94 Chair:** Why have you had to increase the training estate? I did not even understand that.

**David Olney:** The increase in the training estate comprises three components. We increased the freehold of the training estate by some 2,300 hectares. This mainly arose from the purchase of Cape Wrath in Scotland from Naval Gallery in 2000. We increased the leasehold estate by 1,700 hectares and the main increase was training rights; that is to say, walkover rights from estates we do not own but we use from other large land owners in the UK, of some 8,600—

**Q95 Chair:** But why?

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**David Olney:** Because of the increase in training that has gone on in the UK.

**Q96 Chair:** With a smaller Armed Services?

**David Olney:** Our mission-specific training has increased from 1.1 million man-days in 2003 to some 3.9 million man-days in 2010, which is an example of our increase in training.

**Q97 Austin Mitchell:** There has been some transfer from Germany?

**Sir Bill Jeffrey:** Some. Redeployment to and from Iraq and Afghanistan has been the main driver.

**David Olney:** Mission-specific training.

**Ursula Brennan:** An example of that would be the Afghan village that we have had to build as a new training estate to train people to fight in Afghanistan.

**Austin Mitchell:** They've got some good estates in Grimsby!

**Q98 Ian Swales:** On the same lines of ownership of land, I am from North Yorkshire, and the MoD own quite a large slice of North Yorkshire as far as I can see, and in fact over 1% of the whole of the UK. How do you assess the cost side of that? If you are taking on new assets, what is the cost benefit analysis? How would you assess the assets that you hold, and whether it is right to retain assets of a certain value? I am trying to get to what financial considerations are taken in deciding to have what, by any standards, are huge tracts of land all over the country.

**David Olney:** In answering how we make an analysis of movements around the estate, I will give an example of the troops back via our Borona Programme into Innsworth, Stafford and possibly Cosford later. We have a full analysis of the cost of the troops and the cost in Germany. We can compare that against the cost of relocating those troops and the build programme in the UK. That is a full business case, which in this case would go to Jon Thompson and Defence colleagues to approve. With regard to the second part of your question, what is the relation to the value of the estate and how we use that to assess whether we keep it, we look at the estate, as you may have read, that we treated as core estate and retained estate. We are continually looking at the retained estate as to whether there is the possibility of disposal of that estate, or indeed greater utilisation of it, should we want to do something else. Therefore when we come to look at those things, it is absolutely a factor that we look at the market value of that estate. In many cases, the cost of moving out of the retained estate is greater than the market value, not the value to us, but the market value of that estate. We therefore obviously make a business decision as to whether it is sensible and affordable enough for us to move out.

**Q99 Ian Swales:** Do you have a register of current values of everything?

**David Olney:** We have a register of 200 sites. We certainly do not have a register of every single value because that would be an enormous undertaking to keep up to date when, on market value—that is the value to the market, as opposed to the value to us—

we have no possibility of disposal, or indeed no desire or plans for disposal.

**Q100 Chair:** The concern articulated in the Report is the way in which you set about determining whether or not a particular site should be part of your core estate is inadequate. If I turn you to figure 13 on page 32, the question that you ask in determining whether or not it should be part of the core estate is whether the site has a defined defence function, to which it is probably dead easy to say yes. Whereas, if you go over the page to figure 14—the suggestions from the National Audit Office of the sort of questions you should be asking as to whether or not that site should be retained as core—you do not ask, is it in good condition? Are the running costs very high? Is the utilisation intense enough to make it worthwhile keeping, and what are the potential receipts? Therefore it seems, as articulated in the Report, that you are not asking the right questions that would enable you to release far more sites to bring in additional income to Government.

**David Olney:** I think it is true, and we have accepted the NAO's observation, that we need to do more in this area. However, I know that when we look at sites for rationalisation—that is individual cases—it is absolutely the case that we look at the condition, because we must look at the expenditure on that estate compared with something else.

**Q101 Chair:** But you do not look across the piece do you?

**David Olney:** We don't, because the resources we would have available to keep that on an ongoing basis while we have no intention of selling large amounts of the estate would be enormous. What we do is focus our efforts and resources on that estate which we believe has a potential to be sold and realise value to Defence, and also estate where studies indicate that there is high market value. Therefore we put options to Defence.

**Sir Bill Jeffrey:** It is worth remembering where this has come from within the Ministry of Defence. It is not very long since responsibility for the estate was spread all over the place, including in the individual services. When we created Defence Estates, we brought this together for the first time. We are now managing the estate more as a single entity and although it has some criticisms, which I think we broadly accept, the NAO acknowledges that we have seen a significant strengthening of the estates planning and a longer-term focus that was previously absent from defence estate management. So there is some praise in there as well. This is a journey; we need to learn from support and receive much better information from the centre. We need to be more driven by the considerations that the second of these charts points us towards.

**Q102 Stephen Barclay:** If I take you to figure five on page 16, specifically to airfields? It shows in 1998 we had 27,000 hectares and 10 years later, it is only reduced by 800 hectares. To benchmark it, RAF Kinloss is 666 hectares, Lossiemouth is 580. So a

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reduction of 800 hectares in 10 years seems a little modest, why is that?

**Ursula Brennan:** It may be worth commenting that one of the factors that is true of the defence estate all together, particularly in relation to disposals, is that we have a large and very diverse estate comprising of all sorts of different types of buildings and holdings. Disposal is much easier when you are able to say an entire base is closed down. Closing down a whole base quite often relates to disposing of a particular type of aircraft. If you get rid of a particular type of aircraft you can close a base, remove all the pilots who must train to use it and you can sell off the premises. A lot of what happens in Defence is not that kind of removal of a particular variety of thing. If you got rid of all the tanks in the Army, there are various portions of the estate that you would dispose of, but the reductions that you see in manpower are mostly not of deleting an entire type of thing, so that is one of the reasons why in relation to airfields—

**Q103 Stephen Barclay:** The Department did a review of airfields in 2004 during this, and obviously that does not seem to have had much impact. Do you keep a central record of utilisation of airfields?

**David Olney:** It would return to the point I raised earlier of what you mean by utilisation of airfield. It is an extremely difficult thing to assess. It is not like with BAA, who would look at it in relation to how many flights are going abroad. We have a number of measures. We look at how much we spend on the airfields and what the condition of the airfields is. We compare what we spend on one airfield to another. However, it is extremely difficult to have a measure.

**Stephen Barclay:** Surely if you look at how you spend, you are looking at how they are used?

**Q104 Mr Bacon:** I simply do not accept that it's difficult to have a measure. You probably want more than one measure. I accept that. I recently visited RAF Marham with a fellow Norfolk MP, and it is used for lots of different things. Tornados are flown from there. I watched a couple take off and a couple land, going on an exercise. It is used for air traffic control purposes. There is a big hangar there where they basically strip down Tornados after they have flown for 160 hours and put them back together again. You might want to have a metric about the number of takeoffs and landings like a civilian airport would, the amount of air traffic control activity, the number of aircraft that are repaired and serviced in a year. These are all metrics you could have. The idea that it is difficult because there is more than one is surely not sustainable.

**David Olney:** As Sir Bill said, our focus on the years in which we have been managing the estate has been more about understanding the nature of the assets we have, the condition of those assets, the health and safety of the estate, energy and those things. We are now in a position to move forward and, as the Report notes, we are now looking at an asset management system and the metrics going forward to start to measure such things. We have been in discussion with companies and organisations that have large-scale assets, be they BAA or Shell or others to assist us.

Indeed, the NAO are assisting us with that work in the future.

**Q105 Chair:** How many people work with you on this at the centre? How big is the team managing the entire MoD estate?

**David Olney:** It is over 3,000.

**Q106 Chair:** 3,500 people work in this area, but you do not have sufficient resources at the centre.

**David Olney:** That is within the defence estate, covering everything. That includes site teams, managing the training estate, managing projects and chartered surveyors.

**Q107 Mr Bacon:** Can I ask if you are a qualified chartered surveyor?

**David Olney:** No, I am a chartered engineer.

**Q108 Mr Bacon:** I know you are an electrical engineer, because it says so on your CV but you are not a surveyor. You manage one of the largest chunks of land in the country. It says in the report that it is 1.5% of the UK land mass. It is an enormous estate. Is it not rather odd that you, as the person in charge of it, do not have an estate management qualification or surveyor qualification?

**David Olney:** I have a large number of qualified surveyors who work for me.

**Q109 Mr Bacon:** How many do you have?

**David Olney:** I do not have that exact number but I could find out if the Committee wanted to know.

**Mr Bacon:** I do, yes.

**Q110 Stephen Barclay:** Going back to the utilisation point, is one of the problems that there is too much inflexibility with just one type of aircraft tending to be used. For example, I was quite surprised to see one base is used for the Red Arrows, who spend a lot of their time training overseas, but I do not see much that much else going on in terms of flights. Perhaps we could take the GR4A Tornado because that relates to Norfolk and also RAF Lossiemouth. How many Tornados do we have in the UK that are flying in service?

**Ursula Brennan:** Can I respond to this? Some of the questions that you are asking about, for example the usage of airfields, are precisely the things that the RAF is concerned with in terms of how they organise their manpower, equipments and contracts. The arrangement that we have between the RAF and Defence Estates is that it is the business of the RAF to organise how it organises and manages itself efficiently across the different sites. The questions about where aircraft are and where it is sensible to put the Red Arrows will be to do with the tasking they perform, the sunk costs and the investment they are making.

**Q111 Stephen Barclay:** I am making a separate point.

**Ursula Brennan:** These decisions are not being taken by Defence Estates.

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**Q112 Stephen Barclay:** It is a separate point I am trying to make. Firstly, there seems to be inflexibility in terms of which flights are used in particular airports. Some fields seem to have very low usage. Of course the RAF will want as many airfields as possible. That stands to reason.

**Ursula Brennan:** Could I just correct you? It is not in the interest of the RAF to have as many sites as possible, because it is very expensive for them to be distributed across a variety of sites.

**Q113 Stephen Barclay:** It has only been reduced by 800 hectares in 10 years so they are not exactly driving this change. From Defence Estates making a recommendation for one of these sites to be closed, how long does it take before sign off to that decision is given?

**David Olney:** It is not Defence Estates' individual decision; it is done with the services for the closure, so we would make that point. The nearest that we would give would be would be Cottesmore, which has come up recently, where that would be closed in 2013.

**Q114 Stephen Barclay:** That was not my question. In a commercial world, you present a paper to the Board. A couple of weeks later they make a decision. That is the way you expect it to work. Is it taking up to 18 months from Defence Estates making recommendations for actual sign off to take place to those decisions? How long does it take, because there are a multitude of stakeholders here? We have 3,500 members of staff at Defence Estates, usually with two or three going to each meeting, so I am told. They then make a recommendation, so there is huge bureaucracy. Even once you get through that bureaucracy and get to that recommendation, from Defence Estates making that recommendation, how long does it take before a decision is taken?

**David Olney:** It varies hugely, depending on the nature. There are some small sites where we can move rapidly within a week or month. There are other sites that take longer because of what we must re-provide or what the knock-on effects are of that closure.

**Q115 Stephen Barclay:** How many people are involved in the decision, in terms of the various stakeholders that it needs to go through?

**David Olney:** There would be a recommendation from the TLB and Defence Estates, and it would go to the Defence Board if it were a large scale reduction.

**Sir Bill Jeffrey:** In terms of what Mr Barclay has been talking about, a decision to divest ourselves of an airfield would almost certainly flow from decisions about the future shape of the RAF, where flights—

**Q116 Stephen Barclay:** But we have already heard that no decisions were being taken on that because of the lack of an SR and all the rest of it.

**Sir Bill Jeffrey:** One of the reasons for the small reduction, which you have noted in these figures, is actually a wider consideration, which is that, against the prospect of the Army returning from Germany, there is an argument for keeping some defence sites available for purposes of basing them upon their return. That is one factor. The other, which has come

out of the conversation, is that the RAF has a large stake in this. The way in which the budget arrangements work these days, if the senior managers of the RAF and commanders can find ways of reducing the size of their estate, it is very much in their interest to do so.

**Q117 Ian Swales:** Can I just go a bit further on this? I think although it is specific, it perhaps draws out some wider lessons. We all know from civilian airfields that there is no limit to how many aircraft can be serviced, landed, taken off and so on, even on quite small airfields. I certainly do not buy the argument that you must have a separate airfield for every type of plane. I can understand there might be strategic reasons why you might do that and so on, but you said that it is not in the RAF's interest to have a load of airfields, because they must bear the cost. Do they really bear the economic cost of having all that land? How many of the staff on those airfields do they actually pay for? Or are they paid for perhaps through the estate's budget? In other words, if the RAF have a lot of financial pressure to do with having many airfields, would they make different decisions?

**Ursula Brennan:** Could I respond to that? I come back to the point that the decision about closure of something like an airfield will emerge from a variety of sources, as for almost any major decision of the sort; there will be a variety of people with an interest in it. The primary interest will be the RAF, who will be looking at, as we have been across the whole of Defence, trying to reduce down to a smaller number of sites because that is a more efficient way of managing our business. So one of the things that they look at is the point at which it is sensible to be able to get out of this business; can they bring these things together? It will be to do with contracting—a whole raft of things—and training. This will determine how the RAF will be approaching this prospect.

From Defence Estates' perspective, a team of people who are not simply people taking the decision of wanting to close an airfield are looking at our major or large sites and having a dialogue with the RAF, asking if it is possible to get out of a particular RAF base. There is then a discussion. If there is a significant amount of money there, and Defence Estates think there might conceivably be scope to dispose of that site, and we do not need to use it to bring anybody back from Germany, then if there was a feeling that someone was dragging their feet, for argument's sake, the RAF in this case, that is the kind of issue that would be exposed to the Defence Board through the Defence Estates route.

In other words, the questions about the economic driver are something that is within the responsibilities of Defence Estates. The NAO Report brings out clearly that in relation to estates, we have been on a journey, where the primary concern around the defence estate has tended to be quality in recent years and operational effectiveness. That is where a lot of Defence Estates' attention has been directed, as you might imagine, particularly in the context of the SDSR. To improve our ability to manage these things, Defence Estates are developing asset management tools, which will enable them to be sharper on that



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driver about the economic side of it. However, I can assure you in the context of the SDSR, we have worked our way through every single one of the areas of estate that is worth more than, I think, £5 million, and satisfied ourselves that we are being as aggressive as we can about divestment where that is sensible.

**Q118 Chair:** Using the questions on figure 13?

**Ursula Brennan:** Predominantly we have been looking at them in terms of what we might be able to get in terms of if we were able to move out of the estate and sell it. But yes, clearly in that context, we have looked at what remediation we would have to put in if we were going to be able to sell, because a lot of these sites are quite polluted and damaged. Therefore there is investment that has to be undertaken, but certainly in relation to those kinds of questions.

**Sir Bill Jeffrey:** As I said earlier, this is about context. We are doing this better than we were before but not as well as we could. The prescriptions in this Report are ones we will follow.

**Q119 Austin Mitchell:** I just want to prolong Bill's last appearance. You said that in the defence estate you have 1.5% of the total land mass of the UK. According to figure 9 on page 20, you are only considering disposal of 2% of that enormous estate. It looks to me as though the Crichel Down mentality still lingers in the Department of Defence: what I bomb, I hold.

**Sir Bill Jeffrey:** I do not think so. The significant thing about the defence estate is that a huge proportion of it is the training estate. It is something like 78% according to the Report. I think that is the right figure. It has relatively low asset value. It is typically in remote parts of the country where there is no other alternative use. Sometimes it is in national parks, and one of the things we do there is fulfil our corporate citizen responsibilities in relation to national parks, and I believe we do so rather well. We do our best to ensure that these areas are well used. The prospect, particularly given how much we rely on training people who are about to go into theatre, divesting ourselves of large parts of the country, where frankly there is not much demand and which we would need to clean up mightily and spend a lot of money before we started to sell them it. We must put that in context. We will divest ourselves of as much as we can. All the economic and other pressures point in that direction. We are not that apologetic for having concentrated on quality and support for operations in the last few years, because the really important thing has been that our young men and women have had the chance to be well trained before we put them into theatre. That is another context in which we tend to be criticised for not doing that well.

**Q120 Austin Mitchell:** When I went on the Armed Forces scheme, I had a fantastic time. The fleet set out and we were attacked. I did not realise this, but it was explained to me that the attackers, who looked like RAF planes as far as I could see, were all on contract. They were contractors. The attack lasted for a limited period, and then they said, "Contract's over now," and

they all buggered off. They must have flown from an RAF field. Are the contractors charged for that?

**Sir Bill Jeffrey:** It depends on the relationship. If we are employing them, then the cost will eventually fall to us anyway. I do not know the individual case.

**Ursula Brennan:** It depends on what kind of aircraft they were that were doing the attacking and what kind of contract it was.

**Austin Mitchell:** I was looking down.

**Ursula Brennan:** Some of our contracts involve contractors on our sites. The contract includes the cost of them occupying our premises or using our facilities.

**Q121 Matthew Hancock:** Moving onto the office estate, I noticed that one of the things that Mrs Brennan said is that you reduced down the number of estates. Then you said that you wanted in the context of the RAF, an aggressive reduction, but I noticed that from a series of Parliamentary questions, the average office space in MoD is 13.1 metres squared, which compares to 12.7 in DEFRA, 12.35 in the Northern Ireland office, 12.1 in Home Office and 9 in the tribunal service. You have a larger area per employee than other Departments, and what's more, the number of offices over 500 square metre has increased from 21 to 23. At the time that you are losing all these civilian staff, why have you not been as effective as other Departments in making good use of your office space and why has the number of units increased?

**Ursula Brennan:** In relation to our office space, we have had a strategy around reducing it in central London and reducing the number of buildings so it is down to one. Our intention is to get down to being simply in the main building in Whitehall. We are close to getting there.

**Q122 Matthew Hancock:** And are you improving the utilisation of that space fit for purpose?

**Ursula Brennan:** We are improving utilisation of that space by a restacking process, as it is called, in which we move people out, put more in and move them down again. However, there is a constraint. The design of the building, the air conditioning and so on limit the number of people you can put in the building. We have a PFI—

**Q123 Mr Bacon:** Are you talking about the main MoD building?

**Ursula Brennan:** Yes. We have a PFI contract, which specifies that there is a limit to the number of people we can place in that building.

**Q124 Matthew Hancock:** I do not want to get into that catastrophic PFI decision. That may well be the case, but according to the answers provided to me, the total office space has increased from 2007/8 to 2008/9 from 259,796 square metres to 272,683. You have increased the amount of office space while the number of civilians in the MoD has fallen.

**Sir Bill Jeffrey:** I cannot immediately explain the increase in the short time we have with the Committee, but I would draw your attention to paragraph 1.27 of the NAO's report. They quote an OGC report on the state of the estate, which shows that our total property cost score exceeded the

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benchmark average of 100. We performed well compared with other Departments. There is a figure—

**David Olney:** The fifth lowest cost per square metre.

**Sir Bill Jeffrey:** Yes, out of 16 Departments, so I think in this area there is some evidence we are doing well. I don't recognise the figures you gave.

**Q125 Matthew Hancock:** They came from Gerald Howarth.

**Sir Bill Jeffrey:** I'm sure they're accurate.

**Ursula Brennan:** I am sure they are accurate. Perhaps something else has been added to our baseline, groups that were not in the list previously, because it does not sound consistent with what has actually been happening to our buildings.

**Q126 Stephen Barclay:** Can I take you to page 13, paragraph 1.12. The Report says the Defence Estates Development Plan gives insufficient attention to efficiency and cost reduction, and it goes on to say no targets are set such as for cost and size of the estate. No milestone is set to assess progress and trends. There are no supporting measures such as data, value cost, personnel and utilisation, which was the point I was trying to make before. Why is that the case?

**Sir Bill Jeffrey:** That is what I was fessing up to in my earlier answers. As I have said, I think we have made quite a bit of progress in this area, and there are some unvarnished favourable comments elsewhere in the Report about what Defence Estates has done in recent years. There are criticisms that we do not have enough of the right type of information at the centre. We do not have an information-driven categorisation of the estate and detailed plans for reducing costs. I think they are well made and we are acting on them through the study that is being undertaken now and strategic management activity.

**Q127 Chair:** There have been a number of reports on the management of the estate by the MoD. This is the first I have had to deal with, but looking back, to try and improve your management of the estate, you introduced an estate performance measurement system three years ago. You have now decided to abandon it, I do not know why. You have suddenly talked today about a new asset management tool. I do not know what that means. Presumably that is to replace this system that you have abandoned. How will it be different? How long will it be until you get that in place so you can make some sensible decisions across the piece rather than this piecemeal approach you have to estate management at present?

**David Olney:** The EPMS was an attempt to regrade all the performance metrics of running our contracts in one single source document to give a picture of how well we were managing the estate. To give examples, we could do metrics on health and safety, sustainability, energy use, delivery of projects, reactive maintenance, help desks, etc. As we collected data and took experience in this—and I should add at this point that when we started to develop it we went out again to industry and other Departments and could not find a single similar system or systems which did such a thing—we engaged the services of the Building Research Establishment to try and help us; as you say,

the NAO previously commented on this in previous reports. We took lots of professional advice in building this system, but as we began to fill it with data we realised we were starting to spend more time trying to understand what the data was telling us than actually using it to manage the estate. Therefore we have introduced a simplified—

**Q128 Chair:** How long did it take you to get to that point?

**David Olney:** About two years.

**Q129 Mr Bacon:** How much did you spend on EPMS in total before you canned it?

**David Olney:** I do not have those figures with me to hand. It was not a large sum of money.

**Sir Bill Jeffrey:** We could try to provide those figures.

**Q130 Mr Bacon:** It was basically a database?

**David Olney:** Yes. We have utilised those lessons learned to build our new system, which is a very much simplified system. We are confident as we collect the data, and we will have a second quarter's data by Christmas, that we should have a system which we believe will have had two quarters' data, as we only started it as the NAO Report says, earlier this year, to assess how well we are managing the estate. That is the first piece.

The second system you mentioned, asset management, is to address the points that Sir Bill and the Report mention, which are about utilisation of our estate—collecting good utilisation and asset data on our estate so that we can make, as the Report says, even better and more informed decisions about disposal and utilisation.

**Q131 Chair:** And when will that be in place?

**David Olney:** We are currently doing the study and we will have the study Report by Christmas of this year, with recommendations of how we take it in the future.

**Q132 Chair:** When could we as a Committee know that you know your utilisation of your estates?

**David Olney:** Gradually over the coming year.

**Q133 Chair:** So by autumn of next year, 2011, you will know on all your sites the intensity of utilisation?

**David Olney:** That will take longer. Until we see the final report and the scale of the data collection exercise, it is rather difficult to put a date on it.

**Q134 Chair:** This is so simple, I cannot believe it.

**Ursula Brennan:** I think the experience with the estate performance management system demonstrated that this was not simple. The experience when we were seeking to create the estate performance management system, when we went out and looked at what other people were doing, showed that it was not simple. One reason why—and this came out in the hearing on the earlier report—is that information in Defence, divided between the three services and the components that make up Defence, is divided into many systems. Collecting that information together and being able to take action on it is not a simple

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matter. We are not waiting until we have a system that enables us to do that—

**Q135 Mr Bacon:** Mrs Brennan, this is extraordinary. Figure 15 has five things in it: operational importance, potential resale value, running cost, utilisation data and condition. For the column “Are the data comprehensive?”, there is a red flag indicating no for every single one. If you were a very large private sector organisation, say Shell or BP, with operations in 120 countries, they would expect to be able to answer that question for all five relatively quickly if they could not do it already. The Chief Executive globally of the business would say we need answers to those questions.

I expect that there are reasonable answers, accepting that for the reasonable sale value it will be a parameter, because you will have to say for a particular site, yes it needs remediation work or it would depend on whether it had planning or not. Obviously agricultural land or an ex-base will be one thing, if we know it is an area where we know there will be a lot of housing expansion it is another. You can put some square brackets in there.

If the said Chief Executive said that he wanted this information on his desk within 12 weeks, it would be done. We all know that it would be done. Here we are near the end of 2010—the financial management initiative in the Treasury started in 1982. The Next Steps Initiative to have executive agencies, in which the MoD has played a role, as much of it is run by executive agencies of one kind or another, has been going since the late 80s and was fully in train by the mid 90s. Here we are, 30 years later, and you are telling us you are not able to answer these questions and it is too difficult. It is not good enough, to be perfectly honest.

**Ursula Brennan:** I think what I was attempting to say is that in relation to this sort of information about our sites, bearing in mind—

**Q136 Mr Bacon:** It is basic information. Point at that site—how much does it cost to run it? I do not know if you read Kate Jenkins’ book on Whitehall. She says in there that the question about how much it costs was often met with a blank stare. She was of course the person who drove through the Next Steps Initiative. This was 15 to 20 years ago. Here we are, still getting blank stares.

**David Olney:** In a number of cases we have that data but as the Report said, it is collected locally. What we don’t have, and you’ve made the point, is a system—

**Q137 Mr Bacon:** We have e-mail; we have telephones. You have 3,500 members of staff whose job it is to ensure that you, at the top of this organisation, have this information centrally. What is Defence Estates for if it is not able to advise the people at the top, including Sir Bill and the finance function under Mr Thompson and Ministers, of what is going on?

**Ursula Brennan:** I was trying to make the point that, with the diversity of estates that we have and the number of estates and locations we have, and the path we have been on in terms of moving from all of this

being run and managed locally within the three services and the other components of Defence, we have moved to having estate strategy information available, brought together with plans for our estate for the first time. The next step was to take the top 500 or so sites—

**Chair:** We have to go and vote, but we will come back. Honestly, I must say to you Mrs Brennan that sort of waffle answer does not work on us.

**Q138 Matthew Hancock:** Before we go, when are those red lights going to be green?

**Chair:** They do not know.

**Matthew Hancock:** Page 25, figure 15. This is about whether you have the information to manage what you are supposed to be managing and it is clear that you need that information. When will that be sorted?

**Ursula Brennan:** Collecting the data available as described centrally and comprehensively cannot be done until we are able to invest in an asset management system.

**Q139 Chair:** But you have just wasted two years on one asset management tool.

**Ursula Brennan:** Forgive me, that was not an asset management system, that was a contract management system.

**Q140 Matthew Hancock:** Clearly you need this sort of information to be able to run an organisation and add value—when will it be available?

**Ursula Brennan:** We have this information with regards to the most valuable parts of our estate already. We have that centrally already; we do not have it for our entire estate of over 4,000 sites. We will not have that until we have developed the asset management system.

**Q141 Mr Bacon:** You could fit it all on one spreadsheet and at the end there would be two parameters, rather like the £6 billion and £3 billion that Sir Bill and I have discussed before. There will be a range of things for the potential value line but you can get it all on one spreadsheet to a degree of tolerability and then improve it. You can put a few bright graduates on it and spend a few hundred of thousands of pounds and have quite a sensible answer in six months.

**Ursula Brennan:** Can I explain the question about the number of offices? There was a change in the categorisation by OGC about office space which explains the variation. Can we give you a written explanation? The number went up because the terms on which we were measuring them increased.

**Q142 Chair:** Thank you for that, but can we just press you on this issue of a date, an ambition, an aim, a time by which you will have proper asset management information to enable you to take the necessary decisions to ensure that you are dealing with your estate efficiently?

**Ursula Brennan:** Figure 15 gives us a set of traffic lights for data in terms of whether they are collected centrally or locally and are comprehensive and so on. Our ambition with the asset management system is to

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populate that, starting with the value of the estate that is most important—our largest estate, our most valuable estate, and so on. We will not be able to have a comprehensive answer across all the 4,000 elements of our estate and indeed it has tended not to be a priority—

**Q143 Mr Bacon:** Do you mean at all?

**Ursula Brennan:** No, not at all. If you take for example the submarine site at Faslane, establishing what we would receive for selling that has not been a top priority because the notion of selling it and recreating that activity elsewhere—the cost involved in remediating it, the likely value of selling it, the cost of identifying a place where you could put nuclear submarines—has simply not been a top priority for our energy in terms of working out the utilisation and the value of the estate. Rather than take a completist approach in that way, we have looked at the estate from a development perspective in terms of the balance between the value to us and the value we could make from selling it, and to approach our analysis by getting more information on the top few hundred elements of our estate and to work out from there rather than starting with an attempt to get a comprehensive asset management approach, where we would have to ask a lot of questions, many of which would not be of value.

**Q144 Mr Bacon:** I understand exactly where you are coming from. Your use of the word “completist” puts it very well. Surely an alternative approach, which might end up giving you more information and surprising you because you would unearth things you did not expect to find, would be to take, if you like, a globalist approach, and then improve the quality of it as you went on. I do not understand how you can begin to run this organisation. You have 3,000 employees in a thing called the defence estate and it is not obvious to me that you can answer the question of what is the right size estate. How can you get to be able to answer such a question unless you have some sort of approximate answer so that all these five questions have green flags against them rather than red ones? If the information is held locally, why do you not get them to send it in?

**Ursula Brennan:** That would be helpful.

**Q145 Mrs McGuire:** Could you give us a date as to when you could answer four of the questions, recognising that you may have an issue about potential site value? When would we be at a point when at least we would have that and we could have an explanation as to why we cannot complete on the first question.

**Ursula Brennan:** Yes.

**David Olney:** For our top core sites, the 500, we could do that within in a year.

**Q146 Mr Bacon:** What? I find this really, really unimpressive. I would have thought that you would be able to answer the running cost line now, the third line along. I would have guessed, or hoped, that you would be able to answer that question for every single site now. Is that not the case?

**David Olney:** We can at a local level identify the running cost of every single site. We then need to have a system that could bring it together.

**Q147 Mr Bacon:** You could put it on one spreadsheet. I keep on saying. I was not being facetious. The civil service famously employs some of the brightest people in the country. Get people with two or three years’ experience, put them in a unit and say, “Right boys,”—or girls—“you have six months,”—or four months—“get to it, and don’t spend too much money either while you are about it.” That would come up with some sort of approximate answer to the 80% right—that is directionally right—and then improve on it. Surely that is the way to do it? Is it not? What am I missing?

**Ursula Brennan:** In relation to some of these questions, for example, the definition of running costs, one of our problems is that a lot of information is held locally and it is held to answer the questions that are predominately important locally. We could go out to everybody locally and ask them to report back running cost information against a given set of parameters. In the current pressures on the Department, I simply do pause because one of the things that we try to do as administrators within the Department is not to ask questions that we do not believe will drive us to make a serious decision. Because we know what the defence need of the estate is, and because we know the kind of remediation that would be necessary, asking that question of everybody is not something we have thought useful. In conjunction with the Treasury, we have been doing a lot of analysis around the sites where serious scrutiny of these kinds of questions is likely to yield a very valuable answer. But we really do not want to spend time capturing a lot of information that people have locally, getting them to change it to be able to bring it to the centre, and then, in the end, not being able to reply positively to the question: “are you going to make any different decision about the submarine base at Faslane? No, we are not.”

**Q148 Chair:** So on what basis, given the financial pressures, will you now take the decisions to take costs out of your estate?

**Ursula Brennan:** The basis on which we are analysing our estate in relation to taking costs out of it is in terms of looking at the top sites in terms of value and the likelihood of being able to dispose of them.

**Q149 Chair:** But if you have information on something you call the top sites in value that assumes you know the value of all your sites. How on earth do you get your 200 top sites without knowing the value of all of them?

**David Olney:** Because we have professional chartered surveyors who, without doing the detailed Red Book value, can have an opinion of what the top value sites are on the market—

**Q150 Chair:** How do you know they have looked at the right ones?

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**David Olney:** We would not look at those, for argument's sake, with a single radar head on site. We would not look at single elements where it's agricultural value of sites, so we can dismiss large numbers by simply looking at the estate and saying that the airfield at Kinloss is very unlikely to attract much value compared with a barrack block in the south-east. So we can very quickly get to what we think are the top value sites.

**Q151 Mrs McGuire:** If there was potential for local commercial development—I know this because I had an MoD site right in the middle of Stirling—that would be the sort of site that you would flag up?

**David Olney:** Yes, we would.

**Ursula Brennan:** This is how the Estates Development Plan was developed, so that we look at places we are vacating: are they inside the wire or outside the wire? When we vacate space inside the wire, for security reasons it is extraordinarily difficult to divest it. Therefore we look at that and, having made a decision about the security, we do not pursue it much further unless we are confident that we can get everybody out of the site and dispose of the whole of it. It is those kinds of 80:20 judgments that we have been making, which is the reason why we are not able to give you a lot of this data for all 4,000 sites.

**Q152 Mr Bacon:** May I return to the issue of the MoD main building? Mr Hancock said earlier that he did not want to get into what he described as the disastrous PFI contract, but I understood you to say that although you were hoping eventually to restack everybody pretty much into the MoD main building only, one of the constraints was that the PFI contract did not allow more than a certain number of people because otherwise the air-conditioning would not be good enough.

**Ursula Brennan:** Sorry, I would not want to elide those two things together. The MoD main building is an old building, and it has constraints, such as where the pillars are, in terms of how you can physically stack people into it. It does also have constraints in terms of its heating system, and we have contracted for support services for a given number of people within the building. So if we wished to increase the number of people in the building and if we were able to do that because of the physical and security constraints, we would bump up against the need to renegotiate that contract.

**Q153 Mr Bacon:** This contract is already costing £746 million at the present prices when it was contracted. Can you remind us, Sir Bill, over how many years the annual unitary charges are made?

**Sir Bill Jeffrey:** I cannot offhand.

**Q154 Mr Bacon:** Nineteen years is the number in my head, but I am not sure if it's accurate.

**Sir Bill Jeffrey:** I am not certain.

**Q155 Mr Bacon:** But I do know, because I remember getting a letter from your office at the time, that £2.514 billion was the total sum of the annual unitary charge payments over the life of the contract, however

the years is was over. It is an awful amount of money, and you are spending it for a building that does not have adequate air-conditioning.

**Ursula Brennan:** I did not say it had inadequate air-conditioning. I simply said that, as is often the case with elderly buildings, there is a limit to what you can do in terms of investment in air-conditioning and heating, and that kind of things, and there is a limit to what you can do in terms of where the pillars are and the structures.

**Q156 Mr Bacon:** I understand pillars, although frankly—I watched it happen—the building was completely gutted. You could have put anything in there if you had wanted to.

**Ursula Brennan:** You can put anything in, but the building still has physical constraints in terms of how many people you can get inside it.

**Q157 Mr Bacon:** I do not understand you correctly. What is the point that you are making about the air-conditioning?

**Ursula Brennan:** I am simply making the point that, in relation to the square metres that people occupy, when we let that contract, I am sure that the average number of square metres that people were expected to have was larger than the standard that we operate against now. In order to get more people into the MoD main building, we must bear in mind the charge we pay—the unitary charge per number of people in the building—to the contractor, and also some constraints around the building, including the heating and air-conditioning and so on.

**Q158 Mr Bacon:** If you put more people in, you would have to pay more per person because of the air-conditioning?

**Ursula Brennan:** No, not because of the air-conditioning. These are two separate factors. The physical status of the building constrains the number of people, as any building does—

**Mr Bacon:** Yes, obviously.

**Ursula Brennan:** There is also in this particular instance the fact that we have contracted for a particular number of occupants for that building.

**Q159 Mr Bacon:** Right. So in other words you had a bad contract that does not give you the flexibility you need.

**Ursula Brennan:** Well, I think the point that I was making is that when the contract was let, the assumption about the numbers who would be in that building was smaller than the space standards would be now.

**Q160 Mr Bacon:** Surely the whole point about PFI contracts is that you need to build in flexibility?

**Ursula Brennan:** We have had flexibility. We are putting a lot more people in.

**Q161 Mr Bacon:** You make it sound like it is a constraint because you would have to pay more.

**Ursula Brennan:** We would have to renegotiate the contract if we wanted to put more people in.

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**Q162 Mr Bacon:** In that case it was not flexible enough in the first place.

**Ursula Brennan:** With any contract, you buy a certain amount of flexibility—

**Mr Bacon:** It sounds to me like Mr Hancock's description was probably an accurate one.

**Sir Bill Jeffrey:** Whether it is a good contract or not depends a bit on what its terms are. I do not think that it is that surprising that if we choose to stack more people into the building, we need to look at what the contractual implications of that are. What this goes back to, in the spirit of the report, is that in the last years we have been trying rather doggedly to scale down our holdings in London, and subject to getting the remaining people into the main building, we look like being successful.

**Q163 Mr Bacon:** May I briefly go back to the question about collecting the data? Mrs Brennan, you sounded like you were saying that one of the issues is that it would be difficult to justify collecting all of this data given the burden locally. But you are talking about assets of probably £20 billion. How can you say it will be difficult to justify? I would have thought the opposite would be true: that it is extremely difficult not to justify having a full picture of such an enormous set of assets.

**Ursula Brennan:** I think that the point that I was trying to make is that in terms of collecting information, one of the things that we have been seeking to do in Defence and across Government as a whole is to streamline the extent to which we ask questions on which we are not expecting to take action, and in relation to—

**Q164 Mr Bacon:** Hang on. You phrased that in a very good way, because we have just established that what you are expecting might change. You were expecting to put x number of people into the MoD building, now you are discovering it is x plus 2 or x plus 3 because your assumptions have changed.

**Ursula Brennan:** Indeed.

**Q165 Mr Bacon:** Therefore it is quite possible that what you are expecting to do about the 4,000 sites that you have may change. If you have full information à la figure 15 about those sites, you will be in a better position to make those decisions, including changing them, than if you do not. This is so obvious. I can't understand what the problem is. You make it sound like you do not want to have full information.

**Sir Bill Jeffrey:** The point that is being made here is about materiality. I do not have the figures at my fingertips, but I would hazard that our highest value properties, for which we do have good central information, account for the overwhelming majority of the value of the estate.

**Q166 Mr Bacon:** Of the £20 billion?

**Sir Bill Jeffrey:** Yes.

**Q167 Mr Bacon:** What proportion?

**Sir Bill Jeffrey:** I do not know offhand.

**Q168 Mr Bacon:** I will not ask you to sign your name in blood but, within a ballpark figure, a billion either way, roughly. You have just made an assertion that it will account for the overwhelming majority of it. Is it 13? Is it 12? Is it 17? Is it 19.9? Roughly. What?

**Sir Bill Jeffrey:** We could try to check that figure. All I am saying is—

**Mr Bacon:** You made an assertion suggesting that you know it. "I think it would be the overwhelming majority," you said.

**Q169 Chair:** Does Mr. Olney know, as Head of the Department.

**David Olney:** We do not know the market value of the top 200. We have a view as to what the top 200 are and we have a market value for the 200 sites, recognising that the £20 billion is not the market value of the estate; it is the depreciated cost value of the estate.

**Q170 Stephen Barclay:** Do you have a market value of RAF bases?

**David Olney:** We would have a market value of some RAF bases. We may not have a market value of RAF Honington or we might not have a radar head that is still an RAF base.

**Q171 Stephen Barclay:** But in 2006, there was an RAF base review, and that base review did not include the actual valuation of the sites.

**David Olney:** It may well have done in 2006, but as the Committee is well aware, the property market has changed immeasurably since 2006 and that market value would have to be updated.

**Q172 Stephen Barclay:** What was the output of the RAF base review, given there was no or only a modest change in terms of acreage? What was the output of the 2006 RAF base review?

**Ursula Brennan:** I assume that was a review conducted by the RAF and from an estates perspective we would not know.

**Q173 Stephen Barclay:** To the accountable officer surely, so what was it for?

**Sir Bill Jeffrey:** It is, but the point that I was about to make, at the risk of provoking Mr. Bacon's ire, is that all organisations operating on the scale that we do with very large entities within them, like the RAF, have to make a judgment about how much to hold at the centre and how much to leave within the big operating businesses.

**Q174 Mr Bacon:** Sir Bill, as if you would provoke my ire. But surely to goodness, it is not beyond the scope of—

**Sir Bill Jeffrey:** The RAF is a substantial organisation.

**Q175 Mr Bacon:** Of course it is. I am told that at RAF Marham there are some 10,000 people. It was a very impressive facility when I went there. But Mr Olney, who is responsible for all of this, presumably knows the chief person in the RAF on estates matters,

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and he can ring him up, and the same must be true for the Army, the Royal Navy and the Marines.

**Sir Bill Jeffrey:** To go back to the beginning, the whole direction of our approach to this issue has been towards centralisation. If you go back to the earlier part of this decade, estates matters were all over the place. There was no central management at all. One of the things, boringly, I know, that I have tried to do with this Committee is to draw attention to those moments at which NAO reports have been favourable to the MoD. This one says at paragraph 11 that there has been a significant strengthening in the estate planning. It says in paragraph six that long-term focus previously absent from the defence estate management is to be observed. So we have made progress. We need to operate on a more centralised basis, because my answer to the question, in an MoD context, of how much you leave in the operating businesses and how much you are pulling in, is that on the whole we should be more centralist than we have been, and that is the course we are pursuing.

**Q176 Stephen Barclay:** I think that it is right that the NAO has recognised improvements from what was there before, and that is a very fair point, and an important one for us to recognise as we draw to a close. But is that centralist approach not to some extent undermined by the fact that defence estates does not even have a chief executive?

**Sir Bill Jeffrey:** I would acknowledge that there is a particular issue over that. There is likely to be a competition to fill the post soon, but I do not think that I ought to say any more than that at this stage. We have an interim Chief Executive in the shape of our Commercial Director, who is holding the role, but we have been exceptionally reliant on the Deputy who is sitting before you today, who has actually done a very good job.

**Q177 Mr Bacon:** Is it the intention that that role will be solely focused on defence estates, or are you unable to say at this stage? Or will it be double-hatted with other areas of the MoD?

**Sir Bill Jeffrey:** Our thinking at the moment, and Ursula Brennan may want to say something about this, is that as we go through the next period—the review that the Secretary of State has asked Lord Levene to do is relevant to this—we should move towards something more like a single organisation responsible for procurement, sustainment and disposal of all defence infrastructure. In the spirit of what I was saying earlier about a somewhat more centrally grouped approach to these issues, the next development is likely to be towards a wider role than the Chief Executive of defence estates has now.

**Q178 Mrs McGuire:** I never thought I would hear the words “corporate” and “social responsibility” in this context. Is there an element where the corporate responsibility, which the Permanent Secretary has clearly identified, is certainly part of the consideration now with the MoD, and will that impact in any way on some of the estates, particularly the runways and the bases in some of the more fragile areas? We have mentioned Lossiemouth, Kinloss, Benbecula—all

those areas where the value of that RAF or MoD estate has also to be taken into consideration with the Department’s corporate and social responsibility. These are fragile areas. They are not in the middle of or near towns or near valuable commercial opportunities.

**Sir Bill Jeffrey:** We can provide more information if the Committee wants more on this. Personally, I think this is an area in which we can be proud of what we have achieved because we do happen to have custodianship of some very sensitive parts of the country, for wildlife reasons, for their natural scenic beauty—

**Q179 Mrs McGuire:** For some people as well.

**Sir Bill Jeffrey:** For people as well. I think it is fair to say that our relationship both with local communities and bodies that are interested in these sites is close to exemplary. We are regarded as being very good corporate citizens when it comes to the custodianship of the land that we own.

**Q180 Chair:** Sir Bill, you have been very patient, and this will be your last appearance before this Committee. I understand there is a very good tradition that I would like to keep going which is that Permanent Secretaries are given the opportunity of their very last appearance to reflect on the process that we put you through in appearing before us, and any lessons you think we can learn from your experience of no doubt countless appearances over the last five years.

**Sir Bill Jeffrey:** Chair, they are not countless. I asked my office to check and I have probably appeared before this Committee and its predecessor about 20 times or so, including a memorable encounter with Mr Bacon on Qinetiq, which I am sure we both remember. I have only got two comments to make and I am grateful for the chance to make them. First, I warmly welcome the approach that the new Committee has taken to its work. I have believed throughout that this Committee should see Permanent Secretaries in particular as its allies. When we get behind the individual cases of things that have gone wrong and in some cases badly wrong, what we share is a desire to improve value for money and the way in which big systems like MoD’s work. I think the fact that this Committee has chosen, if I can put it colourfully, not to treat hearings as a sort of blood sport but to see what common ground we can find, is extremely valuable because I have personally have always felt that in trying to improve how the MoD works, this Committee is an ally rather than a hostile force. Secondly, the MoD sometimes gets a very bad press. Sometimes it is justified, but a lot of the time it is not. It is very good to have a chance to publicly say that in amongst all the pressures that we discussed earlier in this hearing, we have some absolutely splendid staff, some in uniform, some not, who serve the country proud, and it is a good chance to say so.

**Q181 Chair:** Well, thank you very much for that. Richard Bacon wanted me to ask you one final question: what are you going to do next?

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**Sir Bill Jeffrey:** I am tempted to say attend away European football matches!  
**Chair:** Well, we wish you all the best and thank you for your service in the Civil Service. Thank you.

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#### Written evidence from the Ministry of Defence

Question 109 (Mr Bacon): *on how many qualified surveyors work for Defence Estates*

As at 30 September 2010 there were 207 qualified surveyors within Defence Estates.

Question 129 (Mr Bacon): *How much did you spend on EPMS before you canned it?*

The Business Case costs for the software which runs Estate Performance Management System were £298,938, excluding VAT.

Questions 124–125 (Matthew Hancock): *on office space*

The increase in total office space between 2007–08 and 2008–09 reflects a net increase by two of the number of sites reported by the OGC Property Benchmarking Scheme (PBS). During this period two buildings were removed from reporting under the scheme because they did not meet the criteria for inclusion, and four were added which had been omitted from the 2007–08 reporting because the OGC did not have sufficient data for the sites or had failed to include them because of IT difficulties.

Question 141 (Mr Bacon): *on office space*

The overall space efficiency per full time equivalent member of staff currently stands at 13.1m<sup>2</sup>, as against 13.6m<sup>2</sup> last year, and is moving towards the 12m<sup>2</sup> Government space efficiency standard. 52% of our occupied space is equal or better than an equivalent private sector benchmark.

Questions 166 and 169 (Mr Bacon): *value of estates*

The £20 billion reported in the NAO's report (more accurately £19.6 billion) is the total Depreciated Replacement Cost of the estate as at 31 March 2009, and includes PFI assets and donated assets (principally in Germany). The value of the MOD owned estate at 31 March 2009 was £16.4 billion, which was calculated at £15 billion in March 2010 following the annual revaluation exercise. These values should not, however, be confused with the market value of the estate.

Earlier this year, we conducted a desk top exercise to assess the market value of those top 200 sites which were considered to have the highest potential market value. This accounted for 187,000 hectares of the estate representing some 78% of the total area of the UK MOD owned estate with a market value of £3.6 billion. This compares with a Depreciated Replacement Cost of these sites of £9.2 billion. While we do not hold the market value of the entire MOD owned estate (for the reasons discussed at the hearing), the informed assumption is that the market value of the rest of the estate against its Depreciated Replacement Cost value will be proportionally lower than for the top 200 sites.

We have previously declined to publish the list of the top 200 sites for reasons of possible commercial disadvantage.

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