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Part 4

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Confidential Filing

BSA Restructuring
Wardale Enquiry.

CIVIL SERVICEPart 1: July 1982Part 4: August 1990

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PREM 19/4033

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PRIVATISATION - IN CONFIDENCE



Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon John Gummer MP
Secretary of State for the Environment
2 Marsham Street
LONDON
SW1P 3EB

23 June 1993

Dear John

PRIVATISATION OF PSA BUILDING MANAGEMENT

I have seen a copy of your minute to the Prime Minister of 18 June.

I welcome the prospect of being able to sell the five BM businesses to reputable purchasers on terms preferable to closure, and I agree that we should seek to move rapidly to exchange of contracts as soon as we decide the preferred purchaser for each business.

I am also content that decisions on the preferred purchaser for each business should be taken by DOE, MOD and Treasury Ministers.

I am copying this letter to the Prime Minister, to other members of Cabinet, and to Sir Robin Butler.

Stephen Dorrell

STEPHEN DORRELL

COMMERCIAL IN CONFIDENCE

NAPM

GPJ

Prime Minister

PRIVATISATION OF PSA BUILDING MANAGEMENT

Following your agreement, the five PSA Building Management (BM) businesses were offered for sale on 26 January. A number of indicative offers were received, and between three and four serious bidders were shortlisted for each business. Some bidders were shortlisted for two businesses.

Final offers were received on 1 June; since then my officials have been clarifying aspects of the bids with bidders.

There appears to be a good prospect of selling the five businesses to reputable purchasers on terms preferable to closure. It would be advantageous to move quickly to exchange of contracts as soon as we have reached agreement - possibly as soon as 28 June in the case of some of the businesses. However exchanges for other businesses could be later.

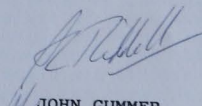
After exchange of contracts staff in each business will choose whether or not to transfer to the privatised business before the sales are completed. This process will take about two months; it is possible though unlikely that some sales might not proceed because insufficient staff choose to transfer.

There will inevitably be some publicity associated with the exchanges of contracts, which will need to be announced. However most of the sales should attract positive considerations (although the Government will retain a substantial share of contingent redundancy liabilities); none will involve negative considerations of the size of that for PSA Projects, which attracted largely misplaced criticism when sold late last year.

The European Commission have indicated that they are content with the conduct of the sales, subject to confirming the actual terms of each deal in due course.

I shall assume, if I do not hear ~~from~~ by 28 June, that neither you nor colleagues have any objection to proceeding to exchanges of contracts as soon as we are ready to do so. Because I foresee no significant political difficulties associated with the sales, I do not propose to consult colleagues generally on each deal, but will of course seek the agreement of H M Treasury and the Ministry of Defence once I am satisfied with the details of the deal.

I am copying this minute to members of the Cabinet and Sir Robin Butler.


JOHN GUMMER

(approved by the Secretary of State and signed in his absence)

18 June 1993



Minister for Local Government
and Inner Cities

Department of the Environment
2 Marsham Street
London SW1P 3EB

Telephone 071 276 3000

POLICY IN CONFIDENCE

0 2 FEB 1993

Dear Stephen,

PRIVATISATION OF PSA BUILDING MANAGEMENT

Thank you for your letter of 22 January about staff aspects for the proposed sale of the BM Businesses.

There is no difficulty in agreeing that the proposed pension scheme and Astra clause should be neither formal nor informal requirements of the sale.

We have however to be realistic and not to mislead bidders. The fact is that we are very unlikely to shortlist a bidder who does not offer a proposed pension scheme and the Astra clause. The chances of a bidder having an alternative pension scheme that is comparable to the one proposed and of then being able to persuade the Unions of this are small. And a bidder not prepared to offer the Astra clause would provoke such anxiety and suspicion among staff that we would have to assume a very poor response indeed to staff choice. As the return from the sale, possibly the viability of sale at all in some cases, depends on a reasonable number of staff being prepared to transfer with the business on sale, failure to offer the Astra clause must severely prejudice a bidder's chance of being selected. We should make this clear to bidders.

The line you suggest we take with staff would also severely prejudice our efforts to reduce staff anxieties and produce the climate more conducive to staff willingness to transfer on sale. If we are to have any chance of getting full value from these sales we need to tell staff at the outset that bidders will be advised of the importance in the selection of bidders of offering both the proposed pension scheme and the Astra clause. We can of course emphasize to staff and bidders that these features are not government requirements but simply a realistic assessment of what is needed to reassure staff in the wake of what was agreed by Tarmac in the Projects sale.



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POLICY IN CONFIDENCE

I hope therefore that you can agree to my making what I consider to be the realistic position clear to both staff and bidders. Under it bidders would still be free to put in bids on an alternative basis but they would be under no illusions as to the likely staff reaction, impact on staff choice and therefore on our assessment of the attractiveness of their offer. It is certainly the position that our advisers have strongly recommended they should take with bidders and which the management of the businesses feel reflects the stance that staff will take on staff choice.

If you still have reservations about what I am proposing, perhaps we could have a word rather than continuing this correspondence.

I am copying this letter to the Prime Minister, members of the Cabinet and to Sir Robin Butler.

Yours
JH

JOHN REDWOOD

Stephen Dorrell Esq MP
Financial Secretary
Treasury



POLICY IN CONFIDENCE



nbpm

Treasury Chambers, Parliament Street, SW1P 3AG

John Redwood Esq MP
Minister for Local Government and Inner Cities
Department of the Environment
2 Marsham Street
LONDON SW1P 3EB

22 January 1993

Dear John

PRIVATISATION OF PSA BUILDING MANAGEMENT

Thank you for your letter of 21 January about staff aspects of the proposed sale of the BM Businesses.

I am grateful to you for accepting that the proposed pension scheme and the Astra clause should not be formal requirements of the sale. However, for the same reasons, I think it is important also that they are not allowed to become informal requirements.

On the pension scheme, I am, as I said, content for advisers to offer guidance to potential bidders, but advisers should not go so far as to suggest that a bidder would not be short-listed unless they adopt the proposed pension arrangements.

Likewise, I have no objection to the advisers circulating a draft of the Astra clause to short-listed bidders indicating that these assurances were given by Tarmac to the former PSA employees who joined them from PSA Projects, but again it should be made clear this is not a condition of the sale. The preferred purchaser may, or may not, be a bidder who has decided on the Astra clause.

For these reasons, I could not agree to your telling staff that the vendor unit will do all it can with its advisers to get the proposed pension scheme and Astra clause accepted by bidders. PSAS should go no further in messages to staff than to say that the vendor unit's advisers will indicate to bidders that staff would find the adoption of the proposed pension scheme and the Astra clause reassuring, and the vendor unit will let staff know as soon as it becomes clear whether the preferred bidder will be offering them.

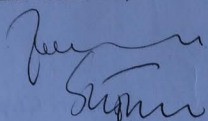
On secondment arrangements, I accept that the bidder will be constrained by the need to secure adequate continuity of service to clients, but I would ask you to accept that some bidders will be able to meet this requirement by redeploying their own staff. This should not be precluded.

fst.nb/fst/22a.01.93

POLICY IN CONFIDENCE

CIVIL SERVICE
BA MC

I am copying this letter to the Prime Minister, members of the Cabinet and to Sir Robin Butler.



STEPHEN DORRELL

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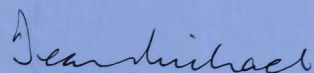
NAC

CEPO

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Michael Howard QC MP
Secretary of State for the Environment
2 Marsham Street
LONDON
SW1P 3EB

22 January 1993



PRIVATISATION OF PSA BUILDING MANAGEMENT

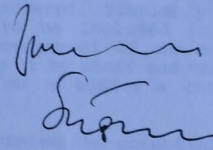
Thank you for your letters of 22 December and 15 January in which you seek agreement to launching the sale of the five PSA Building Management businesses.

I am aware that the state of readiness of some of the businesses is less than ideal and that rapid solutions to their particular difficulties are not available. However I am satisfied that the balance of advantage, though narrow, lies with your proposal to proceed with all of the sales at the earliest practicable date of 26 January. I agree that every effort should be made between now and the beginning of "due diligence" to maximise the prospect that all the businesses will be sold at an acceptable consideration.

Your letter notes that I have been in discussion with John Redwood on certain staff-related aspects and I await John's reply to my letter of 15 January. I am pleased to note that the uncertainties referred to in Malcolm Rifkind's letter of 5 January have now been resolved.

In conclusion I am content for the launch of the sale of the five PSA BM Businesses to take place on that date.

I am copying this letter to the Prime Minister, members of the Cabinet and Sir Robin Butler.



STEPHEN DORRELL

& received today



Minister for Local Government
and Inner Cities

Department of the Environment
2 Marsham Street
London SW1P 3EB

Telephone 071-276 3000

POLICY IN CONFIDENCE

21 JAN 1993

Car Stephen

PRIVATISATION OF PSA BUILDING MANAGEMENT

Thank you for your letter of 15 January about staff aspects of the proposed sale of the BM businesses.

I am grateful for your agreement to my proposals on staff choice and on secondment. On the latter it will be for the purchaser to decide how many secondees to take and for how long but the purchaser will be constrained by the need to secure adequate continuity of service to clients. Unless the purchaser is particularly successful in persuading staff to transfer there is therefore almost certain to be a need for some secondments if only for a transitional period.

I am however disappointed by your response on my proposals on pensions and the so called Astra clause. As I explained in my earlier letter, it is potentially misleading to imply to bidders that they have much discretion over the pension arrangements to be provided to staff if they wish to be shortlisted. However I accept the proposed pension scheme does not need to be made a formal requirement of the sale if the advisers can make clear to bidders the likely impact on staff willingness to transfer and therefore on the likelihood of being the successful bidder if the proposed pension scheme is not offered. Similarly it is not essential for the Astra clause to be included in the draft employee letter proposed by the government if the advisers can indicate the importance attached to it by staff and therefore the adverse impact of its omission on a bidder's chances of a successful bid.

What is important if we are to maximise the potential return to the taxpayer from the sale of these businesses is to ensure that as many staff as possible decide to transfer with businesses rather than opt for redundancy. To do this we need to start the process of reassuring and persuading staff now rather than go through the run up to exchange with staff uncertain and fearful about whether their pension and severance entitlements will be adequately secured in the sale. Arguing that staff dismissed for refusal to accept inferior severance terms would have a claim for unfair dismissal will do nothing to win hearts and minds.



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POLICY IN CONFIDENCE

In the first place staff can correctly point out that the purchaser may be able to argue if he runs into financial problems that severance entitlements need to be reduced for economic reasons and that the dismissals for failure to accept the changed terms are not therefore unfair. This is what Astra did successfully as I understand it. (Staff are not convinced by the argument that the sort of financially robust purchaser the government is committed to securing would not be able to run the 'Astra' defence to unfair dismissal claims successfully as this depends on government's judgement of the viability of the purchaser.)

Secondly even if unfair dismissal were established the maximum compensation falls far short of many staff severance entitlements and reinstatement cannot be guaranteed. The discrepancy between the levels of compensation available and average size of severance entitlement (£47,000 on average for a P&T staff member) distinguishes this case from the typical private sector case arguably adequately covered by general employment law.

Therefore I can accept that neither the proposed pension scheme nor the Astra clause be made formal conditions of sale if the advisers can make the position clear to bidders in the way you propose. As we need to maximise the likelihood of staff agreeing to transfer with the businesses on sale, which in turn should maximise the return to the taxpayer, I need to make it clear to staff that the vendor unit will do all it can, with its advisers, to get the proposed pension scheme and Astra clause accepted by bidders.

I am copying this letter to the Prime Minister, members of the Cabinet and to Sir Robin Butler.

JOHN REDWOOD

Stephen Dorrell Esq MP
Financial Secretary to The Treasury



COMMERCIAL AND POLICY IN CONFIDENCE

MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1A 2HB
Telephone 01-218 2111/3

MO 10J

20 January 1993

Dear Michael

PRIVATISATION OF PSA BUILDING MANAGEMENT

I have seen your minute of 22 December to the Prime Minister seeking agreement in principle to offering the five BM businesses for sale early in 1993, possibly as soon as the end of this month.

I am grateful to note that you intend to seek my agreement to the timing of the sale. Although I remain of the view that the transfer of PSA BM to the private sector through sale as five separate business is in the MOD's best interests in more rapidly introducing commercial methods of operation and increasing competition in this sector, I would not yet wish to be committed to launching the sale as early as the end of January.

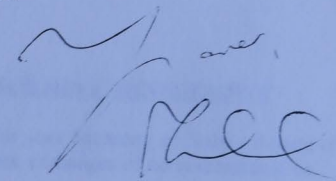
Good progress has been made in turning the forward workload into contracts of up to 5 years duration with each business but this has inevitably been complex. There are a large number of changes in hand or in prospect in the deployment of the Services and MOD civilians, involving base closures and relocation. Before the BM businesses are offered for sale, it is essential to ensure that these have been properly reflected in the forward work programme and that we do not, therefore, lay ourselves open to claims of

The Rt Hon Michael Howard QC MP
Secretary of State for the Environment

COMMERCIAL AND POLICY IN CONFIDENCE

misrepresenting the value of the workload on offer. My officials are, as you say, attempting urgently to finalise the programme but it is too soon to judge whether this can be resolved to the satisfaction of both MOD and PSA within the next week or so to meet an end of January deadline. My officials will keep closely in touch with yours with the aim of reaching agreement as soon as possible on the content and value of the forward programme and hence the earliest possible date for sale.

I am copying this letter to the Prime Minister and members of the Cabinet, and to Sir Robin Butler.

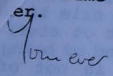


Malcolm Rifkind

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and Astra clause accepted by

the Prime Minister, members of the



JOHN REDWOOD

Stephen Dorrell Esq MP
Financial Secretary to The Treasury



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POLICY IN CONFIDENCE



10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

20 January 1993

PRIVATISATION OF PSA BUILDING MANAGEMENT

The Prime Minister was grateful for your Secretary of State's minute of 22 December. He has seen the subsequent exchanges of correspondence on this.

The Prime Minister is content that the five PSA Building Management businesses should be offered for sale straight away, and that the sales should be launched on 26 January.

I am sending copies of this letter to the Private Secretaries to all members of the Cabinet and to Melanie Leech (Cabinet Office).

(MRS. MARY FRANCIS)

Alan Riddell, Esq.
Department of the Environment

POLICY IN CONFIDENCE

POLICY IN CONFIDENCE

PRIME MINISTER

PRIVATISATION OF PSA BUILDING MANAGEMENT

Mr Howard proposes that the five PSA Building Management businesses should all be offered for sale straight away. The sales would be launched on 26 January. The alternative would be to hold two of the businesses back, because they are not in as good a state as the rest. Mr Howard concludes, however, that waiting 6 months would not materially improve them, and would be damaging to the privatisation as a whole. Treasury agree.

MOD are less confident that the businesses are ready for sale, and Mr Rifkind may argue for delay.

David Poole and I recommend that you should support a quick sale of all five businesses. We do not believe that, in the present business climate, a six month delay will help. The professional advisers support this.

Content for all five sales to be launched on 26 January?

MF.

MARY FRANCIS

18 January 1993

economic\psa.kw

POLICY IN CONFIDENCE



Treasury Chambers, Parliament Street, SW1P 3AG

John Redwood Esq MP
Minister for Local Government and Inner Cities
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

15 January 1993

Dear Minister,

PRIVATISATION OF PSA BUILDING MANAGEMENT

Thank you for your letter of 22 December about some staff issues in connection with the preparations for sale of the five PSA(BM) businesses.

I accept that BM staff should have the same right as Projects staff to choose whether to transfer with the business to the private sector.

I can also agree to your proposal to make maintenance of existing terms and conditions of staff employment at the time of sale a condition of offers to tender.

Likewise, I accept that the Project secondment arrangements should be imposed as a condition of BM sale, provided that the potential purchaser is not constrained in any way about the number of secondees which he offers to take (including, if he so chooses, taking no secondees at all).

However, I have some difficulty with your other proposals. I do not believe that the Government should impose requirements on bidders relating to pensions or the "Astra" clause.

In my view, insisting on the pension scheme as a formal requirement would not meet our need for giving bidders maximum discretion and would create an awkward precedent for other privatisations. It would be perfectly acceptable, of course, for the advisers to offer guidance to potential bidders, highlighting the problems of staff perceptions and what might be done to accommodate the difficulties if bidders so desire, although this would not be a requirement of the sale.

Likewise, for the Government to propose a draft "approved form" employee letter assuming the adoption of the Astra clause would

POLICY IN CONFIDENCE

imply greater Government support for the Astra clause than is desirable, with all the dangers this would create for a read-across to other privatisations and wider policy considerations. The Astra clause goes further than employment law, which the Government views as the correct level of response by employers in all other circumstances. Under law, staff have the right to agree changes in redundancy entitlements, and, if dismissed for refusing to agree, would have a claim for unfair dismissal.

I would not, however, have any objection to the advisers circulating a draft of the Astra clause to short listed bidders indicating that these assurances were given by Tarmac to the former PSA employees, who joined them from PSA Projects, although again it should be made clear that this is not a condition of the sale. In truth it is a material piece of information for bidders considering how to deal with the staff of this intended acquisition.

Finally, I look forward to receiving your detailed proposals for the timing of the five sales.

I am copying this letter to the Prime Minister and members of the Cabinet and to Sir Robin Butler.

Yours sincerely,

William Nye

pp STEPHEN DORRELL

(Approved by the Financial Secretary and
Signed in his absence)

POLICY IN CONFIDENCE



POLICY AND MANAGEMENT IN CONFIDENCE

2 MARSHAM STREET
LONDON SW1P 3EB
071-276 3000

My ref:

H/PSO/606/93

Your ref:

15 January 1993

The Rt Hon Norman Lamont MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
LONDON SW1

Dear Chancellor,

PRIVATISATION OF PSA BUILDING MANAGEMENT

I minuted the Prime Minister on the timing of the offers for sale of the five PSA Building Management businesses on 22 December.

Since then I have received further advice from the reporting accountants and my financial advisers on the readiness of the businesses for sale. In addition Malcolm Rifkind wrote on 5 January about the possible effects of uncertainties over the future of MoD bases.

In the light of progress and further advice since 22 December I propose that the sales should be launched on 26 January.

The prospects for sale of at least most of the BM businesses appear reasonably good. All have substantial contractually committed workload which should be attractive in the current climate. However two of them have experienced more difficulty than the others in developing their financial information systems, and there is some risk that these businesses will not be as ready as I would wish for purchasers' due diligence.

I have considered the case for delaying the sales until there can be more confidence in the businesses' readiness. To have a noticeable effect, my advisers now believe that the delay would need to be of the order of six months. However the risks associated with such a delay would be considerable. Momentum and morale - and possibly key management - would be lost. There would be a perception that the sales were in difficulty, and purchasers might be put off as a result.

I understand that officials now expect to be able to clarify the uncertainties referred to in Malcolm's letter in time to issue the Information Memoranda on 26 January. I am grateful for the MoD's cooperation in solving these potential difficulties.



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POLICY AND MANAGEMENT IN CONFIDENCE

No option is risk-free. But I believe that the balance of risk and advantage point to launching the offers this month, and making every effort over the next few weeks to ensure that the businesses are prepared as well as they can be for due diligence.

Stephen Dorrell and John Redwood are discussing details of the offers relating to staff; the outstanding issues will need to be resolved quickly in time for offers this month, but I hope this will not be a problem.

In conclusion, and subject to the Prime Minister's and other colleagues' views on my minute of 22 December, I seek your agreement, and Malcolm Rifkind's, to launching the BM sales on 26 January. To allow the logistical arrangements to be put in place I would be grateful for replies by no later than 21 January.

I am copying this letter to the Prime Minister, Malcolm Rifkind and Sir Robin Butler.

Yours sincerely

M Howard

MICHAEL HOWARD
(Agreed by the Secretary of State
and signed in his absence)



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COMMERCIAL AND POLICY IN CONFIDENCE

c- P/O



MINISTRY OF DEFENCE
WHITEHALL LONDON SW1A 2HB
Telephone 071-21 821111/2/3

SECRETARY OF STATE

MO 10J

5 January 1993

Dear Michael

PRIVATISATION OF PSA BUILDING MANAGEMENT

I have seen your minute of 22 December to the Prime Minister seeking agreement in principle to offering the five BM businesses for sale early in 1993, possibly as soon as the end of this month.

I am grateful to note that you intend to seek my agreement to the timing of the sale. Although I remain of the view that the transfer of PSA BM to the private sector through sale as five separate business is in the MOD's best interests in more rapidly introducing commercial methods of operation and increasing competition in this sector, I would not yet wish to be committed to launching the sale as early as the end of January.

Good progress has been made in turning the forward workload into contracts of up to 5 years duration with each business but this has inevitably been complex. There are a large number of changes in hand or in prospect in the deployment of the Services and MOD civilians, involving base closures and relocation. Before the BM businesses are offered for sale, it is essential to ensure that these have been properly reflected in the forward work programme and that we do not, therefore, lay ourselves open to claims of

The Rt Hon Michael Howard QC MP
Secretary of State for the Environment

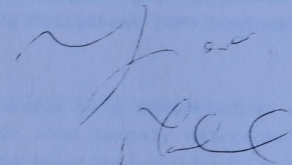
COMMERCIAL AND POLICY IN CONFIDENCE



Recycled Paper

misrepresenting the value of the workload on offer. My officials are, as you say, attempting urgently to finalise the programme but it is too soon to judge whether this can be resolved to the satisfaction of both MOD and PSA within the next week or so to meet an end of January deadline. My officials will keep closely in touch with yours with the aim of reaching agreement as soon as possible on the content and value of the forward programme and hence the earliest possible date for sale.

I am copying this letter to the Prime Minister and members of the Cabinet, and to Sir Robin Butler.



Malcolm Rifkind



PRIME MINISTER

PRIVATISATION OF PSA BUILDING MANAGEMENT

1. This minute seeks your agreement in principle to launching trade sales of the five PSA Building Management (BM) businesses in the New Year.
2. The sale of PSA Projects was successfully completed at the beginning of the month, albeit with some largely misconceived media and Opposition criticism of the negative consideration and the way the sale was handled. The sale was less financially advantageous to the Exchequer than I had hoped, as a result of the disappointingly small number of staff choosing to transfer into the privatised business.
3. John Redwood and Stephen Dorrell are exploring ways of reducing the risks for the BM sales arising from the commitment to PSA Services staff given before and after the election that they will be able to choose whether to transfer. Removing staff choice is not an option; without it sufficient staff commitment to commercialisation of the businesses and the preparations for privatisation would be unachievable.
4. There are two main factors affecting our ability to launch the BM offers for sale: the quality of financial information on the businesses and knowledge of the Ministry of Defence's future workload.
5. It would not normally be prudent to launch trade sales without being able to describe the businesses adequately and without confidence that they would be able to withstand purchasers' 'due diligence'. Considerable progress has been made in this area, and it is likely that at least three of the five businesses will

be ready to be offered for sale in January. However it is not clear in the case of one and perhaps two of the businesses whether they are yet in this state.

6. I propose to review the position again in January in the light of further advice from my reporting accountants and financial advisers. The most likely conclusions point to a simultaneous launch of all five businesses within the first quarter of 1993, although other possibilities such as offering one business at a later date cannot be wholly ruled out.

7. Offering the businesses at different times would be difficult to manage and might put the later sale(s) at substantial extra risk. On the other hand if the launch of all five were delayed beyond March we would risk significant damage to external perceptions of the sales as well as to the businesses' morale. The additional costs of the preparations for sale would also be material.

8. I therefore expect, subject to review in January, that simultaneous offers of the five businesses sometime in the first quarter of 1993 - and perhaps as soon as late January - will be the preferred course. The risks and benefits of the options will be considered further with advisers; no option will be risk-free.

9. The other matter needing resolution before the offers can proceed is the contracted workload with MoD, which currently comprises three-quarters of the businesses' workload. Contracts of up to five years have largely been agreed with MoD in line with Ministers' agreement in the summer. However I understand that there are some outstanding queries and problems to be resolved stemming from the complexities and the implications of 'Options for Change' which may result in some changes to these contracts. Officials are looking urgently into how to avoid changes which will materially affect the business plans and financial projections and consequently result in delaying the offers.

10. In conclusion I seek your agreement in principle to offering the five BM businesses for sale in the first quarter of 1993, if possible as early as late January, and propose that I should agree the detailed timing with Norman Lamont and Malcolm Rifkind

in the light of advisers' views on readiness. My office will of course liaise with yours on the details and timing of announcements.

11. I am copying this minute to members of the Cabinet and Sir Robin Butler.

Kenny Blais

M H

22 December 1992

(Approved by the Secretary of State
and signed in his absence).

CIVIL SERVICE : PSA Roobrocky Pt 4

FROM DOE MARSHAM ST

12.02.1992 17:19

NO. 7 P. 2



Minister for Local Government
and Inner Cities

Department of the Environment
2 Marsham Street
London SW1P 3EB

Telephone 071-276 3000

2 December 1992

PSA
Invitation

Dear Sir

The articles written by Mr Hencke on the sale of PSA Projects which appeared in the Guardian on 1 and 2 December contain gross inaccuracies and unpleasant invendos.

My officials and financial advisers took all necessary steps to ensure that the sale by open competition was properly and fairly conducted, ensuring that the best value available in the market place was secured for the taxpayer. I did not request that any particular company be invited to bid and I did not in any way try to influence the bidding process or the ranking of bids.

The full cost subject to the final results emerging under the terms of the contract of the sale was ~~disclosed~~ to Parliament on 25 November in a written answer to a question from David Evans. The article in yesterday's Guardian in an attempt to impinge my integrity, my officials' integrity and the integrity of the bidding process ignores the details set out in that statement. In particular, the article linked the sale process with discussions between MOD and Tarmac over costs relating to Trident construction projects; these discussions were kept separate from negotiations over the price for PSA Projects. Any contractor or consultant buying PSA was likely to have other contractual relationships with government, and none were given any indication that claims or other disputes would be treated differently if they bought PSA. The contracts referred to in the article then were deliberately excluded from the sale to avoid any conflict of interest!

I find it quite extraordinary that your paper should allege that independent civil servants should wish to favour one company over another because it had given to Conservative party funds. (I see no reason why they should and know that they did not.)

I did not sanction meetings between officials and leading construction companies to persuade them to take over the PSA. I am advised that quite properly officials did meet Tarmac over dinner once it had been decided to proceed to final contract with Tarmac, and once the other bidders had been notified of this. This is, I assume, the dinner you mention in the last paragraph of your article of 2 December.



RECYCLED PAPER

Yours faithfully

JOHN REDWOOD

The Editor
The Guardian

POLICY AND COMMERCIAL IN CONFIDENCE - NO COPIES TO BE TAKEN



10 DOWNING STREET

From the Private Secretary

28 September 1992

Dear Alan,

PSA PROJECTS PRIVATISATION

The Prime Minister was grateful for the minute of 22 September from the Secretary of State for the Environment, and is content for the proposed sale to Tarmac to proceed, on the terms outlined.

I am copying this letter to all members of the Cabinet and to Melanie Leech (Cabinet Office).

Yours ever,
William

WILLIAM CHAPMAN

Alan Riddell, Esq.,
Department of the Environment.

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sept92\25psa



DEPARTMENT OF NATIONAL HERITAGE
Horse Guards Road, London SW1P 3AL

From Hayden Phillips CB, Permanent Secretary

POLICY AND COMMERCIAL IN CONFIDENCE

Sir Geoffrey Chipperfield KCB
Chief Executive and Chairman
of PSA Board
Department of the Environment
2 Marsham Street
LONDON SW1P 3EB

25 September 1992

Hayden Phillips

PSA PROJECTS PRIVATISATION

As you know, this department was grateful to your Secretary of State for copying to us your minute to the Prime Minister of 22 September reporting on the proposed selection of a preferred purchaser for PSA Projects. Our interest in this is, as you know, almost entirely related to the British Library's St Pancras Project, on which PSA are the project managers.

The St Pancras project is, I believe, the largest civil construction project undertaken in the public sector this century. Phase 1A of the Project is well advanced but we are only due to let the tender for the Completion Phase (at an estimated cost of £92m) next Spring.

I ought to warn you that, although Phase 1A will be completed as planned, there is a danger that a new Secretary of State may need to postpone indefinitely the letting of the Completion Phase if the pro rata cuts to this Department's programmes which have been put to EDX go ahead. Otherwise we will be faced with making wide-ranging and extremely damaging cuts to other DNH programmes on the arts, the heritage, museums and galleries, and sport. You should know while we are extremely committed to seeing the British Library project through to completion, it was Mr Mellor's view that we would only be able to do so if it was not perceived to be in effect at the expense of all our other programmes.

My former Secretary of State made clear the position in the note he sent to the Chief Secretary commenting on the options for this Department's programmes which have been submitted to EDX.

cc M P 024

4 I am copying this letter to Robin Butler, Nick Monck and Alex Allan.

HAYDEN PHILLIPS

fst.nb/fst/01a.23.92

POLICY AND COMMERCIAL IN CONFIDENCE



Treasury Chambers, Parliament Street, London, SW1P 3AG

The Rt Hon Michael Howard QC MP
Secretary of State for the Environment
2 Marsham Street
London
SW1P 3EB

24 September 1992

Dear Michael

PSA PROJECTS PRIVATISATION

I have seen a copy of your minute to the Prime Minister of 22 September, and agree with its conclusion.

Although we face paying a negative consideration to achieve the privatisation of this business, we had expected this to be the case and I am satisfied both that the sale process has resulted in a satisfactory range of competitive bids from the private sector, and that the bid you have received from your selected bidder is the best offer on the table.

The only realistic alternative to sale to your selected bidder is closure of the business; and we need to assess the likely relative costs involved in these two approaches. Although you refer to a central estimate of the direct costs of closing projects of some £101 million, there is a range of estimated direct costs of closure from £89 million to £114 million. At some points on the range (ie where lower numbers of staff opt to transfer), the cost of sale to your selected bidder would be equivalent to (or conceivably somewhat worse than) the lower end of the estimated range of the direct costs of closure. At other points on the range (higher numbers of staff opting to transfer), sale to your selected bidder is clearly to be preferred to the direct costs of closure.

In order to form a considered view of the merits of sale versus closure, I think we have to add in three further ingredients.

The first extra ingredient is the fact that there will also be indirect costs of closure, which are extremely difficult to quantify, but which could prove to be substantial. Such costs would arise, in particular, from the legal claims contractors might make against the business once they see that the project

managers who are able to dispute the merits of those claims are in process of being made redundant.

The second factor concerns our wish to give Projects' staff as good and secure a future as possible. As I understand it, senior managers in the business believe that sufficient staff will opt for transfer to place the choice between sale and closure at a point on the range where sale is distinctly to be preferred on financial grounds. Clearly, there are no guarantees about the outcome of a staff consultation exercise which has not yet taken place, but I am satisfied that the balance of probability supports the case for sale to your selected bidder rather than closure.

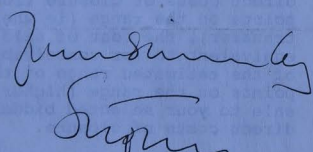
Third, I do not believe it would be helpful to our objective of privatising the five PSA Building Management businesses - and, wider, to our privatisation strategy more generally - if the sale of Projects was to be aborted at such a late stage.

I therefore agree that final negotiations with your selected bidder should now take place with a view to exchanging contracts by end September, and completing the sale - after the staff consultation exercise - by end November. I am also content with your suggestion that the outcome of these final negotiations should be reported both to Malcolm Rifkind and to me before final decisions are taken next week.

As we go forward to sale, a number of actions will call for careful handling. Officials have already identified what needs to be done, and I am satisfied with this, but these plans now need to be delivered.

Within Government, we need to be sure that we have identified all potential conflicts of interest, and have put in place appropriate safeguards. Likewise, the plans for assured future workload need to be enshrined in legal contracts prior to sale, as our lawyers have advised. Aside from work in progress under existing contracts, and from assured future workload under contracts to be signed before sale, the privatised business will compete for future orders on merit.

Copies of this letter go to the Prime Minister, to all members of Cabinet, and to Sir Robin Butler.



STEPHEN DORRELL

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PRIME MINISTER

PSA PROJECTS PRIVATISATION

You agreed earlier in the summer that work on privatising PSA Projects should go ahead and an announcement was made. DOE now wish to exchange contracts with their preferred bidder, Tarmac, by the end of the month. The net consideration for the sale will be a negative sum, because Tarmac will pick up the costs of restructuring the business and of financing substantial redundancies. Mr. Howard is, however, satisfied that good terms have been agreed and that the sale should now be concluded.

The Treasury and MOD are content.

Tarmac are in some difficulties themselves, but DOE are assured that the company is in a position to go through with the sale.

Content for me to give your approval to the sale?



MARY FRANCIS

24 September 1992

ECONOMIC\PSA.DCA

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POLICY & COMMERCIAL IN CONFIDENCE



SECRETARY OF STATE

MINISTRY OF DEFENCE
WHITEHALL LONDON SW1A 2HB
Telephone 071-21 82111/2/3

MO 21/8/5M

24th September 1992

Dear Michael

PSA PROJECTS PRIVATISATION

Thank you for your letter of 22nd September seeking, as promised, my specific agreement to proceed with the exchange of contracts for the sale of PSA Projects. I have also seen your minute to the Prime Minister.

I understand that the conditions which I placed on proceeding with the sale when I agreed to the launch in May have been met and, in particular, that we now have satisfactory financial information on the projects concerned and specifically for Trident projects. I also understand that there is agreement on arrangements to deal with conflicts of interest, and that the contract documentation is agreed (except for a few technical details) to cover both work currently with PSA Projects and guaranteed future work. These arrangements provide the safeguards which I require as PSA Projects' major client, and I am grateful for the co-operation between our Departments which has enabled us to achieve this satisfactory outcome.

I can therefore confirm that I have no objection to your exchanging contracts with Tarmac at the end of this month.

Rt Hon Michael Howard QC MP
Department of the Environment

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POLICY & COMMERCIAL IN CONFIDENCE

I am copying this letter to the Prime Minister, members of
Cabinet and to Sir Robin Butler.

Y^{rs}
Mall

Malcolm Rifkind

POLICY & COMMERCIAL IN CONFIDENCE



cc Mr [unclear]
No further copies
2 MARSHAM STREET
LONDON SW1P 3EB
071-276 3000
taken

My ref:

Your ref:

POLICY AND COMMERCIAL IN CONFIDENCE

Mrs Mary Francis
Private Secretary to
The Prime Minister
10 Downing Street
LONDON
SW1A 2AA

22 September 1992

Dear Mary

My Secretary of State has asked me to draw your attention to the very great sensitivity of the enclosed minute. It is not only a matter of commercial confidentiality. A successful sale depends on ensuring that choices are properly presented to staff when the time comes, and it would be very damaging for news of Ministers' decisions to emerge prematurely. Can I ask you therefore to ensure that the minute is given only very limited and controlled circulation.

I am copying this to the Private Secretaries of other recipients of my Secretary of State's minute.

Yours
AR

ALAN RIDDELL
Private Secretary

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PRIME MINISTER

PSA PROJECTS PRIVATISATION

As you know, PSA Projects was offered for sale in May. We have now evaluated the final offers from shortlisted bidders and, subject to your and colleagues' views, propose to select a preferred purchaser and enter into final negotiations with the aim of exchanging contracts by end September. As agreed earlier, I would not exchange without the specific agreement of Malcolm Rifkind who will want to satisfy himself that his interests, not least in relation to the Trident Works Programme, are protected. Treasury consent is also required under the legislation.

The preferred purchaser is Tarmac who are keen to enhance their design and project management skills in order to provide a single stop construction capability as part of their overall strategy as a major European construction organisation. They see Projects as forming the core part of a new professional services division. They have been pressing to buy Projects for over a year.

As expected, the net consideration will be a substantial negative sum, both to reflect the cost of restructuring Projects to make it fully commercial and competitive and because the purchaser will be taking over creditors but leaving debtors in Government. Tarmac would be taking over an organisation of up to 1800 staff (1500 permanent) which, on Projects' own projections, is expected to reduce to around 900 over the next five years. On any scenario therefore substantial redundancies will be required post sale.

Tarmac are prepared to take over the accumulated severance liabilities for up to 925 staff depending on the total number of staff prepared to transfer. The Government would reimburse

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PRIME MINISTER

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the purchaser on an agreed basis for severance payments made to staff in excess of this number transferred to Projects who are made redundant over the next five years when and if redundancy occurs. There is therefore a common interest between the purchaser, staff and the Government in Projects being successful and sustaining a large core size.

Tarmac are planning on the basis that if sufficient staff transfer the long term business could sustain in excess of 900 staff. Their bid therefore offers the real possibility of long term employment for a substantial proportion of the professional and technical staff in Projects. The majority of the permanent AEG staff (about 350 in total) can be reabsorbed within Government if not required by Tarmac in the longer term, if unwilling to transfer or for whom Tarmac see no long term future. Staff interests are further protected by the Government commitment to honour their severance liabilities at the point of sale in the event of the purchaser's bankruptcy within five years and by the cross guarantee from the Tarmac parent company to reimburse Government any such costs.

Replacement commercial contracts have been agreed between client departments and PSA Projects to protect client departments interests once PSA becomes a private sector body. The client departments affected have agreed with us ways of handling the conflicts of interest that could otherwise arise in the small number of cases where PSA Projects are managing a Tarmac group company contract on their behalf.

Subject to final negotiations, the net present value of the bid will be in the range £80-105m, the latter sum depending on how successful the business is in the five years after sale and therefore on the numbers that need to be made redundant. The negative consideration proposed, whilst substantial, would represent savings of up to £20m against the central estimate of the direct costs of closing Projects provided the minimum

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number of staff specified by the purchaser are willing to transfer permanently. The direct costs of closure have been estimated conservatively with no allowance made for the indirect cost to client departments for example of disruption, increased claims. It is significantly above the other bids we have received.

Because completion will take place before the Winter Supplementaries are approved, I shall need to seek an advance from the Contingencies Fund. If access to the Fund is approved, I propose to inform Parliament later this week. I shall of course not indicate who the preferred purchaser is at this stage, nor the amount.

While I am confident that the deal on offer from Tarmac represents the best prospects of securing long term employment for a significant proportion of the staff of Projects while protecting the taxpayer's and client departments' interests, there remains the risk that insufficient staff will be prepared to transfer with the privatised business. For both Tarmac and the government there is a minimum number below which the proposed sale would be put at risk and might have to be called off. Tarmac are confident of their ability to convince staff of the attractions of transfer. In my judgement sufficient staff will agree to the transfer once they have heard direct from Tarmac but I can give no absolute guarantee. The presentation of our decision to start will need very careful handling, and I must ask colleagues to ensure that tight control is kept within their departments on the identity of the successful bidder.

We are under very great pressure from the purchaser to exchange by the end of the month, and it is in the Government's interests to meet this timetable. If therefore colleagues have any objections to these proposals please could

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they let me know by close of play on Friday 25 September. I am sorry not to be able to give longer notice.

Copies of this minute go to all members of Cabinet and to Sir Robin Butler

HL Butler

N. MH

22 September 1992

(Agreed by the Secretary of State and signed in his absence)

1

CONFIDENCE



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FILE KK



10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

28 August 1992

Dear Naresh,

PRIVATISATION OF PSA BUILDING MANAGEMENT

The Prime Minister was grateful for Mr. Redwood's letter of 11 August. He has also seen the Chief Secretary's comments.

The Prime Minister is content that plans for this privatisation should go ahead as Mr. Redwood proposes and that he should make the announcement on the lines of the text you enclosed.

I am sending copies of this letter to the Private Secretaries to Members of the Cabinet and to Melanie Leech (Cabinet Office).

Yours,

Mary.

(MRS. MARY FRANCIS)

Naresh Rao, Esq.,
Department of the Environment.

KK

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PRIME MINISTER

PRIVATISATION OF PSA BUILDING MANAGEMENT

Mr Redwood recommends that preparations should be made to sell the PSA's five regional building management businesses by the end of the year. The Defence Secretary and the Financial Secretary agree. I attach a draft announcement.

Last year DOE were more pessimistic about the prospects for a sale: they thought it might be hard to close the business down. Mr Redwood has now been advised by Coopers and Lybrand that:

there is significant interest from potential purchasers;

the Government would save money by avoiding redundancy costs;

a successful sale depends on guaranteeing a certain amount of work for five years; but MOD could give the necessary guarantees with only a slight adjustment to their plans for market testing of PSA work.

I recommend that you agree that Mr Redwood should make an early announcement on the lines he proposes.

MF.

MARY FRANCIS

27 August 1992

A: PSA.SM

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Treasury Chambers Parliament Street SW1P 3AG

071-270 3000

Fax 071-270 5456

John Redwood Esq MP
Minister for Local Government
and Inner Cities
Department of the Environment
2 Marsham Street
LONDON SW1P 3EE

26 August 1992

Dear John

PRIVATISATION OF PSA BUILDING MANAGEMENT

In the absence of Stephen Dorrell, I can confirm that I am content to proceed with the privatisation of the 5 BM businesses, and with the terms of the draft press announcement attached to your minute to the Prime Minister of 11 August.

I am copying this letter to the Prime Minister, to members of the Cabinet and to Sir Robin Butler.

Yours ever

Michael

MICHAEL PORTILLO

POLICY IN CONFIDENCE



Minister for Local Government
and Inner Cities

POLICY IN CONFIDENCE

Prime Minister

Department of the Environment
2 Marsham Street
London SW1P 3EB

Telephone 071-276 3000

111 AUG 1992

PRIVATISATION OF PSA BUILDING MANAGEMENT

Following your agreement to his letter of 19 July 1991, Michael Heseltine announced on 24 July 1991 that, subject to satisfactory progress and market sentiment, the BM businesses would be offered for sale by the end of the following year (copy at Annex A).

Bovis Construction Ltd were subsequently appointed as contractor manager of BM from 1 November 1991, with the task of managing the preparation of BM for sale.

I have now received advice from Coopers & Lybrand on progress made towards sale, on interest amongst potential purchasers in BM, on the timetable for sale and on the relative benefits of sale compared to closure. I have also reviewed progress and sale strategy in discussion with the Ministry of Defence and H M Treasury.

This minute records my agreement with the Secretary of State for Defence and the Financial Secretary to the Treasury on the way forward in the light of Coopers' report, and seeks your agreement to the terms of an early announcement (Annex B).

Coopers confirm their earlier conclusions that sale is likely to benefit the Exchequer, BM's clients and staff compared with closure. The benefits to the Exchequer mainly relate to redundancy cost savings, but also include lower MoD maintenance costs. Coopers also advise that making offers for sale by the end of 1992 remains a desirable and at present feasible but ambitious target (slippage of a month or two cannot be ruled out). They report significant continued interest among potential purchasers. Taking account of potential purchasers' views, they recommend simultaneous but separate offers for trade sale of the five regionally-based BM businesses. However they believe that sales on acceptable terms will only be achievable if a sufficient volume of profitable work is contractually assured for up to five years beyond sale, to cover the period when new work will be built up to replace work lost through market testing. Last year



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the then Secretary of State for Defence accepted in principle that he would be prepared to slow down the rate of his Department's market testing of BM's work if that was necessary to achieve sale and was in Government's overall interest.

As most of BM's work is for the Ministry of Defence, my officials have discussed with MoD the possible scope of contracts for work after sale. These contracts will provide the legal framework for work which BM will continue to do for MoD before it is market tested in accordance with MoD's programme. Officials have drafted heads of agreement, which will be translated into specific contracts to be offered for sale with the businesses. The volumes and lengths of contract envisaged by the heads of agreement only require a slight adjustment of MoD's previously projected rate of market testing of BM's work.

As agreed with the Financial Secretary, the terms of the sale affecting BM staff - for example the guarantee of redundancy entitlements in the event of bankruptcy of the purchaser - will need to be very similar to those for the sale of PSA Projects, if sufficient good staff are to be willing to transfer to the privatised business. Without staff commitment, purchasers are unlikely to make serious offers. However I propose to review the terms of the sale in the light of experience with selling PSA Projects.

If we are to attempt to achieve offers for sale this year, officials and advisers must now commit resources to preparing the sale information. I therefore seek your agreement to making an early announcement in terms of the attached draft.

/ I am copying this minute to members of the Cabinet and Sir Robin Butler.



JOHN REDWOOD

The United Kingdom's contribution through the Community's budget would be around 17 per cent. before abatement. It is not possible to estimate at this stage what proportion of these funds would be likely to be received by United Kingdom projects or interests.

Mr. Favell: To ask the Secretary of State for the Environment what is his latest estimate of the cost of the implementation of European Community draft directive document Nos. 8149/88, 9204/89, 5807/90 and 4684/91 on habitats of wild flora and fauna to (a) the Exchequer (i) directly and (ii) channelled via the European institutions, (b) industry and (c) the British consumer.

Mr. Baldry: The extent of designations likely to be required under the proposed habitats directive is currently being assessed. However, special areas of conservation will be identified from our network of sites of special scientific interest. In certain circumstances assistance towards the costs of conservation projects could be obtained under the ACNAT regulation which has a budget of 25 mecu—£17.4 million—for each of the next two years. The United Kingdom contribution to ACNAT will depend on both the level and timing of payments and the relative shares of the programme. No significant additional cost to British industry and the consumer has been identified.

Sleeping Rough

Mr. O'Hara: To ask the Secretary of State for the Environment what plans he has for providing accommodation for single homeless people sleeping rough outside London, in response to the preliminary findings of the 1991 census.

Mr. Yeo: My Department's single homelessness initiative has made a very encouraging start in dealing with the problems of rough sleepers in central London. Taking this and the census figures into account, we are considering the possibility of extending the initiative outside central London.

Property Services Agency

Mr. Campbell-Savours: To ask the Secretary of State for the Environment how many applications from the two recent schemes for voluntary early retirement or severance within the Property Services Agency have been turned down.

Mr. Yeo: The total number of non-industrial staff VER applications that have been turned down to date is 385.

Mr. Campbell-Savours: To ask the Secretary of State for the Environment how many staff, excluding natural wastage, the Property Services Agency has declared surplus for the financial year 1991-92.

Mr. Yeo: In order to achieve its business planning projections, PSA Services currently has a target reduction of 2,500 posts in 1991-92. We expect some 700 of these to be achieved by natural wastage.

Mr. Campbell-Savours: To ask the Secretary of State for the Environment how many staff the Property Services Agency anticipates transferring to other Government Departments in the financial year 1991-92.

Mr. Yeo: PSA Services hopes to transfer some 800 staff to other Government Departments in the financial year 1991-92.

Mr. Campbell-Savours: To ask the Secretary of State for the Environment what is his policy on supporting the principle of staff within the Property Services Agency being subjected to compulsory redundancies where volunteers exist.

Mr. Yeo: The policy of PSA Services is to achieve as many as possible of the necessary staff reductions through voluntary means and to keep compulsory redundancies to the minimum. Some compulsory redundancies will be inevitable however even where volunteers exist; for example if any of the volunteers are key personnel who cannot be released or are in a grade and discipline for which PSA Services has a long-term need.

Mr. Campbell-Savours: To ask the Secretary of State for the Environment how many private sector agency staff are employed within the Property Services Agency.

Mr. Yeo: PSA Services currently employs 304 private sector agency staff.

Mr. Soley: To ask the Secretary of State for the Environment (1) pursuant to his oral answer of 10 July, *Official Report*, column 950, if it is his intention to give the redundancy pay dowry to which he referred to the purchasers of PSA Services;

(2) pursuant to his answer of 10 July, *Official Report*, column 949, whether he has any plans to use dowries other than the ones linked to redundancy payments, in cash or in kind, to enable the sale of any part of the PSA.

Sir George Young: When the PSA Services businesses are privatised, the new owners will take over assets, particularly in the form of the expertise of staff and the contracts on which they are engaged, and liabilities, particularly in the form of contractual obligations to those staff. If the value of the contingent redundancy liabilities taken on by the purchaser exceeds the value of the assets acquired, the purchaser will require a "dowry". A trust-fund is unlikely to be the most appropriate mechanism for providing such a dowry.

Mr. Patrick Thompson: To ask the Secretary of State for the Environment if he will make a statement on the future of Property Services Agency Services.

Mr. Heseltine: We remain committed to transferring the activities currently carried out by the PSA Services—PSAS—businesses to the private sector. Following consideration of the reports from my Department's advisers, Coopers and Lybrand Deloitte, we have reached the following conclusions on the options for the different PSAS businesses.

PSA International—PSAI—is not saleable as a separate organisation. We will therefore consult its clients, in particular the Ministry of Defence, about how best to phase out their reliance on PSAI and to complete the work currently underway.

Building Management is being reorganised into five regional businesses. We plan to appoint a contractor manager to carry through the restructuring and preparations necessary to make the businesses ready for sale. Providing satisfactory progress is made and the subject to market sentiment, we aim to offer the regional businesses for sale towards the end of next year.

Again subject to progress and market sentiment, we propose to offer PSA Projects for sale early next year. The necessary financial information is being drawn together to determine the best form of sale or sales.

ANNEX B

DRAFT PRESS ANNOUNCEMENT ON THE PRIVATISATION OF PSA BUILDING MANAGEMENT

The Secretary of State for the Environment today confirmed that the five PSA Building Management businesses remained on course for privatisation.

He said: "Mr Heseltine (then the Secretary of State for the Environment) announced that, subject to progress and market conditions, the five PSA Building Management businesses would be sold. Coopers & Lybrand have reviewed the sale strategy for the five BM businesses and reported to me on progress made over the last twelve months in preparing them for sale. Good progress has been made under the contractor management of Bovis Construction Ltd, and the strategy announced by Michael Heseltine a year ago remains achievable.

"I have therefore instructed my officials and financial advisers to prepare the necessary documentation with the target of being ready to offer the five BM businesses separately for trade sales at the end of the year.

"I am confident that this further stage of privatising PSA Services' work will benefit the taxpayer, staff, and PSA Building Management's clients."

Notes for editors

PSA Building Management (BM) provides property management services to a number of clients, mostly Government Departments. It employs over 9,000 staff, working in five businesses based in Bristol, Manchester, Edinburgh, Leeds and London and covering the whole of the UK.

On 24 July 1991 Mr Heseltine (then the Secretary of State for the Environment) announced that, subject to progress and market sentiment, he aimed to offer the BM businesses for sale towards the end of the following year.

On 28 October 1991 Mr Heseltine announced the appointment of Bovis Construction Ltd as contractor manager of BM, with the task of preparing the BM businesses for sale.

I would like to take this opportunity to register my concern about the disruption which could be caused to the British Library Project if PSA Projects were to close before Bovis Construction Management contract is completed. Since it is not possible to hand over a large portfolio of major projects, we simply do not have the expertise within the Department to manage projects independently of a professional project manager and would therefore have to identify a successor to PSA Projects at what is likely to be a crucial time.

I am copying this note to other members of the Cabinet and to Sir John Gifford.

John Gifford
2 June 1991

CIVIL SERVICE:
PSA Review
1/14

POLICY AND COMMERCIAL IN CONFIDENCE



n JPM
BHP
15/14

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PRIME MINISTER

BRITISH LIBRARY, ST PANCRAS: PSA PROJECT PRIVATISATION

I have seen a copy of Michael Howard's minute of 7 May in which he asks colleagues to identify any additional workload for PSA Projects.

We are currently employing PSA Projects as the project manager for the British Library Project and intend to continue doing so, at least until the completion of the work being undertaken under the Construction Management contract by Laing Management Ltd. That covers, broadly, the first stage of the building and preliminary work associated with the completion stage and we expect this work to be completed late in 1993.

However, I should record that we have not been wholly satisfied with the performance of PSA Projects in controlling the work to date, in particular with their quality assurance role. As a result, we will need to consider very seriously the continued employment of PSA Projects as project manager for the completion phase of the Project. Our other capital projects on a number of heritage properties are small by comparison; we intend that PSA Projects should handle them for the foreseeable future.

I should also like to take this opportunity to register our concern about the disruption which could be caused to the British Library Project if PSA Projects were to close before Laing's Construction Management contract is complete. Since we do not handle a large portfolio of major projects, we simply do not have the expertise within the Department to manage projects independently of a professional project manager and would therefore have to identify a successor to PSA Projects at what is likely to be a crucial time.

I am copying this minute to other members of the Cabinet and to Sir Robin Butler.

DAVID MELLOR
8 June 1992

POLICY AND COMMERCIAL IN CONFIDENCE



DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

My ref:

Your ref:

The Rt Hon Michael Howard QC MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

3 JUN 1992

Dear Michael,

PSA PROJECTS PRIVATISATION

Thank you for sending me a copy of your minute to the Prime Minister of 7 May. I note that the Prime Minister has agreed to proceed with the privatisation of PSA Projects as proposed in your minute.

You asked colleagues to identify any additional forward workload for Projects. New work of interest is likely to arise from the need for my Department to move its HQ from 2 Marsham Street which is to be demolished. I cannot say what work will be involved in setting up a new HQ until consultants have carried out a study of our future accommodation needs in London and evaluated the options. They are expected to report by September. I will need to ensure that my Department obtains best value for money in drawing up its proposals. No promises can be made to PSA Projects for whatever work is eventually required, which will need to be let by competitive tender, but we shall put PSA Projects on the tender list.

/ I am sending a copy of this letter to members of the Cabinet and to Sir Robin Butler.

*Yours etc,
jl*

JOHN MACGREGOR

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KW
cle/psa
NOT COPIED

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10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

2 June 1992

Dear Phillip,

PSA PROJECTS PRIVATISATION

The Prime Minister was most grateful for your Secretary of State's minute setting out his response to the questions raised in the Defence Secretary's minute of 20 May.

The Prime Minister has noted that your Secretary of State was able to resolve outstanding issues with the Defence Secretary, before the announcement of the sale was made last Friday.

Yours ever,
Barry

BARRY H POTTER

Phillip Ward Esq
Department of the Environment

CONFIDENTIAL



CONFIDENTIAL

PRIME MINISTER

PSA PROJECTS PRIVATISATION

You asked for clarification of the timing of the proposed sale of PSA Projects in the light of Malcolm Rifkind's minute of 20 May. Malcolm was concerned that there should be satisfactory financial data on all projects passing on sale to the private sector. He had particular concerns about the Trident related set of contracts.

His officials had some very constructive discussions with mine last week which culminated in Malcolm's agreement that the sale should be launched last Friday. This was on the basis of our recognition of his legitimate concerns about financial data and reassurance that we would not proceed to exchange of contracts without his department's explicit agreement. My officials are now working closely with his to reach a satisfactory agreement about the Trident future works. Malcolm's swift reaction enabled us to keep up the sale momentum which is so important to staff morale and purchaser sentiment.

Malcolm's minute to you also referred to the £8M additional workload promised by MOD. This is obviously helpful to the sale process and I would hope that as his department firms up its 'options for change' work programme, it will be possible to increase that sum in time to get value for it in the sale. PSA Projects is uniquely placed to take such work forward rapidly at market prices. This sale is important to the government and will make an important contribution to better service in the future. I do hope all concerned will help secure it on satisfactory terms.

N.H.

M.H.

2 June 1992

CONFIDENTIAL



10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

22 May 1992

Dear Simon,

PSA PROJECTS PRIVATISATION

The Prime Minister was grateful for your Secretary of State's minute indicating that he supported an early sale of PSA (Projects). My letter of 18 May confirmed that the Prime Minister is content for the sale to go ahead.

The Prime Minister has noted, however, your Secretary of State's view that an end May launch will be extremely tight, and, in order to avoid unnecessary mistakes, postponement to early June might be desirable. The Prime Minister would appreciate further clarification from the Environment Secretary of his plans on the timing of the proposed sale.

I am copying this letter to the Private Secretaries to members of the Cabinet and to Sonia Phippard (Cabinet Office).

Yours,

Barry

BARRY H POTTER

Simon Webb, Esq., CBE,
Ministry of Defence.

CONFIDENTIAL

QJ

Prime Minister



SECRETARY OF STATE

To note. Basically supportive
of Environment Secretary's proposals -
while noting a few weeks delay
may be desirable to avoid
mistakes.

BHP
21/5.

MO 10D

PRIME MINISTER

PSA PROJECTS PRIVATISATION

WITH B1

Michael Howard sent me a copy of his minute to you of 7th May seeking agreement to launch the sale of PSA(Projects) in the last week of May.

2. I support an early sale if proper arrangements can be agreed as that should help to ensure that a large number of my department's works projects can be completed successfully without costly disruption. To that end I have offered a future design workload, subject to the conditions Michael mentions, which would have a fee value of £8M over two years. Officials are close to an agreement on how this work will be defined and priced.

3. Nevertheless before our business with PSA(Projects) is transferred to the private sector by the sale, it is crucial that we have satisfactory information on the financial status of all the projects concerned. Otherwise the Department will be exposed to major financial risk in its dealings following the privatisation and there would be legitimate criticism of its failure to safeguard the public purse. In his minute of 13th March, Tom King made clear that provision of information would determine the timescale for the sale.

4. The requirement for this financial information has been acknowledged for over a year: but it has not yet all been provided and much of the data handed over has been in an unsatisfactory state. Fortunately there are now hopeful signs of progress. A schedule has been agreed for the provision of the financial information we need by the end of June. If this plan is adhered to,





SECRETARY OF STATE

it should all be available and agreed before we are too far down the sale path. But the flow of information is only just beginning and we shall need a little more time to be certain that the information is being provided to a standard that gives us confidence that the sale process can start. We could not agree to the final exchange of contracts until we were satisfied that the data that had been provided was adequate.

5. In particular we do not have, nor we expect until mid-June, the necessary financial information on Trident. This project is of such importance that we could not agree to its transfer unless we were satisfied that the state of the project allowed that. Officials are in discussion about the project, and I hope to let Michael have a definite view about that very soon.

6. The implications of these matters are being considered between officials. Although I should like to work for an end of May launch, that will be extremely tight; I should not want to see mistakes made which might be avoided by going for an early June date, and a small revision of dates now would be preferable to making a major change to the scope and timing of the sale once the process had begun. At this stage I could not commit myself to a precise date, but I believe we should aim to begin the sale process immediately after the Recess. I am asking my officials to work urgently with Michael's to set the earliest possible date.

7. I am copying this minute to members of the Cabinet and to Sir Robin Butler.

MR

Ministry of Defence

20 May 1992

(M R)



Recycled Paper

POLICY AND COMMERCIAL IN CONFIDENCE



Northern Ireland Office
Stormont Castle
Belfast BT4 3ST

The Rt Hon Michael Howard QC MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

WPM
BAP
20/5

19th May 1992

Dear Nicholas:

PSA PROJECTS PRIVATISATION

Thank you for sending me a copy of your minute of 7 May to the Prime Minister about the sale of PSA Projects.

I am content with your proposals in relation to the target date for the launch of the sale of Projects and the timing of the announcement.

We have not involved PSA Projects in work for the Northern Ireland Office or for Departments in Northern Ireland and I am not therefore able to identify any forward workload for them.

I am copying this to other members of the Cabinet and to Sir Robin Butler.

Yours faithfully
Michael Howard

POLICY AND COMMERCIAL IN CONFIDENCE

PM/SOFS/9275



file DS9
(A: Economic / PSA)

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

18 May 1992

PSA PROJECTS PRIVATISATION

The Prime Minister was grateful for your Secretary of State's minute of 7 May, proposing the privatisation of PSA projects and seeking agreement to a sale date later this month. The Prime Minister has also seen the minutes on this subject from the Social Security Secretary (27 April) and the Financial Secretary (12 May).

The Prime Minister is content to proceed as proposed by your Secretary of State. He has noted that a number of issues need to be resolved, for example, with the Ministry of Defence: as your Secretary of State suggests, a precise launch date needs therefore to be agreed with MOD and Treasury, and the remaining minor differences resolved.

I am copying this letter to the Private Secretaries to members of the Cabinet, to Alastair Bridges (Financial Secretary's Office) and to Sonia Phippard (Cabinet Office).

Barry H. Potter

Phillip Ward, Esq.,
Department of the Environment.



10 DOWNING STREET

File Note

These papers were not brought
to the Prime Minister's
attention before the election.
After the election new minutes
were issued which made these
obsolete.

C. Stephen.

4/5

I am copying this letter to the Prime Minister, other
members of the Cabinet and to Sir Robin Butler.

Yours ever,
Nick

VISCOUNT ULLSWATER



Employment Service - Training Agency
Health and Safety Executive - ACAS



STATEMENT IN CONFIDENCE



Minister of Employment
Street, London SW1H 9NF

071-273 5806/7
Fax 071-273 5821

Under Secretary of State
Environment

MP
Environment

26th March 1992

Will be most helpful

your minute of 9 March to the
sale of PSA Projects. I am
convinced.

an early launch of the sale of

with your proposal that part of
work programme should be committed
to PSA Projects to you on 22 July 1991
because it would put at risk,
Department Service Agency, policies and
estimates more efficiently and
Department Service Agency competitively
acts, and to change this policy
step and one which would undermine

I am sorry that we cannot be any more helpful. PSA Projects
will, of course, be invited to tender for Departmental
projects, and I hope will be in a position to win a
reasonable proportion of the work.

em.psa

POLICY AND MANAGEMENT IN CONFIDENCE



Department of Employment
Caxton House, Tothill Street, London SW1H 9NF

Telephone 071-273 5806/7
Telex 915564 Fax 071-273 5821

Parliamentary Under Secretary of State
Viscount Ullswater

The Rt Hon Michael Heseltine MP
Secretary of State for the Environment
2 Marsham Street
LONDON
SW1P 3EB

26th March 1992

Dear Michael,

PSA PROJECTS PRIVATISATION

Will be most if you

You copied to Michael Howard your minute of 9 March to the Prime Minister about the sale of PSA Projects. I am responding in Michael's absences.

We support your proposal for an early launch of the sale of PSA Projects.

However, we cannot agree with your proposal that part of this Department's forward work programme should be committed to PSA Projects. When Michael wrote to you on 22 July 1991 he resisted this proposal because it would put at risk, especially for the Employment Service Agency, policies and initiatives to manage our estates more efficiently and effectively. The Employment Service Agency competitively tenders all its work contracts, and to change this policy would be a retrograde step and one which would undermine managerial initiatives.

I am sorry that we cannot be any more helpful. PSA Projects will of course be invited to tender for Departmental projects, and I hope will be in a position to win a reasonable proportion on merit.

I am copying this letter to the Prime Minister, other members of the Cabinet and to Sir Robin Butler.

Yours ever,
Nick

VISCOUNT ULLSWATER



Employment Service · Training Agency
Health and Safety Executive · ACAS



RECYCLED PAPER

From: THE PRIVATE SECRETARY



HOME OFFICE
QUEEN ANNE'S GATE
LONDON SW1H 9AT

20 March 1992

Dear Philip,
WITH BP

Your Secretary of State copied to the Home Secretary his minute of 9 March to the Prime Minister, on the privatisation of PSA Projects, seeking agreement to the proposed timetable, and also to a strategy to guarantee PSA Projects a proportion of Departments' future workload.

The timetable set out in the minute will, of course, be affected by the announcement of the General Election, but we see no objection to the early launch of the sale of PSA Projects, providing that Departments' interests after the sale can be adequately protected.

I am afraid, however, that as far as the Home Office is concerned, we cannot agree to guarantee PSA a proportion of future design work in existing prisons. As we have explained at official level, PSA do not have expertise in this field, and the Directorate of Works do not consider that it could fulfil its obligations to the Prison Service if it were required to allocate a proportion of this work to PSA. Moreover, we could not be satisfied that an arrangement of this kind would offer value for money. We would, however, be prepared to guarantee PSA Projects the opportunity to bid for a proportion of design work on the existing prison estate, in competition with others.

A copy of this letter goes to the Private Secretaries to recipients of your Secretary of State's minute.

Yours,
Heather
MISS H J WILKINSON

Philip Ward Esq
Private Secretary
Department of the Environment
2 Marsham Street
London SW1

fst.nb/Maude/2.12.3

POLICY AND COMMERCIAL IN CONFIDENCE



FROM: FINANCIAL SECRETARY
DATE: 13 March 1992

PRIME MINISTER

PSA PROJECTS PRIVATISATION

live end?
I have seen a copy of Michael Heseltine's minute to you of 9 March.

There has been some recent correspondence between Emily Blatch, Archie Hamilton and me on this subject, and I agree with the strategy summarised in the penultimate paragraph of Michael's minute. In particular, I fully support the objective of launching the sale of the Projects business as soon as possible after the Election, subject to the conditions that Michael mentions, in particular that appropriate documentation is available to sustain a proper competitive valuation of the business. In this context, it is clearly crucial that officials in PSAS and MOD should continue to give high priority, during the pre-Election period, to assembling the financial information on which the Sales Memorandum critically depends, and understanding any deficiencies in that information. If this window of opportunity to sell the business is missed then I agree with Michael that there will be no subsequent opportunity.

On the question of forward workload, I would strongly endorse Michael's view that it will be for individual Departments to satisfy themselves that the nature and volume of such work will not exceed that which Projects might reasonably have been expected to win in competition and subject to market prices being negotiated, thereby securing departmental value for money. I would similarly endorse his comment that, if the attempt at sale fails, Departments should be free to withdraw work and put it to competitive tender.

fst.nb/Maude/2.12.3

POLICY AND COMMERCIAL IN CONFIDENCE

I am copying this minute to members of the Cabinet and
Sir Robin Butler.

F. M.

FRANCIS MAUDE



SECRETARY OF STATE

MO 10G

PRIME MINISTERPSA PROJECTS PRIVATISATION

Michael Heseltine sent me a copy of his minute to you of 9th March about the progress of work necessary to offer PSA Projects for early sale.

Like Michael I am keen for a sale to proceed if possible, and I agree that unnecessary delay may reduce the chances of securing sensible competition and reasonable terms. Nevertheless as has I think been fully recognised by Emily Blatch in previous correspondence, if we are to have any chance of controlling expenditure and protecting the Defence budget once PSA Projects is in the private sector, we must have full details of the financial status of those contracts currently being managed on our behalf. I know that the Projects business is pulling out all the stops to give us the details we need, but their success will be the controlling factor in determining the timescale to which we can proceed in setting the sales competition in motion.

Michael deals too with setting up arrangements for committing certain work to the new organisation. I have made it clear that I should find it difficult to consider more than the £8M over two years which I have already said that the Ministry of Defence could offer, subject of course to the general point on competitive pricing to which Michael refers. There is still much to do in sorting out the exact details of the way in which these pricing arrangements should be defined in order to obtain value for money, and my officials are in touch with those in the Department of the Environment about that.





SECRETARY OF STATE

There are too other matters about which officials are in consultation. But these need not hold up the competition process. We have been promised the financial information we need by around the end of March, and if that is achieved then I hope it will prove possible to launch the sale competition immediately after the Election.

Ministry of Defence
13th March 1992

(T K)



100% Recycled Paper



POLICY AND COMMERCIAL IN CONFIDENCE

PRIME MINISTER

PSA PROJECTS PRIVATISATION

Last July you agreed that we should continue preparations for offering PSA Projects for sale early this year. This was subject to progress and market sentiment and to a review of these at the end of last year.

The result of that review, which calls heavily on our privatisation advisers' analysis and judgement, is that we remain convinced that attempting sale as early as possible this year is the right way to proceed. We have developed an offer structure in consultation with the Treasury which provides potential purchasers with reassurance on the two key issues of concern to them ie the contingent redundancy liabilities and inherent uncertainties for the forecast profitability of the current workload. This significantly increases the prospects of a successful sale.

Closure would be difficult to defend when we have significant players professing a strong interest in the acquisition of Projects. I cannot of course guarantee that we will receive acceptable bids. However, the cost of attempting a sale, but failing, adds little to the cost of closure.

In the light of progress made and the continuing indications of interest in Projects I would like your and colleagues contingent agreement that we should aim to be ready to offer Projects for sale by the end of March despite the uncertainties about the timing of the election. If the election were called for April 9th it would be impractical to launch the sales competition until shortly thereafter. This would lead, all going well, to an exchange of contracts in June. We would not however launch a sale competition until, and only if, we were satisfied that adequate progress had been made in terms of the sale preparations. Emily Blatch has agreed this approach with Francis Maude and Archie Hamilton.

We have of course been working for some time on the basis that the sales memorandum should be ready for issue in March but not issued until after the election. However, a major player in the construction industry has put in a potentially attractive unsolicited indicative and conditional offer for the whole of Projects. It would be wrong to negotiate sale exclusively with a single potential purchaser: the taxpayers' interest is best protected by an open competition. But the prospective purchaser feels strongly that speed is of the essence if further decline in the workload and morale of the business is to be arrested and reversed. Our privatisation advisers, both Coopers and Kleinworts, are clear that it is in the interest of a successful sale to go as fast as we properly can to meet the potential purchaser's concern over timing. In somewhat problematic trade sales of this nature, inflexibility over timing can fatally reduce the chances of securing the Government's objectives in the

most cost-effective way. They advise against leaving starting the sale process later than April, provided satisfactory progress is made on the sale preparations, even if the election is still pending.

We must of course ensure that we allow the time for a proper competitive process and for staff consultation. We must also be sure that preparations are sufficiently advanced to ensure that the Government is not at a disadvantage in the sale negotiations, nor, post-sale, in terms of client Departments dealing with privatised business. My present judgement - and it has to be a provisional judgement subject to review in the light of progress for example in producing the financial information for the sales memorandum - is that it should be possible to launch a sale competition in the first half of April. This represents an ambitious target, but an achievable one, if staff here and in other Departments give the resolution of the remaining problems sufficient priority.

We must also maximise the prospects of a successful sale. Our advisers are clear about the importance of securing adequate workload if purchasers are to take maximum severance liabilities over from Government. The strategy agreed last July involved Departments leaving currently committed work with Projects despite the risk that a sale might not be achieved, and in some cases, providing some limited forward workload at market prices for up to three years. To get value for this in the sale we now need to press ahead with settling the umbrella agreements with departments so these can be described in the sales memorandum.

There is however some concern that this strategy conflicts with the Government's general drive toward competitive tendering as a way of securing value for money. To allay that concern I seek your and colleagues' endorsement of the strategy of providing Projects with some forward workload subject to the nature and volume not exceeding that which Projects might reasonably have been expected to win in competition and to market prices being negotiated thereby securing departmental value for money. It will be for individual Departments to satisfy themselves on these latter points. The reason why I am seeking your agreement to this strategy is to improve the prospects of transferring severance liabilities to the purchaser, thus facilitating the achievement of our wider objective of privatising Projects' activities this year, whilst securing continuing employment for as many staff as possible. If the sale failed because for example the bids received represented less value for the taxpayer than closure or because the arrangements proposed for staff post sale were unacceptable, Departments would be free to withdraw work and put it to competitive tender.

For these reasons and to secure the commitment of all concerned to making every effort to achieve the ambitious timetable proposed, I would be grateful for your agreement to the proposals discussed above, ie

- set ourselves the target of being ready to launch the sale of Projects as early in April as possible;
- but only to confirm and announce the launch date and

timetable for sale when we are confident that an acceptable sales memorandum can be issued, client Departments' interests post sale can be properly protected and a proper competition launched. (It is likely to be late March before we have sufficient comfort on the financial and other aspects);

- for your and colleagues' endorsement of the strategy of providing Projects with some additional forward workload in addition to its current workload subject to the conditions set out above, (it follows from this that Departments should expedite work on identifying possible forward workload).

I am copying this minute to members of the Cabinet and Sir Robin Butler.

MH

9 March 1992



POLICY AND MANAGEMENT IN CONFIDENCE

The Rt Hon Kenneth Baker MP
The Home Secretary
Queen Anne's Gate
London SW1

2 MARSHAM STREET
LONDON SW1P 3EB
071-276 3000

My ref:

Your ref:

- 8 AUG 1991

Dear Home Secretary

PSA PROJECTS : PRIVATISATION

Thank you for your letter of 23 July.

The best prospect we have of ensuring the satisfactory completion of work for client departments is a successful privatisation of PSA Projects. Only then will it be possible to put an end to the uncertainty staff are bound to have about what the future holds. I hope that we will be able to secure a successful sale. But I cannot guarantee it. That depends on prospective purchasers' judgements about the business and its prospects. The workload the business has when it is privatised will obviously be an important consideration; my officials are in touch with yours about this.

It is clearly important that client departments should be satisfied about the arrangements that will apply after sale. Officials have been discussing the contractual arrangements that we need to put in place. I am not aware that there have been any serious difficulties. So far as closure is concerned, it is not an option we can rule out; it takes two to make a sale. We would obviously discuss with you in that event how existing projects could best be managed to completion. But a degree of disruption cannot be ruled out.

Copies of this letter go to the Prime Minister, the Lord Chancellor and members of EA.

Yours sincerely

Benny Adams

MICHAEL HESELTINE

(Approved by the Secretary of State
and signed in his absence)



recycled paper

CIVIL SERVICE: PSA PT4

FROM THE RIGHT HONOURABLE THE LORD MACKAY OF CLASHFERN



n.b.P.T.
RTP
2/8

HOUSE OF LORDS.
LONDON SW1A 0PW

3/ July 91

Dear Michael, Hop

The Home Secretary sent me a copy of his letter to you of 23 July about the future of PSA Services, and I have also now seen a copy of your letter to the Prime Minister of 19 July.

As you know I have a significant interest in these matters mainly because of the contribution made by PSA Projects to my Court Building Programme. I realise that the pressure of events requires prompt action, but I support the view that there should be full and prompt consultation at Ministerial and official level as things develop. This will help to ensure that, whether or not disposal of PSA Services to the private sector proves possible, the considerable current investment in building programmes using PSA Services is fully protected, and that the transitional arrangements made safeguard all our interests.

Copies of this letter go to the Prime Minister, the Home Secretary and members of the EA.

Yours etc,
James.

The Right Honourable
The Secretary of State for the Environment

CIVIL SERVICE: PSA Restructuring P4



10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

24 July 1991

Dear Phillip,

PSAS PRIVATISATION

The Prime Minister was grateful for your Secretary of State's letter of 19 July, setting out plans for taking forward the proposed privatisation of PSAS.

I submitted your Secretary of State's letter plus the attached draft PQ to the Prime Minister yesterday evening.

As you were informed over the telephone this morning, the Prime Minister is content for the written PQ and answer to be given as drafted.

I am copying this letter to the Private Secretaries to members of EA.

Yours ever,

Barry

BARRY H. POTTER

Phillip Ward, Esq.,
Department of the Environment.

MANAGEMENT AND POLICY IN CONFIDENCE



QUEEN ANNE'S GATE LONDON SW1H 9AT

23 July 1991

Mr Michael

I have now seen a copy of your minute to the Prime Minister of 19 July about the announcement you propose to make on 24 July on the future of PSA Services. The Home Office has a considerable interest in this matter, and I was surprised therefore that a copy was not sent to me.

It is clearly most desirable that the speculation about the future of PSA Services is ended. I am, however, very concerned that the steps you propose should not affect the delivery of the badly needed prison places which will be provided in the eleven new prisons which PSA Projects are building for us and which are in most cases now in their final phases. I hope therefore that every effort will be made to retain the services of experienced and well regarded staff in the run-up to privatisation, and that they are for instance given assurances about their future which will encourage them to remain.

Equally we look for full and prompt consultation both at Ministerial and official level on the arrangements for sale and how these will affect our projects. Officials in particular will need to agree the services which a private buyer would be required to provide on our projects, and these will need to be reflected in explicit commitments which fully safeguard our interests. Should disposal to the private sector of PSA Projects not prove possible, we must have ample notice of closure so that we are ready to take over PSA's responsibilities. Whilst I recognise the pressures in this sort of exercise, we must know where we stand, so that we can plan accordingly.

Copies of this letter go to the Prime Minister, the Lord Chancellor, and members of EA.

Michael Heseltine

The Rt Hon Michael Heseltine MP
Department of the Environment
2 Marsham Street
London SW1

PSA
PSC



MO 10J

MINISTRY OF DEFENCE
WHITEHALL LONDON SW1A 2HB
Telephone 071-21 82111/3

23 July 1991

Dear Stephen,

PSAS PRIVATISATION

My Secretary of State, having been consulted by the Environment Secretary, endorses the proposals in Mr Heseltine's minute of 19th July but there is one point of detail on which I have been asked to put the record right: the date for the closure of PSA International, at the end of the ante penultimate paragraph, should read "by 1993", instead by "by end 1992/93".

Yours sincerely

Miss J R Binstead
(MISS J R BINSTead)
Private Secretary

J S Wall LVO CMG
10 Downing Street



100% Recycled Paper



Confidential

10 DOWNING STREET

Prime Minister

PSA PRIVATISATION

I asked Carolyn S. for advice on substance. She agrees that the DOE drive - i.e. effect putting off closure is acceptable. It is better than earlier DOE ambivalence to pump in a 'clonny' before full.

I have checked with Treasury. They too are content.

Given earlier political controversy about PSA, I was a little concerned about channelling - a written answer on the last full day of term. But on balance you may feel the second answer will cause no difficulty.

Content?

BHP 2317

Such a commitment, there is no guarantee that sale or sales can be achieved at a cost less than that of closure. If it looked as if it might cost more than closure we would go for closure. There are however a number of substantial companies who profess serious interest in acquiring Projects. A decision now to go for closure rather than attempt sale would put at risk the completion of Projects' current workload to cost and time. Given the professed interest and the potential savings to the taxpayer, I do not consider it advisable to decide to close now thereby incurring an additional 1100 redundancies in addition to the 1000 or so already envisaged in the sale option assessed by CLD.

SENT & POLICY
CONFIDENCE

2 MARSHAM STREET
LONDON SW1P 3EB
01-276 3000

My ref:

Your ref:

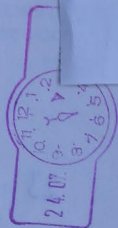
19 JUL 1991

reports by Coopers and Lybrand for privatising various parts of g extensive discussions with MOD, t client, and with Treasury, Tom come to the following conclusions.

g the activities of PSAS as soon ually no assets. It has only its f its staff combined with their to sell. As civil servants the entitlements. Privatisation will imise the cost to Government of the public sector to the private take place through closure.

projects as a the major consultancy sign and related services are not mproved significantly if the main part of their future workload to make a limited commitment of this rangements can be negotiated to

So are certain other client sury endorses such commitments as vernment overall.



MANAGEMENT & POLICY
IN CONFIDENCE

2 MARSHAM STREET
LONDON SW1P 3EB
01-276 3000

My ref:

Your ref:

The Rt Hon John Major
10 Downing Street
London
SW1

19 JUL 1991

Prime Minister

PSAS PRIVATISATION

I have been considering the reports by Coopers and Lybrand Deloitte (CLD) on the options for privatising various parts of PSA Services (PSAS). Following extensive discussions with MOD, by far and away PSA's largest client, and with Treasury, Tom King, Francis Maude and I have come to the following conclusions.

We are committed to privatising the activities of PSAS as soon as practicable. PSAS has virtually no assets. It has only its workload and the expertise of its staff combined with their experience of Government work to sell. As civil servants the staff have generous redundancy entitlements. Privatisation will not raise cash; it might minimise the cost to Government of moving PSAS's activities from the public sector to the private sector, which would otherwise take place through closure.

The prospects for selling PSA Projects as a the major consultancy or consultancies providing design and related services are not good. The prospects would be improved significantly if the main client departments could commit part of their future workload to Projects. MOD are prepared to make a limited commitment of this kind provided satisfactory arrangements can be negotiated to safeguard their interests. So are certain other client Departments provided that Treasury endorses such commitments as securing value for money to Government overall.

Even with such a commitment, there is no guarantee that sale or sales can be achieved at a cost less than that of closure. If it looked as if it might cost more than closure we would go for closure. There are however a number of substantial companies who profess serious interest in acquiring Projects. A decision now to go for closure rather than attempt sale would put at risk the completion of Projects' current workload to cost and time. Given the professed interest and the potential savings to the tax payer, I do not consider it advisable to decide to close now thereby incurring an additional 1100 redundancies in addition to the 1000 or so already envisaged in the sale option assessed by CLD.

I recommend instead that we announce that we are continuing to pursue sales options for Projects with a view to sale early next year. If there were insufficient interest at that point or if satisfactory arrangements could not be negotiated with client departments and with potential purchasers within a fairly tight timescale - say before end 1992 - we would revert to the closure option. Either way Projects' activities would end up in the private sector by end 1992/3.

Much the same issues arise on Building Management except that very early closure is not an option. MOD would have the greatest difficulty in replacing BM with alternative suppliers in the short to medium term. Equally if a decision were taken now to run BM down over a period of years, the cost effective completion of work by PSA staff in such circumstances could not be guaranteed. The better option in my view is to aim to sell the BM regional businesses by 1992/3. To help ensure the businesses are ready to be offered for sale late next year, I propose to appoint an interim contractor manager to oversee and advise on the restructuring needed. I would review progress made and market sentiment next Summer and then proceed to sale as soon as possible. I would however retain the option of managed closure if sale prospects looked poor.

My Department and MOD have agreed to give priority to the preparations needed for the sale of the BM businesses in late 1992. For the present MOD will continue with its market testing programme but will review with my Department the prospects for a successful sale over the forthcoming period of contractor management. If then appropriate and if in HMG's interests MOD are prepared to contemplate giving the regional businesses substantial relatively stable workloads over a 3 year period following sale.

PSAI

The clear advice is that PSA International is not saleable as one organisation because of its almost total dependence on MOD and the lack of a domestic base. The only option is therefore managed closure. We are talking to MOD about how best to manage the closure of PSAI by end 1992/93.

SUMMARY

Subject to your views I propose to give the attached written Answer on Wednesday. An early announcement is essential to make progress on the appointment of a contractor manager for Building Management, to secure staff commitment to the necessary preparations and to give clients confidence in continuing to put work with the PSA businesses. If we allow the present uncertainty and press speculation to continue over the summer, we reduce the prospects of successful sales.

I am copying this to members of E.A.


MICHAEL HESELTINE

MANAGEMENT & POLICY IN CONFIDENCE

DRAFT PQ

TO ASK THE SECRETARY OF STATE FOR ENVIRONMENT IF HE WILL MAKE A STATEMENT ON THE FUTURE OF PSAS

DRAFT ANSWER

1. We remain committed to transferring the activities currently carried out by the PSAS business to the private sector. Following consideration of the reports from my Department's advisers, Coopers Lybrand & Deloitte, we have reached the following conclusions on the options for the different PSAS businesses.
2. PSA International is not saleable as a separate organisation. We will therefore consult its clients, in particular MOD about how best to phase out their reliance on PSAI and to complete the work currently underway.
3. Building Management is being reorganised into five regional businesses. I plan to appoint a contractor manager to carry through the restructuring and preparations necessary to make the businesses ready for sale. Providing satisfactory progress is made and subject to market sentiment, I aim to offer the regional businesses for sale towards the end of next year.
4. Again subject to progress and market sentiment, I propose to offer PSA projects early next year. The necessary financial information is being drawn together to determine the best form of sale or sales.

MANAGEMENT AND POLICY IN CONFIDENCE

PRIME MINISTER

23 July 1991

PSA SERVICES PRIVATISATION

An Act has been passed providing for the Property Services Agency to be privatised. The PSA consists of:

- PSA Projects
- PSA Building Management
- PSA International

For some time it has been clear that it would be difficult to sell any of these "businesses". There are no assets - just manpower and a tradition of doing business for Government Departments which are in the process of untying themselves from the PSA. (The untying process would probably have to be slowed down to ensure sale.)

Michael Heseltine has now concluded:

- that despite bleak prospects for a sale costing less than managed closure, we should continue to explore options for selling PSA Projects immediately after the Election. If a sale was not possible we should proceed to closure;
- that despite even bleaker prospects for the sale of PSA Building Management, we should put in a contractor manager now to see if the organisation could be got ready for sale by the second half of 1992. This slower timescale reflects the need for MOD (far and away PSA's biggest customer) to find alternative suppliers of building management services. Again if a sale did not materialise, closure would be considered;

MANAGEMENT AND POLICY IN CONFIDENCE

- that we should manage the closure of PSA International by the end of 1992/93.

COMMENT

PSA are playing for time. There are good arguments for deciding on managed closure for the whole organisation now, possibly with different timescales for the three parts. It is unlikely that PSA will be more saleable in future.

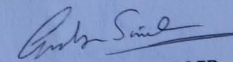
But PSA employ 20,000 people. Many of them believe that they have a future with privatisation. Announcing closure now would be very unpopular. Michael Heseltine has shrunk from this.

The Treasury were worried at an earlier stage that DOE would pump money into the PSA to make it saleable. Michael Heseltine seems to have set his face against this (though the contractor manager will cost a few £ million and there must be doubts about the ability of any manager to turn round such a large and inefficient organisation in a year). The Treasury therefore go along with the proposal to keep PSA going for another year or so before grasping the nettle of closure.

CONCLUSION

Given the Treasury position, and the fact that it is not now proposed to pump PSA full of money to facilitate a sale, you will probably not want to challenge the course outlined by Michael Heseltine. But in agreeing you may wish to stipulate.

- that decisions on closing PSA Projects and Building Management must be taken before the end of 1992-93 if the two businesses have not been sold by then.


CAROLYN SINCLAIR

(288.CS)

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fst.nb/fst/13b.03.91

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n.b. P.M.
BHP
14/13

alp.

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Michael Heseltine MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

13 March 1991

Dear Michael

THE CROWN SUPPLIERS (TRANSPORT) PRIVATISATION

WITH GP?

I have seen your Private Secretary's letter of 11 March to Barry Potter.

I note that the Prime Minister is content with your conclusion that the Transport business should be closed and I fully agree; as I said in my earlier letter the issue was finely balanced, and I understand that recent developments have tipped the balance in favour of closure. I note that your officials will be in touch with mine to discuss consequential.

It will of course be most important to get the best value for money from the wind-up of the Transport business. I assume you will be following the same basic arrangements as for the Contract Furnishing business, which appear to have worked reasonably well. It would be useful for the team responsible for the winding-up to explore urgently the scope for disposing of the vehicles on hire at present in packages, together with the contracts under which they are on hire, to trade purchasers, which may offer some extra value added by comparison with the alternative of sale of the vehicles alone.

Copies of this letter go to the Prime Minister, to George Young and to Sir Robin Butler.

FRANCIS MAUDE

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10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

13 March 1991

Dear Kate,

CROWN SUPPLIERS (TRANSPORT) PRIVATISATION

Thank you for your letter of 11 March in response to my letter of 13 February to Phillip Ward. I submitted your letter to the Prime Minister yesterday evening.

The Prime Minister is most grateful to your Secretary of State for taking a close interest in this matter. He fully agrees with his conclusion that TCS Transport business should be closed. The Prime Minister is also content for an announcement to be made as soon as practical.

I am copying this letter to John Gieve (HM Treasury), Andrew Allberry (Minister of State's Office, Department of the Environment) and Philip Rutnam (Financial Secretary's Office, HM Treasury).

Yours,

Barry

BARRY H POTTER

Miss Kate Bush
Department of the Environment

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COVERING CONFIDENTIAL

2 MARSHAM STREET
LONDON SW1P 3EB
071-276 3000

Prime Minister

You may recall the

background - see letter attached.

The release of TCS is now

being sent.

My ref:

Your ref:

Barry Potter Esq
Private Secretary to
The Prime Minister
10 Downing Street
LONDON
SW1A 2AA

BHP

12/12

11 March 1991

Dear Barry

CROWN SUPPLIERS (TRANSPORT) PRIVATISATION

Thank you for your letter of 13 February to Phillip Ward. I apologise for the delay in replying.

As the Prime Minister requested, my Secretary of State consulted the Department's Accounting Officers and legal advisers and satisfied himself on the point which the Prime Minister raised and those put by the Financial Secretary in his letter of 8 February.

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I am copying this to John Gieve, Andrew Allberry and Philip Rutnam.

Yours

Kate

KATE BUSH
Private Secretary

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10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

CLOSED UNDER THE
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ACT 2000

13 February 1991

BF on p.2.

Dear Pailey,

CROWN SUPPLIERS (TRANSPORT): PRIVATISATION

The Prime Minister has seen a copy of the Minister of State's (Sir George Young) letter to the Financial Secretary of 4 February, setting out proposals for the privatisation of the Crown Suppliers transport business (TCS). He has also seen a copy of the Financial Secretary's letter of 8 February on this subject.

This letter should be copied ONLY to Ministers and officials directly concerned with handling the subject of the letter.

The Prime Minister is concerned that the Government might face considerable criticism if the proposed sale of TCS went ahead. A number of features of the sale have given rise to this concern.

First, the proposed sale price is very near the bottom of the estimated Exchequer proceeds from a straightforward closure. Indeed the expectation, on the basis of the figures available, would be that closure generates more money for the Exchequer.

Second, there would seem to be a serious risk of relatively quick asset stripping, once TCS is sold. It is unclear whether the purchasers, and in particular the private sector partner, SME, can have any other planned use of the assets.

Third, the PSA is the Crown Suppliers' sole customer for the vehicle fleet. But, as your Secretary of State is aware, PSA's future is not yet decided. Were the Government later to close PSA, that would damage, perhaps terminally, a privatised TCS. No matter how much the Government protested that no final decisions on the future of PSA had been taken at the time TCS was sold, the Government would be accused of failing to disclose a material fact.

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Potter/Ward 13/2/91

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- 2 -

DF | Against that background, the Prime Minister would be very grateful if your Secretary of State could consult the DOE's Accounting Officers and legal advisers, in particular on the PSA dimension, and, having reviewed all aspects of the proposed privatisation, indicate whether, in his view, the proposed sale should proceed.

I am copying this letter to John Gieve (Chancellor's Office), Andrew Allberry (Minister of State's Office, DOE) and Philip Rutnam (Financial Secretary's Office, H.M.T.).

You need to read John Gieve's letter of 11th 2, 1991, to understand what is going on in the proposed privatisation of BAA.

Yours ever,
Barry

BARRY H. POTTER

Phillip Ward, Esq.,
Department of the Environment.

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PRIME MINISTER

TCS PRIVATISATION

You should be aware of a problem with the proposed privatisation of the Crown Suppliers (TCS) transport business.

Superficially there is no difficulty. Sir George Young (Flag A) wants to accept a joint bid from the current management in conjunction with an outside company SME. The Financial Secretary (Flag B) goes along with this, while indicating one or two caveats.

You need to read John Mills' excellent note at Flag C, however, to understand what is going on. The dangers in the proposed privatisation are as follows.

- (i) The proposed sale price is very near the bottom of the estimated Exchequer proceeds from simple closure.
- (ii) There is a serious risk of quick asset stripping - the assets are a vehicle fleet and property/land. Indeed it is difficult to believe the purchasers can have any other planned use of the assets. (That risk is partially acknowledged in Sir George Young's letter.)
- (iii) The PSA is Crown Suppliers' sole customer for the vehicle fleet. But PSA's future is undecided. If the Government did later decide to close PSA, that would damage, probably terminally, TCS. Any protestations that no such final decision had been taken at the time TCS was sold would not cut much ice.

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You need to consider whether the attractions of pursuing privatisation policy out-weigh the clear political risks in this instance.

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Potter/PM 12/2/91

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- 2 -

Conclusion

The options are:

- (i) Indicate that on balance closure seemed the better option and seek the Ministers' comments?
- (ii) Seek an opinion on the propriety of the sale from the DoE accounting officer (as John Mills recommends)?
- (iii) Invite the two Ministers in for a discussion?

But there are some wider attractions in a fourth option:

- (iv) invite Mr. Heseltine to consult his accounting officer, in particular on the the PSA dimension and let you have his views.

BHP

(BARRY H. POTTER)

12 February 1991

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MANAGEMENT AND COMMERCIAL IN CONFIDENCE

PRIME MINISTER

12 February 1991

PRIVATISATION OF THE CROWN SUPPLIERS (TCS)' TRANSPORT BUSINESS

George Young is seeking agreement to the Government's accepting the single bid which has been received for TCS' vehicle hire and maintenance business. The bid is near the bottom of the range for estimated proceeds if the Government simply closed TCS down.

The assets of the business are principally a fleet of about 4,000 vehicles, on contract hire to PSA, and land on three sites valued at some £3.5m. There are about 90 staff.

The bid is from a group within the current management in conjunction with an outside company, SME, a shell company whose owner has interests in vehicle distribution and sales.

George Young's case for accepting the bid is that:

- it is a bird in the hand: worth £10.3m, compared with estimated net proceeds of closure ranging between £9.6m and £16.3m.
- it offers the prospect of saving 90 jobs which would be lost on closure.
- and it offers the prospect of continuation of a business on which PSA relies very heavily.

The Financial Secretary accepts George Young's case, subject to your views. But it is clear from his letter that Francis Maude has some unease about:

MANAGEMENT AND COMMERCIAL IN CONFIDENCE

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- the bid price, in relation to the range of estimated closure proceeds; and
- the risk of quick asset-stripping by the purchasers.

BACKGROUND

You may recall that last summer, as Chancellor, you accepted advice from Francis Maude to support a proposed management buy-out (MBO), and wrote accordingly to Chris Patten on 31 August. But what was envisaged then was purely an MBO, and at a slightly higher price. The proposal now is different: part MBO part outside bid. The MBO team is putting up £0.25m; SME £1m.

ASSESSMENT

The involvement of an outsider must increase the risk of asset-stripping. The bid values the vehicle fleet at about £6m. This is just about the bottom closure estimate. The top closure estimate is £12m. The outsider, whose specialism is second-hand vehicles, must clearly consider that he is getting a bargain.

Risk also extends to the land assets. These were valued at £3.7m in 1989. For one of the three sites this includes the value of planning permission for housing. For another, in Bristol, it excludes the possibility of planning gain, but the bid allows for clawback by the Government of 30% of any development gain. That is better than nothing, but it means the lion's share of any gain would stay with the purchasers.

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POLITICAL RISKS

Asset-stripping for a quick profit must be a real possibility. George Young accepts this. But the political risks bear most heavily on you, not him. Anything which smacks, even slightly, of another Royal Ordnance case (where newly-privatised land assets were resold at a large profit) would seriously damage the credibility of your privatisation strategy in the run-up to the election.

The involvement of an outside company, as opposed to a wholly MBO approach, must increase the risks. Moreover, DoE officials admit that TCS as it stands is a business with "diminishing prospects". It begs the question, what else can be in it for SME, but to pick up a bargain and sell it on as quickly as possible?

You should also be aware that Dale Campbell-Savours has been active in criticising the involvement of SME, with the clear indication that he believes a knockdown sale of taxpayers' assets is in the offing.

The position of PSA

There is one further angle which is not addressed in George Young's letter. This is the Government's position on the future of PSA, which is effectively TCS' sole customer for its vehicle fleet. Not surprisingly, the bid is contingent upon the financing banks' being satisfied as to PSA's future vehicle hiring policy.

The question is: what is to be said to TCS about PSA?

The Government's public position is that PSA will shortly become a Government-owned company as a prelude to eventual privatisation in 1992. But, as you are aware, PSA's future is extremely precarious, and one option which has been canvassed in the Treasury and in No 10 is its entire closure. You yourself have expressed the view that this may well be the right course. The decisions on PSA's future will need to be taken quite soon.

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It is not DoE's intention to disclose the possibility that there are options for PSA other than eventual privatisation and that closure is at least being considered. Indeed, I do not believe the DoE team negotiating with TCS is aware of this. Nor, I expect, is George Young.

This raises very serious questions:

- what if, shortly after TCS was sold, the Government then decided to close PSA not having revealed the possibility to the bidder? You could not truthfully say that the option of closing PSA only arose after the TCS sale. The Government would be accused of withholding a highly material fact, and you would be put in an extraordinarily difficult position.
- what if, on the other hand, declarations made to TCS about the future of PSA tied the Government's hands against deciding on PSA closure?

CONCLUSION AND RECOMMENDATION

On the facts available my advice is that you should be extremely cautious about accepting what George Young proposes. There are sound financial grounds for concluding that the taxpayers' interest would be better served by a closure. There is a fair risk that, by proceeding with the sale, an asset-stripping situation could arise which might be politically very damaging.

But most important of all, it must be clarified what exactly needs to be disclosed about the future of PSA, and how Ministers (including yourself) with knowledge that closure of PSA is under consideration stand in relation to the disclosure.

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The need for caution is merely increased because of Mr Campbell-Savours' interest.

You may well judge that a clear decision now to go for closure would be the most prudent course and the one most likely to be in the taxpayers' best interests. That might anyway be the outcome if the bidders are not satisfied about PSA, or if they seek to reduce their bid at the last moment. It would be the only proper course if possible closure of PSA is a material fact which nevertheless may not be revealed (and I do not see how it could be given that PSA staff themselves have absolutely no inkling of it).

But if you are inclined to accept George Young's judgement that the bid should be accepted, I recommend that you first seek:

- an opinion from DoE's Accounting Officer as to the balance of financial advantage between accepting the bid and closure.
- legal advice, through Sir Robin Butler, as to whether disclosure about possible closure of PSA is necessary as a material fact; and if it is not, whether this would in fact rule out the option of closure as a conscious policy decision in a few months time.

John Mills
JOHN MILLS

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Treasury Chambers, Parliament Street, SW1P 3AG

Sir George Young Bt MP
 Minister of State
 Department of the Environment
 2 Marsham Street
 LONDON SW1P 3EB

8 February 1991

Dear Minister,

file with SP

PRIVATISATION OF THE CROWN SUPPLIERS: TRANSPORT BUSINESS

Thank you for your letter of 4 February.

I have again considered this matter very carefully. It seems to me that the balance of argument has shifted since the previous round of correspondence in August last year. I have in mind the risk that the restructured bidding team might be able to sell the assets for significantly more than the price paid. I am also troubled by the very slow progress of the negotiations and the inexorable increase in cumulative fees as the negotiations drag on.

In my view the issue is very finely balanced. However, in the light of your advice on the balance of risks I would be prepared to agree to the sale on the terms set out in your letter. I take it that you are prepared to defend the Government's position if the bidder proceeded to strip out the assets of the business, possibly making a substantial profit by closing down the business.

I remain very concerned that the position may not be resolved quickly, and I think it essential that you should set a deadline for exchange of contracts of a month from now. If that deadline cannot be met, I believe the business would have to be closed forthwith.

I note that completion of the deal would be conditional on satisfactory new management appointments, endorsed by Samuel Montagu and Co, as well as negotiations on the detailed legal documentation and satisfaction of the backers' requirements for assurances about business from PSAS. Here too I am concerned about the potential for further delay and the risk that the offer may be reduced. I am sure you will do all you can to bring negotiations to a swift conclusion: you should retain flexibility to break off the further negotiations after exchange of contracts without penalty if the bidders appear to be dragging their feet.

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I understand that you have taken legal advice about the need for disclosure of the state of the Government's thinking on PSAS's future. If "due diligence" or other developments should lead the team to reduce their bid, we would have to reconsider and, I think, go for closure.

Subject to the Prime Minister's views, I am prepared to accept your view that you should proceed with the bid subject to the conditions I have specified. I note that our officials will be in touch over the terms of the announcement which would be made immediately following the exchange of contracts.

I am copying this letter to the Prime Minister.

Yours sincerely,
Philip Rutnam

pp FRANCIS MAUDE

(Approved by the Financial
Secretary and signed in
his absence.)

MANAGEMENT AND COMMERCIAL-IN-CONFIDENCE



Minister for Housing
and Planning

Department of the Environment
2 Marsham Street
London SW1P 3EB

Telephone 071 276 3310

STAFF AND COMMERCIAL IN CONFIDENCE

4 February 1991

Dear Financial Secretary

TCS PRIVATISATION

attach
Last summer there was correspondence between the then Prime Minister, Chancellor of the Exchequer and Secretary of State for the Environment which established principles for considering bids for the two transport businesses of TCS. Since then, our officials have kept in close touch and, as you know, the decision to retain the interdepartmental despatch service (IDS) has been announced. This letter deals with a revised bid for the remaining vehicle hire and maintenance business from a joint team of TCS staff and Sanderson Murray and Elder (Holdings) plc (SME). Samuel Montagu and Company, our banking advisers, recommend that, on balance, the bid satisfies the criteria for the sale set out in the bid documents, subject to satisfactory new appointments to the purchaser's management team.

The bid is the only one and has to be judged, as before, against closure of the business. The bid is evaluated as being worth about £10.3m, compared with the range of £9.6m to £16.3m for the estimated net proceeds of closure. Like the bid approved last summer, it is at the lower end of the range of estimated net proceeds of closure, which are, of course, considerably less predictable than those of sale. On this basis, it is almost as good on financial grounds as last summer's bid. I accept, however, that as a result of the involvement of an outside firm, there may now be a greater risk of the purchaser closing down the workshops part of the business and making a real or apparent profit on the sale of the land assets. I think we shall have to live with that. The finance for the bid has been obtained. It is conditional on the outcome of "due diligence" and on the main financier being satisfied with PSAS' future hiring policy, on which discussions continue.

Another key consideration is the effect on staff of the alternatives. Closure would involve immediate redundancy for 90 or so technical and industrial staff plus any of the generalists who could not be found other posts. It is hard



to predict the job prospects of staff if the sale goes ahead. The business is risky, particularly the unprofitable workshops. If they closed, upwards of 70 jobs would be lost. Centralisation of the HQ at Dewsbury could lead to 5-10 redundancies amongst technical staff plus any generalists who, cannot be found other civil service posts. All we can say is that the job prospects for all these staff are better if there is a sale, and that it would be difficult for the Government to justify itself making redundant the staff of a business which, overall, is profitable, at least before financing costs.

The third key consideration is the ability of the prospective purchaser to run the business. The bid is a joint one from a team of TCS staff (3 civil servants and one working under contract for TCS) and from SME, whose Chairman will chair the board of the new company. SME are subscribing more for shares than the TCS staff, though the TCS staff team plus the managing director (yet to be recruited) will have initial control of the company. SME would take control after 5 years if their preference shares cannot be redeemed and are converted. In addition to the Chairman and the non TCS MD, a sales director, deputy finance director and workshop director have to be recruited. The majority of the management team will not be ex civil servants and any sale will not therefore be to an MBO. The presentational disadvantage of this is, however, outweighed by the strengthened management capability promised by SME's involvement.

In sum, I should like your agreement to proceeding with this deal. There is a respectable financial case for it, and it provides the prospect of jobs for some staff as well as the continuation of a business on which PSAs and OGDS, presently rely. Completion of the deal will have to be conditional on the satisfactory new management appointments, endorsed by Samuel Montagu and Company, as well as negotiations on the legal documentation.

The financial backers' are looking to complete the sale by the end of March 1991. This already looks extremely optimistic, but it is clearly important to proceed as quickly as possible so as not to prejudice the deal.

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ACT 2000



Young/Financial Sec. 4/2/91

A Parliamentary announcement would accompany exchange of contracts. My officials would, of course, clear the text of any announcement with yours.

I am copying this to the Prime Minister.

I would be most grateful if you would let me have a response by close of play on Wednesday 6 February.

Yours sincerely

B. Houlder.

SP
SIR GEORGE YOUNG
(Approved by the Minister
and signed in his absence)

Financial Secretary



CIVIL SERVING: PSA PT4



Minister for Local Government
and Inner Cities

2.5 P.M.
BHP 26/11

Department of the Environment
2 Marsham Street
London SW1P 3EB

Telephone 01-276 3000

26 November 1990

per Francis

The Prime Minister's agreement to the proposed management buy-out of the Crown Suppliers' Transport and IDS businesses was recorded in her Private Secretary's letter of 11 September.

Since then the team have withdrawn their bid for the IDS. There were a number of contributory reasons for this, including doubts about the company's future when the Government re-tendered the IDS contract in no more than 3 years time, and concern about the impact of the Post Office's letter monopoly on their ability to expand the business. These difficulties might have been overcome. But the determinative reason was the withdrawal of the General Manager of the IDS from participation in the team. My officials have kept yours in close touch with events.

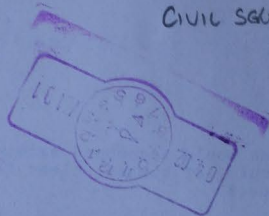
The team have put in a revised bid for the Crown Suppliers' transport business alone. My officials are discussing its details with yours. This revised bid seems reasonable on the face of it, but the team are awaiting confirmation of finance from their proposed backers, Sanderson Murray & Elder (Holdings) plc, National Westminster Bank and Lombard North Central. It may therefore take some weeks before I am in a position to put a proposal to you.

As to the IDS, there was only one other bidder for it, the National Freight Corporation. Their offer was unattractive and their pension scheme inadequate. Sale of the IDS to the NFC was therefore one of options rejected in the officials' paper which we considered last summer. There is therefore little option but to abandon the privatisation of IDS. Closure of IDS and contracting it out to another private operator is unlikely to be possible, at least in the short term, given the impact of the Post Office letter monopoly. In the short run, at least, I believe that the only option this leaves us with is retention of the IDS in Government. Property Holdings is the obvious location, because the management of the IDS fits well with the other functions it has taken over from PSAs. Our officials will need to discuss the vote and running costs implications of this transfer.



recycled paper

CIVIL SERVING: PSA PT4



Minister for Local Government
and Inner Cities

n.b. P.M.
Btp 26/11

Department of the Environment
2 Marsham Street
London SW1P 3EB

Telephone 01-276 3000

26 November 1990

Mr Francis

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recycled paper

I am under considerable pressure to let the staff know the position on the IDS. Until I do, firm plans for its future cannot be made, and the MBO team cannot be open with staff about their intentions. Furthermore, rumours are rife that the MBO has withdrawn its bid for both businesses and that both IDS and the transport business are to be closed. This is having a serious effect on morale and on the performance of the transport business, which we still hope to sell. We have reached the position therefore, where I believe that staff must be told that a bid for the transport business is still being discussed but that IDS is not being sold. I propose to make a parallel announcement to Parliament by way of written answer. I attach a draft. I should be grateful for comments by close of play on Wednesday 28 November.

I am sending copies of this letter to the Prime Minister and to Peter Lilley.

Yours etc

Michael.

MICHAEL PORTILLO

The Hon Francis Maude MP



TCS PRIVATISATION

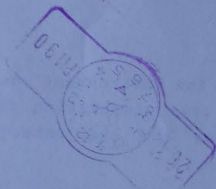
DRAFT PQ AND ANSWER

To ask the Secretary of State for the Environment when he expects to announce the outcome of the sale competition for the Crown Suppliers' vehicle hire business and the Inter-Departmental Despatch Service.

Discussions are continuing on the sale of the Crown Suppliers' vehicle hire and maintenance business. An announcement will be made as soon as possible. There are no acceptable bids for the Inter-Departmental Despatch Service, which will, therefore, be retained in Government.



CS: PSA pr 9



chex.jp/kg/14

CONFIDENTIAL



Treasury Chambers, Parliament Street, SW1P 3AG
071-270 3000

18 October 1990

Barry Potter Esq
Private Secretary to the
Prime Minister
10 Downing Street
LONDON
SW1A 2AA

Dear Barry

PSAS PRIVATISATION

The Chancellor has seen your letter of 8 October to Phillip Ward, and the earlier correspondence on this subject.

Officials here are taking forward the necessary work with colleagues in Property Holdings, PSA Services and the Ministry of Defence principally, consulting others as necessary. The main priorities are to complete the analysis of the arguments for and against slowing down the untying exercise (which indeed seems unattractive on the basis of work done so far); to pursue the points raised by the Defence Secretary in his letter of early October, taking in the issue of the future of PSAS' work overseas for the MOD; and to take forward the study of the "managed disposal" option, taking account of Departments' requirements for support from PSA Services.

The Financial Secretary will be pursuing these issues where appropriate with colleagues, and the Chancellor will take a close interest in the work and report back as the Prime Minister has asked.

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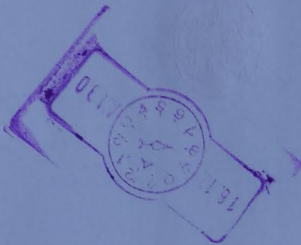


I am copying this letter to the Private Secretaries to members of the Cabinet, to Philip Rutnam (Financial Secretary's Office), to the Private Secretary to the Minister for Arts and Libraries, and to Sir Robin Butler.

Yours

Kate

MISS K GASELTINE
Assistant Private Secretary



CIVIL SERVICE:
PSA Restructuring
Pt 4



ST. ANDREW'S HOUSE
EDINBURGH EH1 3DG

cfpp
n.b. P.M.
BHP
22/10

The Rt Hon Christopher Patten MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

16 October 1990

Dear Chris,

PSA SERVICES : PRIVATISATION

at Patten

Thank you for sending me a copy of your letter of 18 September to Norman Lamont on the latest developments in your plans for the privatisation of PSA services and the creation of a Government-owned company. I note with interest that you propose to adopt Cooper and Lybrand Deloitte's recommendation that PSA's two core businesses should be treated as separate entities and that this has prompted you to think in terms not only of disposing of them separately but of creating more than one Government-owned company.

While deferral of the operative date from 1 April 1991 to 1 July 1991 will, to some extent, help the Scottish Courts Administration in their work of re-negotiating agreements with PSA, the timetable remains very tight for that Department. I referred to the impact on the Scottish Courts Administration in my letter of 19 June. I see no difficulties in the proposed timetable for the Scottish Office or my other minor Departments.

Your letter sheds no further light on the PES implications of what is proposed. I must reiterate the concern I have that whatever arrangement is finally agreed there should be no reduction in the amount of resources available to Departments for the provision and maintenance of accommodation.

*cc to Prime Minister
Cabinet Colleagues
Financial Secretary
Sir Robin Gutter*

*Yours ever,
Malcolm Rifkind*

MALCOLM RIFKIND

PCC00109.100



CIVIL SERVICE

: PSA Restructuring Pt4

CONFIDENTIAL



10 DOWNING STREET . .

LONDON SW1A 2AA 8 October 1990

From the Private Secretary

Dear Philip,

PROPERTY SERVICES AGENCY SERVICES (PSAS): PRIVATISATION

The Prime Minister has seen a copy of the Environment Secretary's minute of 18 September to the Chief Secretary, setting out his proposals for the next steps towards privatisation of PSAS. The Prime Minister has also seen copies of the letters from the Financial Secretary (2 October) and the Defence Secretary (undated) on this subject.

In the light of the consultants' report, the Prime Minister views with concern the proposal to set a target date for incorporation of PSAS into one or more Government-owned companies (GOCOS) as a prelude to privatisation. The Prime Minister is also opposed to slowing down the untangling exercise in order to secure a higher continuing level of business for PSAS.

The Prime Minister agrees with the Financial Secretary that it would be premature to establish a target date for GOCO status at this stage. She also agrees that further work on the managed disposal options is necessary, so that, for the different parts of the PSAS business, the relative merits of sale, retention within Government and closure are thoroughly examined.

The Prime Minister would be most grateful if the Chancellor (who has of course overall responsibility for the privatisation programme) could take a close interest in these further studies of the way forward for PSAS and report back as appropriate.

I am copying this letter to the Private Secretaries to members of the Cabinet, Philip Rutnam (Financial Secretary's Office), and to Sir Robin Butler.

Yours ever,
Barry

BARRY H POTTER

Phillip Ward Esq
Department of the Environment

CONFIDENTIAL

PSA SERVICES (PSAS) PRIVATISATION

PSAS comprises two main businesses: project design and management and building maintenance. Proposed privatisation of PSAS is in serious difficulty.

The Government is committed to privatising PSAS: the Act has received Royal Assent. But PSAS is performing very badly. And a recent consultant's report concludes that, as a company, PSAS probably has negative net worth, if sold in the next few years.

There are two fundamental problems.

- i. PSAS is simply an inefficient, badly run organisation.
- ii. Departments were untied from using PSAS earlier in the year. As should have been foreseen, there has been a great rush to dispense with poor PSAS services and to buy from the private sector.

The result is that on any sensible commercial criteria PSAS has no viable future.

Against that background, Mr Patten (flag A) nonetheless proposes turning most of PSAS into one or more Government-owned companies in preparation for sale; and, to stem the haemorrhage of lost business, to slow down progress on untying.

By contrast, the Treasury (flag B) argue that it is necessary to face up to the problems in PSAS. The option of closure needs to be carefully and quickly costed (though it could involve considerable redundancies). And there is no logic in slowing down the process of untying.

Conclusion

Having committed itself to privatising PSAS, the Government will only achieve this now by large injections of subsidy to make the company attractive to potential purchasers. The political case for doing so, having taken the necessary legislation, is clear; but it does not make economic sense.

E.R.

CONFIDENTIAL

- 2 -

As activity in the construction and related industries slows down, the private sector will compete more vigorously for business released by untying Government departments from PSAS. It is difficult to believe that the financial situation at PSAS can improve. Whatever the political difficulties, both Treasury officials and Policy Unit (flag C) may well be right to conclude that closure may be the best option.

This cannot be simply resolved. There is a serious difference of view between DoE and Treasury. As the letter from the MoD (flag D) shows, the matter has been badly handled.

Further work on options is needed to include the following.

- (i) Closure of all or part of PSAS: what would be the costs of managed rundown; how large would the redundancies be?
- (ii) Retention of PSAS within Government: might this make sense for at least the MOD-related work on missile sites etc?
- (iii) Privatisation: how much injection of public funds might be needed to make the PSAS saleable?
- (iv) Is the best approach a mix of (i)-(iii) above?

The next step might be to call together relevant Ministers. You could do this yourself. Alternatively you might ask the Lord President or the Chancellor to investigate and report.

- i. Content to chair a small meeting yourself?
- OR
- ii. Content to ask the Lord President/Chancellor to consider and report back to you?

BHP

BARRY H POTTER

5 October 1990

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Yes - agree
very much with
Francis P. Randle.
not

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PRIME MINISTER

4 October 1990

PSA SERVICES PRIVATISATION

This is running into trouble. It looks as though the original consultants' advice which informed the decision to privatise PSA Services (PSAS) was over-optimistic. A recent and detailed report by Coopers and Lybrand is much gloomier about the prospects of being able to sell the organisation either as a whole or in parts. Things have got worse since your VFM Seminar in March.

Despite Coopers' advice, Chris Patten proposes to continue on the assumption that most of PSAS will be sold. Francis Maude argues for a hard-headed look at other options such as closing down large parts of PSAS.

The Treasury are right to be alarmed. There is a real risk that privatising PSAS could become a costly business, with taxpayers' money needing to be pumped in to make it look attractive to buyers. In the end this option could cost more than closure, despite redundancy costs.

BACKGROUND

- E(A) decided in September 1989 that early privatisation (1992-3) was likely to be the best course for PSAS. This was a speeding up of the earlier timetable. Nicholas Ridley was keen to get rid of PSAS.
- The Civil Service/Price Waterhouse report argued that

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PSAS' likely loss of Government customers as a result of untying made it sensible to try to sell it sooner rather than later. (Earlier advice had suggested that PSAS should operate for a few years as a trading fund before attempts were made to sell it.)

- The necessary legislation (the PSAS and TCS Privatisation Act) has received Royal Assent.

Coopers' Report

Last May the Department of the Environment commissioned a report from Coopers on prospects for the sale of PSAS. The report points out that:

- (a) unlike some earlier privatisations, PSAS has virtually no fixed assets which might have alternative use values;
- (b) again unlike some earlier privatisations, PSAS no longer, since untying, enjoys a position as a monopoly supplier of essential services;
- (c) there is at present very considerable uncertainty - much greater than typical levels of commercial uncertainty - about the future extent and composition of market demand and hence the level of workload and earnings;
- (d) nonetheless, against any foreseeable demand scenario:
 - (i) PSAS will have to reduce significantly the scale of its operations, perhaps by more than 50% because of untying and reduced defence involvement

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in Central Europe (MOD is by far the largest customer);

- (ii) there will be significant consequential restructuring costs, of upwards of £500m;
- (iii) the timepath to achieving a commercial return in the remaining business is highly uncertain.

Against this background, Coopers conclude that PSAS would probably have negative net worth if sold in the next few years.

Coopers pull their punches when it comes to recommendations. No doubt they felt that privatisation rather than closure was a foregone conclusion. It is the gap between their specific recommendations - such as treating the two main businesses separately - and their pessimistic analysis above which allows Chris Patten and Francis Maude to read the report differently.

Chris Patten's Proposals

Chris Patten proposes:

- separating the two main PSAS businesses (Projects and Business Management) as Coopers propose. This would probably lead to them being sold separately;
- assessing the cost of closing down PSAS at least cost to Government (but this is only suggested as a benchmark against which to measure other options);
- reining back the untying exercise (this would help to keep a captive customer market for a while);

No
3

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- turning most of PSAS into one or more Government owned companies (GOCOs) by 1 July 1991, in preparation for eventual sale;
- incorporating the international business into one of the two main businesses (Coopers suggested incorporating it into the Ministry of Defence).

Francis Maude's Reaction

Francis Maude argues:

- that it is necessary to face up to the gloom in Coopers' report. There will be huge problems in disposing of the PSAS given its present inefficiencies and the uncertainty surrounding its business as potential customers disappear;
- the priority task is costing closure, at least cost to Government (described as the "managed disposal" option). This is not just to provide a benchmark, but because closure may be the best option for large parts of PSAS;
- slowing down the process of untying would be a mistake. (Actually it would be so unpopular in Whitehall - where Departments are relishing their new found freedom from PSA - that it would probably be unworkable);
- it would be premature to set a target date for incorporating PSAS as one or more GOCOs until we know whether the core businesses are saleable in the foreseeable future;

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- incorporating the international business into one of the two main businesses is not necessarily the best course. Tom King should be asked about bringing it into the Ministry of Defence.

COMMENT

Basically Chris Patten and his officials want to steam on with privatisation as before. This is not surprising. It is likely that most people in PSAS - certainly its senior management - would prefer to be privatised than closed down.

The cost of steaming on could be large and open-ended, while closure has at least a maximum cost (100 per cent redundancies) which can be calculated:

- the cost of closure would almost certainly be less than 100 per cent redundancy because some people will transfer elsewhere in the Civil Service, and some will leave before they are made redundant. Whitehall should be galvanised to think about the scope for absorbing PSAS staff now, to reduce the cost of managed closure;
- the Value for Money Seminar on PSA last March showed what a long way PSAS have to go to become an efficient organisation. The cost of restructuring to make PSAS commercially attractive could not be passed on to prospective buyers.

Tom King has also written to say that his Department need to be closely consulted, as PSAS' biggest customer. (They have apparently not yet seen the Coopers' report). It is obviously sensible for them to be brought in.

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CONCLUSION

PSA have long been so inefficient that its customers - the rest of Government - are mostly desperate to be untied from it. It is not surprising that its market prospects look pretty bleak - especially with the uncertainties about the defence programme.

If Departments can manage without PSAS arguably its services are just not needed. Nothing of comparable size exists in the private sector. The logic of this argument is closure of large parts, if not all, of PSAS (some bits with assured Ministry of Defence custom probably could be sold). Colleagues should be encouraged to face up to this now.

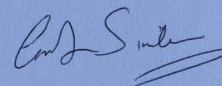
A final decision cannot be taken until we have a costed scheme of closure at least cost to Government. Coopers are confident that "managed" closure would cost the taxpayer less than immediate closure. Costed closure schemes should be ready in January. We must press for this timetable to be kept.

RECOMMENDATION

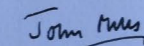
- Express concern at the difficulties of privatising PSAS highlighted in the Coopers' report.
- Warn that the issue must not be allowed to drag on.
- Agree with Francis Maude that it will be necessary to take a hard-headed look at options such as significant closures.
- Press to have a costed scheme of managed closure as a basis for decisions as soon as possible. Can it be ready earlier than January?

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- Redeployment of PSAS staff within the Civil Service will reduce the cost of closure options. There should be a quick co-ordinated exercise within Government, in parallel with the scheme for managed closure, to see what scope there is for redeployment. (Robin Butler could be asked to take this on).
- Meanwhile it would be wrong to slow up untying. And it is premature to set a target date for GOCOs at this stage.



CAROLYN SINCLAIR



JOHN MILLS



MINISTRY OF DEFENCE WHITEHALL LONDON SW1A 2HB

TELEPHONE 01-218 9000

DIRECT DIALING 01-218 2111.3

MO 10J

October 1990

D. Norman

PSA SERVICES PRIVATISATION

I read with interest Chris Patten's letter of 18 September.

I cannot comment on the consultants' conclusions, not having seen their report, but a number of the points in Chris's letter are of direct interest to MOD, as PSAS's largest customer. For example:

- the timetable for privatisation of the two businesses;
- the alternative notion of running them down while they remain in Government;
- the possibility of a change in the rate of untying;
- the suggestion that value for money from works expenditure should be balanced against redundancy costs; and,
- the suggestion that there should be adjustments between Departments' PES programmes to provide working capital for a GOCO.

The Rt Hon Norman Lamont MP
Chief Secretary



As I said in my letter of 21st June to Chris, I could not accept that the redundancy bill should be passed to customer departments. I should also like to know what is likely to be proposed for those parts of PSAS that are not candidates for privatisation. In my letter of 21 June, I put down a number of markers on points of key importance from the customer's point of view that need to be resolved before progress towards PSAS incorporation passes the point of no return. Against that background, I am extremely surprised that as the leading customer, I have not been consulted about the proposals to emerge from the consultants' report. That is not how business behaves.

For these reasons, it is very important that there should be the closest consultation before decisions are taken: I hope that you and Chris Patten will agree that our officials should get together at once to go through these and other points. It will, I believe, be important for my officials to see those parts of the consultants' report that bear on MOD; it will be difficult for them to advise me if they do not. In the meantime nothing should be done to slow down the speed at which work is put out for competitive tender.

I am copying this to the Prime Minister, Cabinet colleagues and to Sir Robin Butler.

Tom King



COMMERCIAL AND MANAGEMENT IN CONFIDENCE

2 MARSHAM STREET
LONDON SW1P 3EB
071-276 3000

My ref:

Your ref:

The Rt Hon Norman Lamont MP
Chief Secretary
HM Treasury
Parliament Street
LONDON
SW1

18 September 1990

Dear Chief Secretary

PSA SERVICES PRIVATISATION

I have now received from Coopers and Lybrand Deloitte (CLD) the report of their feasibility study on the privatisation of PSA Services. I think we can now make progress on the questions of early GOCO and my PES bid.

I propose to accept CLD's key conclusion that we should treat as separate entities the two core businesses they have identified - "project design and management" and "maintenance management" - and that the existing businesses should be restructured in line with this. This will involve inter alia incorporating parts of the existing International and Specialist Services businesses into the present Projects and Building Management businesses.

The fact that CLD see no synergy between these two core businesses suggests that we need not plan to sell them as one. Moreover, CLD see a more easily realised, albeit difficult, path to viability for "projects" than for "maintenance management." We will therefore be developing a strategy for disposing of each business at the most appropriate time so as to give the best overall return to the public purse; this may, of course, be well before October 1992 which we have hitherto seen as the earliest practicable date.

An early stage of the work will be determining a benchmark against which to assess sale options and, eventually, bids. This involves assessing the costs of running down the businesses at least cost while they remain in Government.

An important underlying component of any forward plan is an estimate of the level of work PSAS will get from customer Departments. The rate at which Departments are putting work out to tender is much faster than we anticipated when the decision to "untie" was taken. I



have no doubt that that decision was right but I wonder whether the way in which it is being handled will provide the best overall outcome in public expenditure terms. My officials have taken up your suggestion that we look again at this and at the balance between seeking greater vfm from works expenditure and consequent redundancy costs. My officials will shortly be in touch with yours about it.

I believe that incorporation as one or more GOCOs well before sale would be advantageous, provided we are confident that the businesses are viable and sustainable. We are not yet able to make a final judgement on that. But I do not think we can postpone a decision to get ourselves into a position to incorporate because of the risk that that will, in itself, delay the much needed changes. Although 1 April 1991 now looks too soon, I would like to adopt a slightly later target date of 1 July 1991, subject to reviewing the position nearer that date and, above all, being confident that the businesses are viable.

You will realise that until we have got new PSAS business plans, a benchmark for assessment and a disposal strategy - which will not be ready until about March - I can only make a provisional bid for PES provision for redundancy costs or working capital for a GOCO. Yet when we have identified the most advantageous strategy, it will need the resources to implement it quickly, or I may be forced to adopt less than the best strategy.

In the circumstances, I propose that we should make provision for redundancy costs, which are as you recognise inevitable and whose timing alone is at issue, at the "worst case" level. This will be an unpalatably high figure. I have decided that we will offer secondment to staff where possible in order to reduce redundancies. Even so, it will be of the order of £90m in 1991-2 alone. We have every incentive to try to reduce it. We can consider managing the rate of untying. We must do everything possible to redeploy surplus staff elsewhere in Government and we must evaluate carefully the overall cost of all sale options. If redundancy costs are lower than we have allowed for, the additional provision would have surrendered.

As to working capital (perhaps £150m), we do not yet know when we shall need it. That can only finally emerge from our sale strategy. We do know we shall not need it at 1 April 1991. As you know, I believe that making provision for it should be PES neutral. I do not therefore propose to make a bid. When we do establish a GOCO, there will need to be adjustments between Departments' PES programmes to reflect this.

A third part of any PES bid will need to cover certain costs which we should not expect PSAS to recover through charges. I have in mind the continuing cost of activities such as Vote accounting and also restructuring costs arising from the implementation of our move towards privatisation. If their charges have to cover these costs they simply will not win work. If we bear those cost directly now, PSAS stand a much better chance and we will get a higher price from



RECYCLED PAPER

the sale. Indeed, I think we should regard these as costs to be set against the sale proceeds in due course.

I am copying this letter to the Prime Minister, Cabinet colleagues and Sir Robin Butler.

CEP Bush

pp CHRIS PATTEN

(Approved by the Secretary of State
and Signed in his Absence)



CONFIDENTIAL

CCFO
B

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Christopher Patten MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
London SW1P 3EP

2nd October 1990

Dear Secretary of State.

PSA SERVICES PRIVATISATION

Norman Lamont has asked me to reply to your letter of 18 September.

I am sure that you are right, in the light of Coopers' report, to treat PSAS's two core businesses as separate entities, to restructure the businesses accordingly and to plan on the basis that the businesses be disposed of separately. But there are extremely difficult decisions to be taken in the coming months. The Coopers' report demonstrates the scale of the problems of disposing of PSAS amidst the uncertainties which it faces and of the prospects for its constituent businesses. There is clearly much to be done to make Projects and Building Management into viable units, and it is likely that privatisation would be possible only at significant cost to the taxpayer.

Against this background it is essential to work up the "managed disposal" option, as you suggest. I understand that this should be ready by around January. When this work is ready we shall need to take a hard-headed look at the options. These could include significant closures as well as early sale or retention of parts of the business within Government (perhaps in the form of an Executive Agency) if that course holds out a good chance of turning parts of the PSAS round in two or three years' time. I should be happy to discuss these possibilities further with Michael Portillo at the appropriate time if you judged that helpful.

You mention that it will probably be desirable to incorporate parts of the existing International and Specialist Services businesses into the present Projects and Building Management businesses. We need quickly to decide on the best future arrangements for International and Specialist Services as a whole. I understand that Coopers saw advantage in the return of a large part of International to MOD. This course needs to be seriously investigated, and I should be interested to have Tom King's views on it. I hope we can complete this inquiry speedily, since it would be wasteful to continue investing in systems for this business on the assumption that it would continue to be a self-accounting unit within PSAS. For the same reason, I hope that

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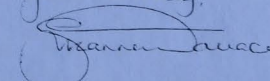
proposals for the division of Specialist Services between the two core businesses and on the issue of whether a substantial part should be separated for retention in Government, will be brought forward quickly.

It would be premature to attempt to reach a firm view on untying until officials have completed the work on this subject to which you refer. But I would be very reluctant to make any substantive change in the policy of untying, just as Whitehall is focussing on its attractions and advantages.

I think it would be unwise now to set ourselves the target date of incorporating PSAS as one or more GOCOs in the summer of next year. A Companies Act company must by definition be able to trade as a going concern and have sufficient assets to pay off its debts and other liabilities. But neither of the core businesses in PSAS appears to be viable at the present: we do not know when they will become viable, or what restructuring costs are likely to be necessary before attempts are made to sell all or parts of PSA Services. The right sequence is surely to establish our strategy towards the disposal of PSAS in the light of the further work on the "managed disposal" option, and to take decisions on incorporation, including the timetable for incorporation, in the light of that strategy. Moreover there must be serious doubt whether we would be in a position to incorporate PSAS as a GOCO by July. To set a target which we then failed to meet would be no help in our policy towards PSAS.

Norman Lamont will deal separately with your Survey bid, on which you touched in your letter but dealt with more fully in another letter of the same date. Suffice it to say that I note the case in principle for making some significant provision for severance; and that the public expenditure implications of providing working capital to a GOCO could in practice be quite awkward and would need careful work by officials. There would, as you say, have to be adjustments from customer departments' programmes in order to ensure PES neutrality.

I am copying this letter to the recipients of yours, and to Norman Lamont.

Yours sincerely,


FRANCIS MAUDE
 (Approved by the Financial Secretary
 and signed in his absence)

CONFIDENTIAL

JM



Minister for Local Government
and Inner Cities

n.b. P.M.
BHP 11/9

Department of the Environment
2 Marsham Street
London SW1P 3EB

Telephone 071-276 3000

PO/PSO/33774/90

11 SEP 1990

Dear Robert

Thank you for your letter of 17 August. My letter of 17 July to Francis Maude did make it clear that an announcement would have to be made very quickly following a decision to close the contract furnishing operations of TCS, and as you say, I announced the closure on 15 August.

Since the announcement our officials have been in touch about the effect of the closedown on the sheltered industries. Many of the contracts involve MOD, and we are looking at ways in which these can continue, either through transfer to The Buying Agency (TBA), which will remain within Government, or the establishment of some in-house capacity in MOD using TCS expertise. Final decisions have yet to be taken, and I can give no commitment; but continuance of these contracts would safeguard all the TCS contracts at the Enham Workshops (worth currently just over £2 million), and some £636,000 of contracts placed with Remploy.

For other contracts we intend to provide suppliers with the names and addresses of customers for their products, and it will be for contractors to market them directly. I understand that Remploy have already determined a marketing strategy which has won them one contract in competition with TCS among others.

All Government Departments are required to participate in the Priority Suppliers Scheme, which gives sheltered workshops and prison industries the chance to provide goods on a competitively priced basis. For contracts for goods which were previously supplied through TCS, the obligation to comply with the scheme will now rest with Departments themselves.



RECYCLED PAPER

Civil Service: Bs 174

Department of the Environment
14 September 1990

I have asked the officials charged with the closure of the TCS contract furnishing operation to keep in close touch with yours on developments which will affect the sheltered industries.

I am sending a copy of this letter to the Prime Minister, Geoffrey Howe, Tom King, Francis Maude and to Sir Robin Butler.

Yours ever

Michael.

MICHAEL PORTILLO



Robert Jackson Esq MP

COMMERCIAL IN CONFIDENCE



10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

11 September 1990

PRIVATISATION OF THE CROWN SUPPLIERS:
TRANSPORT AND INTERNAL DELIVERY SERVICE (IDS)

Your Secretary of State wrote to the Chancellor on 3 August proposing that the Crown Suppliers Transport and IDS services should be privatised by means of a management buy-out. The Chancellor's letter of 31 August indicated that he was content to proceed as proposed by your Secretary of State.

Subsequently I indicated that the Prime Minister wanted to be clear about the reasons for the changes in the Net Present Value figures in your Secretary of State's letter of 3 August from those contained in Mr Chope's letter of 13 June. Your letter of 6 September to me attached a note setting out the latest and better estimates prepared by your department's privatisation advisers, Coopers & Lybrand, Deloitte.

In the light of the figures attached to your letter of 6 September, the Prime Minister is content for the proposed management buy-out to go ahead.

I am copying this letter to John Gieve (HM Treasury).

BARRY H POTTER

Phillip Ward Esq
Department of the Environment

COMMERCIAL IN CONFIDENCE

PRIME MINISTER

CROWN SUPPLIERS PRIVATISATION:

TRANSPORT AND INTERNAL DELIVERY SERVICE (IDS)

Mr. Patten wrote to the Chancellor on 3 August (Flag A) about the privatisation of the Crown Suppliers transport and IDS services.

The letter provided revised Net Present Value (NPV) estimates of the three options: a management buy-out; closure; and closure of transport/IDS kept in public sector. Mr. Patten recommended the MBO. The Chancellor concurred.

Your manuscript note on my covering minute (Flag B) indicated concern about the change in the NPV estimates in the Environment Secretary's minute of 3 August, from those provided by the junior Environment Minister (Mr. Chope) on 13 June.

Accordingly I asked DoE to set out why the NPV figures had changed. The note is attached at Flag C. It is the work of the private sector consultants, Coopers & Lybrand, Deloitte.

The main points in the note are as follows:

- (i) The numbers of 13 June were point estimates of the NPV under the three options. The revised estimates provide a range of values, taking into account uncertainty and other factors.
- (ii) The 13 June point estimates are within the range of NPVs for each option quoted on 3 August: but they are not at the mid-point of the range now quoted.
- (iii) A number of factors have been taken into account in revising the NPV estimates. They reflect more information; more expert advice; and more allowance for uncertainty.

It was on the basis of the 3 August assessment that Mr. Patten concluded the management buy-out should go ahead. His view

reflects the benefit to the Exchequer of proceeding with the privatisation; the fact that the business is then likely to continue; and that, as a result, redundancies can be avoided.

Comment

The course proposed by Mr. Patten has obvious attractions in terms of continuing the privatisation programme and keeping the business going.

The concern must be whether the privatisation can be justified - not least to the accounting officer and in due course the PAC. According to the latest material it seems that it can because:

- the consultants advice is that the net present value is a positive sum within the ranges quoted for the other two options;
- it is the least uncertain and thus most secure course - it minimises risk; and
- it keeps business in being.

Content for the MBO to go ahead?

Or

Prefer to call together Treasury and DoE Ministers for a discussion?

BHP

(BARRY H. POTTER)

10 September 1990

c:\wpdocs\economic\Crown (srw)



CONFIDENTIAL

2 MARSHAM STREET
LONDON SW1P 3EB
071-276 3000

My ref:

Your ref:

6 September 1990

Barry Potter Esq
Private Secretary to
The Prime Minister
10 Downing Street
LONDON
SW1A 2AA

Dear Barry

CROWN SUPPLIERS PRIVATISATION: TRANSPORT AND IDS

We spoke the other day about a query raised by the Prime Minister on my Secretary of State's letter of 3 August. As a result I volunteered you a note giving the reasons for the changes in the cost figures contained in Mr Chope's letter of 13 June.

A note is attached which has been prepared on advice from our privatisation advisors Coopers & Lybrand Deloitte. In essence these are simply later and better estimates prepared by our advisors, reflecting their more detailed consideration and the inevitable range of uncertainty attaching to the various options.

Please let me know if you would like any further information.

Yours
Phillip

PHILLIP WARD
Private Secretary

THE CROWN SUPPLIERS' PRIVATISATION: TRANSPORT AND IDS

1. This note gives a brief explanation of why the figures for the three options for Transport and IDS evaluated in the Secretary of State's letter of 3 August 1990 to the Chancellor are different from the figures for the same options in Mr Chope's letter to the Financial Secretary of 13 June.

	£M	
	13 June	3 August
Bid		
Liquidate Transport and IDS	11.8	11 - 12
Liquidate Transport	15.7	9.4 - 15.9
and retain IDS	17.5	10.6 - 20.4

2. The first set of figures were prepared by Coopers and Lybrand Deloitte as rough estimates to help evaluate bids for the two businesses. No 10's request that the justification for proceeding with the management buy out should be considered in the light of a comprehensive and fair appraisal of the options led to Coopers and Lybrand Deloitte being commissioned to do a more detailed examination of the options and to prepare a revised evaluation, in consultation with the firm's liquidations experts. The figures in the 3 August letter and its attachments are the result.

3. Coopers and Lybrand Deloitte identify the principal reasons for the changes as follows:-

- (i) more information, particularly in relation to the vehicle fleet, was made available to them;
- (ii) they were authorised to speak to key officials, especially to the ex-General Manager of Transport;
- (iii) they took advice from liquidations experts on the valuation of assets and liabilities;
- (iv) they made a more detailed estimate of the likely losses of the transport and IDS businesses in the close-down period;
- (v) generally, they reflected the uncertainty about the outcome by giving a range of figures for each option.

TCSPU
5 September 1990

PRIME MINISTER

CROWN SUPPLIERS PRIVATISATION: TRANSPORT AND INTERNAL DELIVERY SERVICE (IDS)

You may recall that my note of 6 July (attached at Flag A) indicated discussions were underway on the privatisation of the three businesses within the Crown Suppliers:

- Transport;
- IDS;
- Furniture.

Since then, arrangements have been put in place to close the furniture business, because it cannot sensibly be sold.

(Mr Turnbull's minute of 7 August - at Flag B).

My earlier note cautioned against accepting DoE proposals to privatise the other two businesses (Transport and IDS) on the basis of the information then available. At that time the figures showed that closure was a more economic option than any form of sale. Accordingly, I wrote to Mr Chope's Private Secretary on your behalf on 9 July asking him to reconsider the options.

Since then Chris Patten has taken over responsibility for this matter. His letter of 3 August (attached at Flag C) identified three options and revised considerably the assessed net present value of each (NPV):

- A: sale to a management buy-out (£11 to £12 million);
- B: closure (£9.4 to £15.9 million);
- C: closure of the transport business, combined with retention in Government of the IDS (£10.6 to £20.4 million).

Mr Patten concludes in favour of option A. First, it provides for certain privatisation and a small inflow of revenue to Government. Second, though the possibility of a subsequent closure of the business cannot be ruled out, it is unlikely

If we have that in 2011, we've no business selling it to the management at 11/12

that there would be immediate 'asset-stripping' by the new owners. Third, unlike options B and C, it avoids redundancies.

(Flag D)

The Chancellor's letter of 31 August/supports Mr Patten's proposed approach, subject to the privatisation proceeds figure not declining further. He is even prepared to accept that £2 million of the proceeds should be deferred for five years.

The revised figures on the net present value of the options make it possible to defend the MBO on purely financial grounds. The risk of fairly early closure cannot be ruled out: but the counter argument is that either of the other options would in any case involve partial or full closure.

Given the relatively small size of the business, that it is a management buy-out, (to which it is difficult to object on political grounds), and that the NPV of the MBO is not significantly different from the other options, it seems a sensible basis for going ahead.

Content to proceed with the MBO for the Transport and IDS businesses of the Crown Suppliers?

BHP

BARRY H POTTER

3 September 1990

*This sounds like
a better alternative. Why*

the sudden difference in figures?

nt

c:\economic\crown.eam



Treasury Chambers, Parliament Street, SW1P 3AG
071-270 3000

31 August 1990

Rt Hon Christopher Patten MP
Secretary of State for the
Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

For Chris,

TCS PRIVATISATION: TRANSPORT AND IDS

Thank you for your letter of 3 August.

I have looked at this matter very carefully with Francis Maude and we both have concluded that the balance of argument favours your recommendation to pursue negotiations with the MBO team. While the financial considerations point towards closure, their evidence is not decisive and subject to the Prime Minister's views, I believe that the other arguments you adduce justify attempting to reach a settlement with the MBO team on the basis of their offer. However, I must enter the caveat that if the likely price should be reduced in further talks we should need to look at that again.

You sought my views on deferred consideration. There is little to choose, in terms of net present value, between the two options. I suggest you take the alternative of £2 million deferred for 5 years, which has less of the appearance of a loan from the vendor. I assume that Property Holdings would be responsible for collecting the deferred payment when due.

I am conscious of the risk to which Peter Lilley drew attention, namely that if the MBO team or their backers saw a chance of realising the optimistic end of the asset valuation of the business they might proceed to attempt to do so. But I am content to accept your advice that this can be ruled out as implausible.

COMMERCIAL IN CONFIDENCE



I also accept that there is no practical way of safeguarding against this risk, short of going for closure ourselves.

I note that our officials will be in touch over the terms of any announcement.

I am copying this letter to the Prime Minister and to Peter Lilley.

Yours Truly,
J. Major

JOHN MAJOR

CIVIL SERVICE: PSA
Review
A?



Minister for Local Government
and Inner Cities

n. b. P.M.
BHP 3/18

Department of the Environment
2 Marsham Street
London SW1P 3EB

Telephone 071-276 3000

30 AUG 1990

Dear Kenneth

Thank you for your letter of 9 August about The Crown Suppliers (TCS) contract furniture business. As you will know, I announced the closure of the business on 15 August.

One of our main tasks in making arrangements for the disposal of the work currently carried out by TCS will be to find a home for contracts involving MOD. As you suggest, the most promising avenue appears to be a capacity within The Buying Agency (TBA), and we are looking at this as a matter of urgency.

The future of the user rights in furniture and other specifications held by TCS is one of the matters which will have to be decided very quickly. There should be no difficulty about items which are specific to MOD requirements; but we will need to be satisfied that any commercial value attaching to TCS property rights is properly considered in deciding how best to dispose of the assets of the business. We recognise, however, the major interest other Departments have in this question, and this will be one of the factors taken into account in coming to decisions.

My officials charged with winding down the TCS contract furnishing operation will keep in close touch with yours during the process.

I am copying this letter to the Prime Minister, Michael Howard, Geoffrey Howe, and to Sir Robin Butler.

Yours ever

Michael.

MICHAEL PORTILLO



Kenneth Carlisle Esq MP

CIVIL SERVICE: BA Review
Pt 3



COMMERCIAL IN CONFIDENCE

MR POTTER

21 August 1990

PRIVATISATION OF PSA

1. This is running into trouble. The Treasury are getting very cold feet about going ahead. I think they may be right. I am sending you this minute by way of background in case the issue comes up in September while I am away (back on 19 September).

BACKGROUND

- 2. - E(A) decided last September that early privatisation (1992-93) was likely to be the best course for PSA services (PSAS). This was a speeding up of the earlier timetable. Nicholas Ridley was very keen to get rid of the PSA. The Prime Minister apparently shared his enthusiasm.
- The decision was taken on the basis of a joint Civil Service/Price Waterhouse report. The report argued that PSAS' likely loss of Government customers as a result of untying made it sensible to try to sell it sooner rather than later. (Earlier advice had suggested that PSAS should operate for a few years as a Trading Fund before attempts were made to sell it).
- The decision to privatise was announced on 27 September 1989. The necessary legislation (the PSAS and TCS Privatisation Act) has now received Royal Assent.

EMERGING PROBLEM

3. Last May the PSA Privatisation Unit in the DOE commissioned a report from Coopers on prospects for the sale of PSAS. Although we do not yet have the final report (expected in early September) it is looking very gloomy. Key points likely to emerge are:

COMMERCIAL IN CONFIDENCE

- parts of PSAS are not saleable (eg its International business which is really part of MOD). This in itself does not matter much. It would be possible to keep certain functions in Government;
- but the prospects for its main businesses (Projects and Building Management) look pretty dreadful. Business is expected to fall (largely as a result of untying) to between one third and one quarter of the present level by 1995-96. The bottom line, before tax and restructuring is estimated to lie between a profit of 1% of turnover and a loss of 10% of turnover;
- MOD's plans, and recent developments in central Europe, are a major source of uncertainty. MOD accounts for 70% of Projects, and 60% of Building Management business.

4. Given that PSAS is an overmanned and inefficient organisation, redundancy costs are inevitable whatever happens. The gloomy scenario above means that it may be cheaper to close most of PSAS down than to pay someone to take it away.

NEXT STEPS

5. You may imagine that all this is greatly exercising the Treasury. Because large scale redundancies in PSAS look likely whatever happens, it is regarded as immensely sensitive and I have been asked to speak only to named interlocutors. All of them are on leave, whether in the Treasury or DOE. So my judgement is based only on the papers which David Bostock has sent me. But I must say that the case for not going ahead with privatisation now looks pretty strong.

6. However, we are in a pickle:

- we have announced privatisation;
- we have passed the necessary legislation.

COMMERCIAL IN CONFIDENCE

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NEXT STEPS

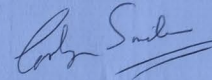
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6. However, we are in a pickle:

- we have announced privatisation;
- we have passed the necessary legislation.

COMMERCIAL IN CONFIDENCE

7. Treasury Ministers will be nervous of reopening such a major decision, especially given the Prime Minister's earlier enthusiasm. But I think officials will press them to do so once Coopers' final report is available.



CAROLYN SINCLAIR

KS



Department of Employment
Caxton House, Tothill Street, London SW1H 9NF

Telephone 071-273 5804/5
Telex 915564 Fax 071-273 5821

Parliamentary Under Secretary of State
Robert Jackson MP

n. s. p. m.
RHP
3K

Michael Portillo Esq MP
Minister of State
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

17 August 1990

Dear Michael

PRIVATISATION OF THE CROWN SUPPLIERS: FURNITURE BUSINESS

Thank you for the copy of your letter of 27 July to Francis Maude. I have seen his reply of 8 August, and also the letter dated 7 August from the Prime Minister's Private Secretary. I am writing to you in Nick Ullswater's absence and am sorry that we were not in a position to reply to your letter before the announcement you made about the Crown Suppliers Furniture Business on 15 August.

As you recognised in your letter, sheltered industry, which with the support of my Department provides employment for people with severe disabilities, is a major provider of furniture for the Product Supply and Services Division (PSSD). We shall need to ensure in implementing the decisions that you have announced that the interests of the disabled labour force should be properly looked after. I have no up to date comprehensive information about work undertaken by sheltered industry for PSSD, but in 1988/89 sales were worth about £10m. That represented, I understand, some 9% of purchases of furniture and furnishings by the Crown Suppliers, and about 7% of the total turnover of all sheltered factories and workshops. The volume of sales will have fallen since that time, but these figures give some indication of the scale of the problem that sheltered factories and workshops will be facing as a consequence of the changes you have announced. One or two enterprises face particular problems because of their high dependence of work for the PSSD.



Employment Department - Training Agency
Health and Safety Executive - ACAS

It will not be easy to adjust to the scale of change involved here. However, the ease with which the enterprises involved will be able to adjust to the implications of the decision to close PSSD will depend upon individual circumstances. All those affected will need reasonable time within which to rearrange their affairs particularly if large capital investment is required, and I am assuming that you will want to be as helpful as you can in this respect. Sheltered industry has shown an ability in the past to adjust to quite major changes in the circumstances, and my officials are already in contact with the enterprises concerned to offer support, advice and where necessary money in finding new markets, or in making adjustments to their arrangements for selling and distribution.

My officials are already in touch with yours to ensure close co-operation in helping sheltered enterprises to make the necessary changes in their business arrangements.

I am sending a copy of this letter to the Prime Minister, Geoffrey Howe, Tom King, Francis Maude and Sir Robin Butler.

MANAGEMENT IN CONFIDENCE



Treasury Chambers, Parliament Street, SW1P 3AG

Trevor Beattie Esq
Private Secretary to the Minister for
Local Government and Inner Cities
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

14 August 1990

Dear Trevor,

PRIVATISATION OF CROWN SUPPLIERS; FURNITURE BUSINESS

Your Minister wrote to the Financial Secretary yesterday in reply to the latter's letter of 8 August.

In light of Mr Portillo's comments, particularly on the readiness of the management of TBA to respond positively to demanding targets for profitability and efficiency, the Financial Secretary is now content for your Minister to proceed as he proposes.

The Financial Secretary understands that officials are already in touch about the terms of the announcement, and hopes that it will be possible to take forward quickly the further work referred to in Mr Portillo's letter.

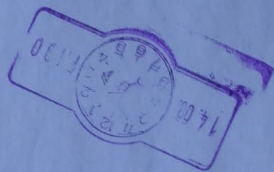
Copies of this go to Andrew Turnbull (No.10), Tim Sutton (Lord President's Office), Simon Webb, (Ministry of Defence), Martyn Wanning (Department of Employment) and Sonia Phippard (Cabinet Office).

Yours sincerely,
Philip Rutnam

PHILIP RUTNAM

MANAGEMENT IN CONFIDENCE

CIVIL SERVICES - PSA P3



MANAGEMENT IN CONFIDENCE



2 MARSHAM STREET
LONDON SW1P 3EB
071-276 3000

My ref:

Your ref:

13 August 1990

Dear Dominic

TCS PRIVATISATION: TRANSPORT/IDS

When we spoke on Friday last 10th August, you asked for a brief explanation of how the figures in my Secretary of State's letter of 3 August to the Chancellor could be reconciled with figures for the same three options for the transport/IDS businesses appearing elsewhere.

The figures in the 3 August letter are the same as those appearing in paragraph 12 of the officials' paper and paragraph 405 of the supporting paper by Coopers & Lybrand Deloitte which formed the attachments to that letter. They derive from a detailed evaluation of the alternatives which was commissioned as a result of the Prime Minister's request for further analysis of the options. The earlier figures appearing in Mr Chope's letter of 3 June cannot therefore be reconciled with the later ones but they do fall within the ranges given in the 3 August letter. Ranges are now given because the detailed analysis revealed a greater range of uncertainties than had been considered hitherto.

My Secretary of State's letter makes the important point that the figures, all of which carry some degree of uncertainty, need to be looked at in the light of other factors. The key points are that the sale option provides the most certain proceeds while the other two options both carry the presentational disadvantage of making redundant the employees of a viable business.

I hope this provides the clarification you require.

Yours

Kate

KATE BUSH
Private Secretary

CIVIL SERVICE!
PSA P63



Minister for Local Government
and Inner Cities

n. b. P.M.
ETP
3/9

Department of the Environment
2 Marsham Street
London SW1P 3EB

Telephone 071-276 3000

13 AUG 1990

Dear Francis

Alas
PRIVATISATION OF CROWN SUPPLIERS: FURNITURE BUSINESS

Thank you for your letter of 8 August. I welcome your agreement (and that of the Prime Minister) that the best option would be to close PSSD. I can assure you that every effort will be made to minimise costs and identify offsetting savings.

I am, however, disappointed that you are not yet satisfied that we should retain TBA. You say there is no need to keep TBA in the public domain. I understand from officials that MOD are concerned about the demise of PSSD, and that they will look to TBA not only for provision of current services but also for provision of such PSSD services, on a very limited and temporary basis, that cannot be readily procured elsewhere. Officials will need to discuss the practicalities of this proposal.

Coopers & Lybrand Deloitte's analysis of TBA profitability did note some outstanding issues. Resolving these and setting detailed financial targets will take some time. We cannot begin to do this until an announcement on PSSD is made and I do not believe it would be right to subject TBA staff to a further prolonged period of uncertainty. The existing management of TBA have taken significant steps to improve the standing and profitability of the Agency. They will I am sure respond positively to the demanding (but realistic) targets for profitability and efficiency that we shall set them. These targets will be subject to continuing review and if they failed to be met it would of course be open to us to consider again the future of TBA.

I am certainly prepared to agree that responsibility for TBA should pass to Property Holdings. We shall need of course appropriate PES and running cost cover to effect the transfer and to provide ongoing management: I hope some of this can be provided by transfers from PSAS.



On this basis I hope that you will agree that we should now as a matter of urgency decide to close PSSD and include in the announcement a statement of our intention to retain TBA in Liverpool.

Finally, I accept your point about the need to learn lessons from this exercise and my officials will be happy to discuss with yours how we might handle the post mortem.

I am copying this letter to the Prime Minister, Sir Geoffrey Howe, Tom King and Michael Howard and to Sir Robin Butler.



Yours ever

Michael.

MICHAEL PORTILLO

Civil Service
PSA P43

The Hon Francis Maude MP



MANAGEMENT IN CONFIDENCE



MINISTRY OF DEFENCE

MAIN BUILDING WHITEHALL LONDON SW1A 2HB

071 6666

Telephone 01-218 (Direct Dialling)

071

01-218 9000 (Switchboard)

PARLIAMENTARY UNDER-SECRETARY OF STATE
FOR DEFENCE PROCUREMENT

USofS(DP) 29/1/9

9 August 1990

Dear Michael,

You sent Tom King a copy of your letter of 27 July to Francis Maude about the future of elements of The Crown Suppliers (TCS) in the light of the outcome of the sale competition. I am replying on his behalf.

My officials have been able to discuss with yours the background to your letter, and we now have a clearer picture of the plight of the Product Supply and Services Division (PSSD) and the pressures for its early closure. However the PSSD is the vehicle through which most of the furniture and furnishings in the Services is procured. Under our longer term plans we expect alternative arrangements to be established by April 1992 following competition in the market, but an early closure of the PSSD would leave us in the lurch. This could lead to an extended break in the continuity of the supply for a range of items of day-to-day use within the Services, and that at what is already a difficult time for Service morale.

If indeed there should be no alternative to a PSSD closure, then I must look to you to establish a suitable capacity within The Buying Agency (TBA) to ensure the provision of a continuing furniture supply service to the Ministry. I understand that this might be achieved by the transfer from the PSSD to TBA of a small corps of furniture specialists to enable TBA to take on that part of PSSD furniture activity essential to the Ministry of Defence. Indeed should it be successful TBA could well find a place in the Department's longer term plans for supply through open competition. These plans of course depend on the Department having user rights in regard to furniture and other specifications held by the PSSD, and you will know that we have stressed this point in previous correspondence. I assume that there will now be no problem here.

Michael Portillo Esq MP
Minister for Local Government
and Inner Cities
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

MANAGEMENT IN CONFIDENCE



Although I understand that the circumstances of the PSSD prevent discussion on alternative plans before an announcement about its future is made, it is clear that we are dependent upon the TBA continuing within the public sector. I hope that nothing will be done to prejudice that, and that our officials can be in a position to discuss the necessary action with the TBA as soon as an announcement on the PSSD is made. In the meantime they should consult urgently on the details of a press release as you suggest.

I am copying this letter to the Prime Minister, Michael Howard, Geoffrey Howe and Francis Maude, and Sir Robin Butler.

Yours,
Kenneth

KENNETH CARLISLE

MANAGEMENT-IN-CONFIDENCE



Treasury Chambers, Parliament Street, SW1P 3AG

Michael Portillo Esq MP
Minister of State
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

C August 1990

Dear Minister,

PRIVATISATION OF THE CROWN SUPPLIERS: FURNITURE BUSINESS

Thank you for your letter of 27 July.

I agree that the best option will be to close PSSD. Neither of the bids you have received is acceptable. It is clear that the costs of closure will be substantial. But the range between optimistic and pessimistic outcomes is very wide, depending mainly on how skillfully the rundown is managed; it will need to be purposeful and efficient as considerable sums of public money are at risk. It is too early to consider access to the Reserve until Norman Lamont and I are satisfied that every effort has been made to minimise the costs and to identify offsetting savings.

Turning to TBA, the arguments are more finely balanced. The net present value of the assumed future profit stream is small, and subject to Tom King's views there is no necessity to keep TBA in the public domain: while it may offer a useful service, Departments could if necessary make other arrangements, perhaps in cooperation with one another. I should like to be sure that there is an adequate business plan for TBA as a free-standing agency, and that the management will be capable of handling the business independently of their TCS parent.

MANAGEMENT-IN-CONFIDENCE

MANAGEMENT-IN-CONFIDENCE



You raised the issue of sponsorship responsibility for TBA. I agree that it would not be right for this to continue to lie with PSAS, and it seems to me that the solution would be for this to pass to Property Holdings, so that the Ministerial responsibility remains unchanged. But on the prior question of whether TBA should be retained I do not think it is possible to form a view without a clear assessment of the prospect for TBA and definite proposals for the performance and management of the business. Your consultants' analysis of TBA's profitability, prepared in June, identified a number of outstanding issues which need to be addressed in that context.

It seems to me that this can be pursued separately from the announcement of the decision to close PSSD. Our officials are in touch about the drafting of this.

We need to be sure to learn our lessons from the difficulties which the attempt to privatisation of TCS have encountered. I suggest there should be a formal post-mortem. My officials are of course ready to work with yours on this.

I am copying this letter to the Prime Minister, to Geoffrey Howe, Tom King and Michael Howard, and to Sir Robin Butler.

Yours sincerely,

FR FRANCIS MAUDE

(Approved by the Financial Secretary and signed in his absence)

MANAGEMENT-IN-CONFIDENCE

MANAGEMENT IN CONFIDENCE



10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

7 August 1990

PRIVATISATION OF THE CROWN SUPPLIERS: FURNITURE BUSINESS

The Prime Minister has seen Mr Portillo's letter of 27 July to the Financial Secretary. She too has come to the conclusion that the least bad course would be to close Product Supply and Services rather than offering it to an outside buyer or to a management buy-out, but to retain the Buying Agency.

I am copying this letter to Steven Flanagan (Financial Secretary's Office), Simon Webb (Ministry of Defence), Martyn Waring (Department of Employment), Tim Sutton (Lord President's Office) and Sonia Phippard (Cabinet Office).

ANDREW TURNBULL

Trevor Beattie Esq
Department of the Environment

MANAGEMENT IN CONFIDENCE

KW
c:\wpdocs\pps\beattie
B



10 DOWNING STREET

Barry

In an effort to minimize the
height of your in house return, I
started to deal with the
privatized a TBS. When it came
up first time, you queried why
it was lower to MBO was found
when it appeared to yield lower.
DoG has sent a revised paper
still advocating the MBO option
but this time the figures are
different. I spoke to the guy that
was responsible for the paper and
why the figures have changed. (and
are not simply a case of making the
previous conclusion look justified).
They would like an answer to
what happened 22/9

BT 6/8



COMMERCIAL IN CONFIDENCE

2 MARSHAM STREET
LONDON SW1P 3EB
071-276 3000

My ref:

Your ref:

3 August 1990

The Rt Hon John Major MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
LONDON
SW1P 3AG

Dear Chancellor

PRIVATISATION OF THE CROWN SUPPLIERS

I refer to Christopher Chope's letter of 13 June to Peter Lilley, his reply of 6 July, and to the letter of 9 July from the Private Secretary to the Prime Minister about the Transport and Interdepartmental Despatch Service (IDS) businesses of the Crown Suppliers. The Prime Minister asked for further analysis of the options, and our views on those options. ^{top enc}

I enclose a paper by my officials, ^(not attached) which has been agreed with yours, and which is backed up by a detailed evaluation of a number of alternatives for the two businesses by Coopers & Lybrand Deloitte, who are retained as reporting accountants for the privatisation. As requested by the Prime Minister, the responsible Minister here, Michael Portillo, has also considered this. The officials' paper focusses on the three alternatives which officials regard as the only courses worthy of serious consideration, namely sale to the MBO team of both businesses (£11-12m), closure of both businesses (£9.4m-£15.9m), and closure of the Transport business combined with retention in government of the IDS (£10.6m to £20.4m).

As the paper makes clear, some degree of uncertainty attaches to all 3 options, not all of which is revealed by the figures. But, in my judgement, sale to the MBO team is the least risky. Provided that the deal currently on the table (£11m up front plus deferred consideration with a present value of about £1m) can be secured, proceeds of at least £11m will be certain. The proceeds of the other options may be less than £11m. Furthermore, they are more risky. They depend on values actually achieved in asset sales and/or the profitability of the IDS if retained by Government. In addition, the costs of hiring vehicles and obtaining the IDS service under existing contracts from TCS are known. The costs of buying the service from elsewhere in the private sector are not.



There is, therefore, a respectable financial case for selling to the MBO, and Samuel Montagu & Co Ltd advise that the price offered is fair and reasonable, bearing in mind the value of the assets and the risky nature of the business.

However, there is another key consideration. Closure of the Transport and/or IDS businesses would both involve immediate redundancies of 90/170 technical and industrial staff, plus any of the 24 administrative staff who could not be found other posts. Sale to the MBO, on the other hand, would not involve redundancies, provided the present level of business could be maintained. It would be very difficult for the Government to justify this number of redundancies as a result of closing profitable businesses, particularly when any financial justification of closure is marginal and subject to the degree of uncertainty described in the paper.

On these grounds, therefore, my strong view is that officials should be instructed to continue negotiations with the Transport MBO with a view to obtaining their signatures on a deal as soon as possible. Once contracts are signed, an announcement can be made and we can begin the consultations with the Unions which are required by the Transfer of Undertakings (Protection of Employment) Regulations.

Finally, Peter Lilley in his letter of 6 July raised the question of the need for safeguards against the risk of the MBO team closing the business down themselves in relatively short order, given the substantial margin which then appeared to exist of capital assets over the price paid. My view is that the risk of this is not great. The latest evaluation of the proceeds of closure to the Government suggests that the MBO's inducement to sell up would be limited since the gap identified by Peter Lilley between expected liquidation proceeds and price offered for the business, was based on a total figure for liquidation proceeds which now appears to be at the optimistic end of a range. The potential gap is reduced further because a private company would receive lower proceeds from liquidation than the Government, (mainly because it would face financial claims from Government for damages on breach of its contracts). It is true that the MBO might get better prices for its assets if it ran down the business slowly, short of liquidation. But its ability to do so at a profit would be limited by its contractual obligations to its customers. A safeguard would be presentationally awkward. It would appear to amount to a statement that the Government had not been able to obtain full market value in the sale of public assets. Furthermore, any effective safeguard would appear to require the Government retaining some control over the privatised company through a special share. Our officials (and those of Peter Lilley's Department) agree that the justification for such a share would fall outside the doctrine for special shares which DTI and Treasury Ministers developed last year.

I should be grateful, therefore, for the Prime Ministers' and your agreement that we should continue the detailed negotiations with the MBO, without seeking to retain a special share. My officials would negotiate on the basis of cash consideration of £11m, adjusted in

Completed in London

the light of the net current asset position on completion, with deferred consideration after 5 years of either £2m without interest or £1m with interest. I should be grateful for your views on which deferred consideration option we should adopt. My officials will keep in touch with yours as negotiations progress and I shall, of course, ensure that Treasury are consulted about the form of any eventual announcement.

I am copying this to the Prime Minister and to Peter Lilley in view of his new Department's interest in the question of the Government holding special shares.

CEJ Bush

PP CHRIS PATTEN

(Approved by the Secretary of State and signed in his absence)



STRICTLY COMMERCIAL IN CONFIDENCE

THE CROWN SUPPLIERS PRIVATISATION: OPTIONS FOR TRANSPORT AND IDS

INTRODUCTION

1. PS/Prime Minister's letter of 9 July asked DOE and Treasury Ministers to consider further the proposed management buy out (MBO) of TCS Transport and the Interdepartmental Despatch Service (IDS) and, in the light of a comprehensive and fair appraisal of the options, the justification for proceeding with the privatisation. This paper provides the basis for such consideration .

2. The TCS Transport business, like the rest of TCS, is part of PSA services (PSAS). It supplies vehicles on a full maintenance and insurance contract hire basis to approximately 1000 customers almost exclusively in the public sector. The largest customer, PSAS, currently has 334 accounts relating to approximately 2000 vehicles out of a total fleet on hire of some 4000 cars, commercial and other vehicles, some of which are highly specialised. Of the remaining 2000 vehicles about 1000 are hired to other government departments. Some 1000 are on hire to other public sector bodies and a small number of private sector customers. Transport Division also operates several workshops in Southern England offering maintenance and repair



services to a proportion of the hire fleet and to other parties, mostly public sector bodies. Its turnover for the last two years was:-

	1989	1988
Vehicle hire	£14.1m	£13.3m
Repairs and sales	<u>£ 2.2m</u>	<u>£ 1.6</u>
	£16.3m	£14.9m

It showed an operating profit of £760,000 in 1989 compared with £298,000 in 1988.

3. The IDS has operated the Government's internal mail service for over 35 years. It principally provides a letter and parcel delivery and collection service to some 90 customer accounts, almost exclusively Government Departments or NDPBs primarily in London, but also in Wales with overnight services between London and Bristol, Cardiff, Birmingham and Hastings and between North and South Wales. It operates as an interdependent network of delivery/pick up points and is charged per call, regardless of the volume picked up/dropped. Its turnover and supplies for the last two years was:-

	1989	1988
Turnover	£2.2m	£2.0m
Operating Profit/loss	£0.24m	(£0.012m)

THE OPTIONS

4. In principle there is a wide range of options for the future of these businesses. Officials are however agreed that the only courses worthy of serious consideration are:



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- a. sale to the MBO of the transport and IDS business;
- b. liquidation of both businesses (in the case of the IDS only after suitable alternative arrangements had been made, probably by contracting out);
- c. closure of the transport business and retention in government of IDS.

The options which should not be further considered include:

- d. long term retention of the transport business in government: there is no good justification for the government's being in the vehicle hire business; the principal customer PSAS, is itself a candidate for privatisation;
- e. retention of the transport business for say 5 years, followed by privatisation: this has the disadvantages of (d) plus the depressing effects on staff and customer morale of a further period of uncertainty, with little prospect of selling the business in the future on better terms than now.
- f. sale of the IDS to the NFC: the NFC's offer is unattractive and their pension scheme is inadequate.

The financial implications of the rejected options are much more uncertain and/or less satisfactory than those of options (a), (b) and (c).

5. In considering the options Ministers may wish to focus on 4 key factors:

- (1) The need to show that good value has been obtained for the taxpayer.



- (ii) the extent to which the option is consistent with the presumption that a body which sells its services in competition with the private sector should not be in government.
- (iii) the extent to which the option offers good job prospects for staff.
- (iv) the extent to which the option provides a continued service to customers, especially Government customers.

6. Sale of the MBO of the Transport and IDS Businesses

There are encouraging signs that the MBO's bid can be financed. Provided the MBO is able to retain the support of its financial backers, the sale would provide a return of £11 million now to the Government with the presumption of a further deferred consideration, the NPV of which is about £1m. Samuel Montagu & Co Ltd advise that the price is fair and reasonable bearing in mind in particular the value of the assets, and the risky nature of the business. The bid also fulfils the non-price criteria set for the sale (see Annex 1). Provided the business is successful, the option should offer reasonable job prospects for the staff - the MBO team do not envisage any redundancies on the basis of current levels of business. The MBO team intend to provide a continued service to Government Departments from the private sector. However the business is a risky one, very dependent on its principal customer, PSAS. PSAS is itself facing major changes as it is untied. Whether because PSAS itself suffers a large drop in business leading to a decline in its requirement for vehicles and/or because PSAS manages to obtain better value for money elsewhere, it may no longer provide the predictable customer base it has hitherto. Furthermore the current trend is



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for vehicle manufacturers to enter the leasing/fleet management market, competing aggressively with hire firms such as TCS. The Transport MBO team's success is not therefore assured.

7. The then Financial Secretary, Mr Lilley, in his letter of 6 July to the then Parliamentary Under Secretary of State to the Department of the Environment, Mr Chope, asked for safeguards to be incorporated in any deal with the MBO, in order to ensure that the MBO could not quickly close down the business and make the substantial gain from selling assets of the business which the figures attached to Mr Chope's letter of 13 June has suggested might be possible. Officials are still considering this point.

Liquidation of the Transport and IDS Businesses

8. Liquidation of the transport business would involve selling all the assets of the business, (mainly vehicles and properties), and making the 90 or so professional and technical and industrial staff redundant as well any of the 23 administrative staff who could not be found other Civil Service jobs. Departments would obtain their requirements for vehicles in-house or from other contract hire companies. For the IDS, 'liquidation' would essentially mean contracting the service out to the private sector: there would be up to 80 or so IDS redundancies.

9. The proceeds of this option are estimated at £9.4 million to £15.9 million, on the assumption that the cost to Government Departments of hiring vehicles is the same as TCS's present charges and that for the IDS private contractors' charges are the same as those of TCS. To the extent that this is not the case the range of proceeds will shift upwards or downwards.



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10. The possible disadvantages of this course are as follows:

- (1) Sale of the transport business's assets at even the very low prices assumed

might be difficult, given the state of the market for motor vehicles: the figures attached to Mr Chope's letter of 13 June assumed that sale at a 10% discount from book value (and leaseback on reasonably favourable terms to the government) would be possible. Coopers & Lybrand Deloitte now believe that sale and leaseback may be difficult to achieve.

- (ii) Liquidation could be disruptive to government customers. Departments are likely to find it difficult to obtain from a single operator the comprehensive hire and fleet management package presently provided by TCS Transport. To replace the large number of vehicles involved with new contracts/vehicles would take a significant amount of time and administrative resources. Many of the vehicles are specially equipped and could not be replaced quickly. Customers might wish therefore to purchase them. Some customers would need to acquire some additional transport expertise to do all of this. On the other hand the market ought to be able to respond to the majority of customers' demands within a reasonable period of time.

- (iii) If Government cannot obtain non-Governmental customers' agreement to assignment of their hire contracts, it could sub-contract them but would still find itself in the anomalous position for a period of retaining central responsibility for



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these contracts (but not for its own), possibly at some cost and contrary to Government policy on Government business activities.

- (iv) So far as the IDS is concerned immediate contracting out would be difficult. Customers have only been prepared to sign contracts that commit them to use the service for one year, which may prove insufficiently attractive to contractors. In practice, therefore, the business would be retained in Government for a period while the specification was reviewed and perhaps revised before being market tested. The decision on whether to contract out or not would be taken in the light of the market test.
- (v) It could be particularly difficult to present the justification for the redundancies, in the light of the current profitability of the businesses.

11. Liquidation of the Transport Business and retention of IDS would be similar as far as transport is concerned to the total liquidation option described in paragraphs 8-10. The difference in the case of the IDS would be that it would continue to operate in Government. The choice of this option would probably depend on whether market testing had shown this to be the best option. The proceeds of the option are estimated at £10.6 million to £20.4 million on the assumption that the cost to Government Departments of hiring vehicles is the same as TCS's present charges and on the basis of an assumed range of profitability for the retained IDS of £0-£0.2m per annum. To the extent that this is not the case the range of proceeds will shift upwards or downwards.

SUMMARY

12. A summary of the figures for the three options considered is as follows:-

	Pessimistic	Optimistic
Bid	£11.0m	£12.0m
Liquidate Transport and IDS	£ 9.4m	£15.9m
Liquidate Transport and retain IDS	£10.6m	£20.4m

Note: All future income streams discounted at 6% real. This is low for the private sector and the MBO will be evaluating the business at a higher discount rate, reflecting the risky nature of the business and the real cost of the funds they will need.

Further details are contained in Annex 2, which is Coopers & Lybrand Deloitte's detailed evaluation of the alternatives.

TCSPU

26 July 1990



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PRIVATISATION OF THE CROWN SUPPLIERS

CRITERIA USED IN EVALUATING BIDS

- Size of net consideration offered
- Ability and intention of bidders to operate business as a going concern
- Financial robustness of bidder
- Terms and conditions of service offered to staff: especially comparability of pensions to Principal Civil Service Pension Scheme and opportunities for staff to share in the success of the business
- Employment prospects for staff
- Potential to expand business
- Attitude to Trade Union recognition, and negotiating rights in relation to transferred staff.



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TRANSPORT AND IDS

EVALUATION OF ALTERNATIVES

25 July 1990

I Introduction

101 We reported previously in our paper "Evaluation of Alternatives" dated 4 June 1990 on estimated costings of alternatives to sale for TCS' Transport and IDS businesses. The alternatives we considered were:

For Transport:

- * Total closure through sale and leaseback of the fleet to one or more leasing companies.
- * Retention of the vehicle hire business in Government but closure of the workshops.

For IDS:

- * Total closure by contracting out the business.
- * Retention of the business in Government.

102 TCSPU have now asked us to refine the alternatives and to consider the costing of them more closely.

103 As for our consideration of PSSD/TBA, the scope of our work has been restricted by the fact that, because of the sensitivity of the issue, we have been able to talk to only one existing member of TCS management, namely Mr Routh. We have been able to talk also to Mr Rowe, the Transport General Manager until 1 June 1990, to Mr Butter of PSA who is responsible for its vehicle hire arrangements and to Mr Wanstall of DOE who would be responsible for coordinating the IDS service after privatisation.

104 In performing our work we have also relied on certain unaudited financial information from TCS: in particular, management accounts for Transport and IDS for the five months to 31 May 1990 and also details of vehicles.

105 For options involving cash flows in the future a crucial factor is the discount rate that is applied to those future cash flows. Treasury have advised us of two rates used in Government: 6% which is applied to entities that deal almost exclusively within the public sector and are perceived as low risk and 8% which is applied to entities that deal with the private sector and which are subject to more risk. Treasury believes that 6% is the appropriate rate to use in evaluating options for TCS. Accordingly this is the rate we have used. However, we would note that a rate of 6% is low for the private sector. The MBO team are likely to be evaluating Transport at a higher rate linked to the risky nature of the business and to the cost of the funds they will need. This may go some way to explaining the value of their bid.



II Transport

201 The alternatives we consider are:

- (a) **Liquidation.** Under this alternative the Government would cease to provide the service after 6 months. During this 6 month period the vehicles would be sold by TCS, staff would be made redundant and the business closed as quickly as possible. Customers would need to seek alternative arrangements where sale and leaseback had not been arranged.
- (b) **Long Term Retention.** This alternative involves the vehicle hire business being retained as one entity in Government for the indefinite future. It is assumed that the workshops would be closed within 6 months. TCS' May 1990 management accounts show the workshops continuing to incur losses.
- (c) **Short term Retention.** Under this alternative the vehicle hire business would be retained and would seek custom from the private and public sectors for 5 years. At the end of the 5 year period the business would be sold. Again, it is assumed that the workshops would be closed within 6 months.
- (d) **Wind-down.** Under this alternative, Transport would not enter into any new vehicle hire agreements but would continue to service existing agreements until expiry. The business would therefore be wound down over a period of 5 years. Again, the workshops would be closed within 6 months.

202 Our evaluations of the alternatives are set out in Appendices 1 to 4 respectively. The results (showing a range from optimistic to pessimistic) are summarised below. Comparison of the alternatives with the bid is set out in Section IV on page 7.

	£m
Liquidation	17.1 to 10.6
Long term Retention	27.8 to 2.0
Short term Retention	$9.6 + X$ to $2.0 + X$
Wind-down	7.7 to 0.6

203 In the Short Term Retention option, the "X" represents the present value of the sale proceeds of the vehicle hire business in 5 years time.



204 Critical points pertinent to the alternatives are as follows:

Liquidation

- It is assumed that departments will be able to obtain vehicles and a similar level of service from an external vehicle hire company at a similar cost to what they currently pay Transport. PSA has said that, on the basis of limited market testing that it has already done, the prices charged by Transport are broadly comparable to the charges that a private sector company would make to them. Mr Rowe believes that Transport's prices are generally competitive when comparing like with like except that the major motor manufacturers do offer slightly lower prices.
- There is an unquantifiable cost to departments of the disruption caused by having a change in arrangements.
- Not all of Transport's vehicles are currently on hire to Government departments and so TCS has contractual commitments to some third parties. Many of the contracts have no provision for early termination. TCS may still be able to agree to terminate the contracts or novate them to a private sector operator. If not, it is assumed that the service could still be subcontracted to a private sector operator without any material cost to the Government although the Government would still retain the contractual commitment to provide the service.
- TCS does hire some specialist vehicles (for example, vehicles with special lifting gear etc) to various customers, particularly PSA. PSA might find it difficult to obtain replacement vehicles at short notice. Furthermore, these vehicles have high costs. It may therefore be desirable for customers to take over these vehicles and retain them.
- In the current climate in the motor industry, the sale and leaseback of vehicles to fleet operators may be just as impossible as it has been to find bids for the business as a going concern.
- It is most likely that TCS would sell the vehicles in the equivalent of a "fire sale". To achieve optimum value for the vehicles in a fire sale, the sale would need to be well planned with consideration given to timing, location and nature of sale. Mr Rowe has suggested that a special sale for TCS vehicles may be beneficial.



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Long term Retention

- Evaluation of this option is crucially dependent on forecast future profitability of Transport. The evaluation above is based on an illustrative range of future profitability from nil to £1.5m per annum. Transport produced a net profit of £0.8m in 1989, is budgeted to produce in excess of £1m in 1990 and as at May 1990 was ahead of budget. However, there are significant risks in relation to future profitability, particularly in relation to PSA's position as such a major customer (with about 50% of the fleet) and uncertainties resulting from PSA's proposed privatisation. Indeed, the Government may decide it is inappropriate for Transport to continue to trade in such a large way with PSA once PSA is in the private sector. Furthermore, Mr Rowe has suggested that, without a redirection of Transport so that it provides a service similar to that provided by private sector companies and without a review of the overhead structure, profits of Transport are likely to decline. The level of future profitability is therefore very uncertain. Also, we have not reviewed Transport's 1990 budget with management. Profitability may therefore fall outside the range of nil to £1.5m.
- It should also be noted that the comparatively low discount rate of 6% gives a high present value for any profit stream in perpetuity.

Short term Retention

- The evaluation of this option is again very dependent on the forecast future profitability of the vehicle hire business. The first point under the Long term Retention option above is therefore relevant also to this option.
- The evaluation also depends on any proceeds that might be received for Transport in 5 years time. We are unable to estimate these proceeds and so the discounted value of them is reflected by the "X" in the evaluation.

Wind-down

- In evaluating this option, significant assumptions have had to be made to assess the profitability of vehicle hire over the 5 year run-down period and also to estimate the amount that may be realised for the vehicles as the agreements expire. A high degree of estimation is therefore involved.
- Again it has been necessary to assume that when departments obtain replacement vehicles from private sector operators, they will be able to do so at a similar cost to what they currently pay Transport.
- There will also again be an unquantifiable cost to departments of the disruption caused by having to find an alternative source for replacement vehicles.



III IDS

301 The alternatives we consider are:

- (a) **Closure.** Under this alternative, it is assumed that the vehicles would be sold and all the staff made redundant. The Government would contract the service out to a private sector operator.
- (b) **Retention.** Under this alternative, the existing service would be retained in Government in perpetuity.

302 Our evaluations of these two alternatives are set out in Appendices 5 and 6 respectively. The results can be summarised as follows:

	£m
Closure	(1.2)
Retention	3.3 to 0

303 Critical points pertinent to the two alternatives are as follows:

Closure

- It is assumed that it would be possible to find a private sector contractor who would operate the network at the same price to departments as they currently pay to IDS. If such a contractor would charge more, there is an additional cost that should be taken into account. If such a contractor would charge less, there is a benefit that should be included.

Retention

- Evaluation of this alternative depends crucially on the expected future profitability of IDS. It is estimated that IDS made a profit of £240,000 in 1989. Mr Balderson's forecast on the basis of the May 1990 management accounts is that IDS will earn a net profit of not less than £30,000 in 1990. We have not examined forecast future profitability of IDS. The evaluation above is based on an illustrative range from nil to £0.2m. Profitability could in fact fall outside this range.
- Retention of IDS is also dependent on departments continuing to participate in the service. IDS is a network and so, if major departments withdraw, the network could disintegrate.



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IV Comparison with bid

401 The Transport MBO have made an offer for Transport and IDS. Our evaluation of the bid dated 4 June 1990 estimated the value of the bid (assuming no deferred element and no clawback on properties) at £11.8m. This evaluation assumes the same value of debtors and creditors as used in the evaluation of the various alternatives in Sections II and III above. To the extent that debtors and creditors are different, all alternatives should be affected by the same amount and so the comparative position does not change. If the MBO were to fail within 5 years, the Government may not receive the deferred consideration element valued at £1m. This gives a range for the value of the bid from £10.8m to £11.8m.

402 The bid has recently been the subject of further negotiation and revised terms are summarised in a note by Samuel Montagu dated 13 June 1990. The consideration offered was:

- cash of £11m
- Deferred consideration of either
 - (a) £2m payable in a single amount at the end of year 5 or
 - (b) £1m payable in a single amount at the end of year 5 plus interest on the £1m linked to base rate payable over the five years.

403 For purposes of this paper we have valued the bid in the range £11.0m to £12.0m. The actual value will depend on the value of debtors and creditors at completion and on the value of the deferred element of the bid.

404 National Freight Corporation have made an offer for IDS. The evaluation of their bid (after taking into account detriment payments to staff in relation to the bidders incomparable pension scheme) is estimated at minus £0.05m.

405 The bids can be compared with the other alternatives as follows:

	Optimistic	Pessimistic
	£m	£m
Bid	12.0	11.0
Liquidate Transport and IDS	15.9	9.4
Liquidate Transport/Retain IDS	20.4	10.6
Liquidate Transport/Sell IDS	17.1	10.5
Retain Transport Long Term/Close IDS	26.6	0.8
Retain Transport Long Term/Retain IDS	31.1	2.0
Retain Transport Long Term/Sell IDS	27.8	2.0
Retain Transport Short Term/Close IDS	8.4 + X	0.8 + X
Retain Transport Short Term/Retain IDS	12.9 + X	2.0 + X
Retain Transport Short Term/Sell IDS	9.5 + X	2.0 + X
Wind down Transport/Close IDS	6.5	(0.6)
Wind down Transport/Retain IDS	11.0	0.6
Wind down Transport/Sell IDS	7.7	0.5



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406 The "X" represents the present value of the sale proceeds of the vehicle hire⁷¹⁶
business in 5 years time in the option where it is retained for 5 years and then sold.



APPENDIX 1

LIQUIDATION OF TRANSPORT

This alternative involves ceasing the service in 6 months during which period the vehicles would be sold by TCS, staff would be made redundant and the business closed as quickly as possible. As set out in para 204 above it is unlikely that, having regard to the current climate in the motor industry, sale and leaseback of vehicles to fleet operators would be successful. It is most likely that the vehicles would be sold in the equivalent of a "fire sale".

Cost/proceeds for comparative purposes

	<u>Optimistic</u> £m	<u>Pessimistic</u> £m
1. Workshop properties - value per latest professional valuations (including development value)		
- Nine Elms (valuation at 30 June 1989)	1.5	1.5
- Burnett (valuation at 31 December 1989)	0.7	0.7
- Biggleswade (valuation at 30 September 1989)	1.5	1.5
less:		
Selling costs at 5%	(0.2)	(0.2)
For pessimistic, contingency of 10% to allow for current property market	-	(0.4)
2. Vehicles		
Net book value of TCS vehicles at 31 December 1989	15.0	15.0
less: Net book value of IDS vehicles (estimated)	(0.2)	(0.2)
	14.8	14.8
Assume proceeds, net of selling costs, which equate to between 100% and 75% of net book value (Note: TCS obtains its vehicles at favourable prices and depreciates them heavily in early years. Net book value is low by comparison with published guides as to vehicle values. To some extent this may be offset by lower values for commercial vehicles).	14.8	11.1
3. Computers, plant and machinery - assume negligible sale value	-	-

	<u>Optimistic</u> £m	<u>Pessimistic</u> £m
4. Stocks and work in progress - at 31 December 1989, valued at £0.2m. Assume negligible sale value	-	-
5. Debtors and creditors - for comparison purposes assume same value as used in evaluation of bid. Figure based on debtors and creditors at 31 December 1989	1.4	1.4
6. Redundancy (costs provided by TCSPU/GAD)		
- assume all specialist and industrial staff made redundant	(2.1)	(2.1)
- for pessimistic, assume also that 25% of AEG staff cannot be found alternative Civil Service posts and have to be made redundant	-	(0.4)
7. Profits/losses for period from date of commencement of closure to closure:		

Vehicle hire

Budgeted turnover for 1990

Turnover for 6 months
(At May 1990, turnover 4% over budget so, for prudence, use budget level as base)

Assuming, on average, contracts are for 4 years, 12.5% of fleet will reach end of contract during 6 months. Assume these vehicles are not replaced and, on average, 3 months income is lost

At pessimistic assume a further 20% of income is lost by customers terminating contracts early etc

15.6	15.6
7.8	7.8
(0.5)	(0.5)
-	(1.6)
7.3	5.7

Variable costs (cost of sales, repairs and maintenance, fuel, consumables, bought-in services, loss/damage, vehicle depreciation, insurance)

Budgeted cost for 1990

(12.0)	(12.0)
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Assume same proportionate decrease as for turnover

(5.6)	(4.4)
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	Optimistic £m	Pessimistic £m
Fixed costs (staff, accommodation, Transport overheads)		
Budgeted cost for 1990	(1.7)	(1.7)
Central overhead allocation (excluding interest received)	(1.0)	(1.0)
	(2.7)	(2.7)
Fixed costs for 6 months	(1.4)	(1.4)
For optimistic, assume 10% can be saved; for pessimistic assume no savings	0.1	-
Fixed costs	(1.3)	(1.4)
Total costs	(6.9)	(5.8)
At May 1990, vehicle hire costs 4% below budget: optimistically assume costs 5% under budget, pessimistically assume 5% over budget	0.3 (6.6)	(0.3) (6.1)
Estimated net profit/loss of vehicle hire for 6 months to closure	0.7	(0.4)

Workshops

Budgeted turnover for 1990	2.8	2.8
Turnover for 6 months	1.4	1.4
At May 1990, Workshops turnover only 68% of budget. Optimistically assume turnover for 6 months is 25% of budget, pessimistically only 10%	0.4	0.1
Variable costs (cost of sales, consumables, bought-in services)		
Budgeted cost for 1990	(0.8)	(0.8)
Assume same proportionate decrease as for turnover	(0.1)	-

	<u>Optimistic £m</u>	<u>Pessimistic £m</u>
Fixed costs (staff, accommodation, overheads)		
Budgeted cost for 1990	(1.7)	(1.7)
For 6 months	(0.8)	(0.8)
Optimistically, assume 10% can be saved	0.1	-
Fixed costs	(0.7)	(0.8)
Total costs	(0.8)	(0.8)
Optimistically assume costs 5% under budget, pessimistically 5% over budget	0.1	(0.1)
	(0.7)	(0.9)
Estimated net loss of workshops for 6 months to closure	(0.3)	(0.8)
Total profit/loss for period from date of commencement of closure to closure	0.4	(1.2)
8. Closure costs		
- salary cost for 3 months until staff can be made redundant	(0.5)	(0.5)
- costs of winding up the business after trading ceased including professional costs	(0.4)	(0.8)
Total comparative cost	<u>17.1</u>	<u>10.6</u>

Notes

1. This evaluation assumes that departments will be able to obtain vehicles and a similar level of service from an external vehicle hire company at a similar cost to what they currently pay Transport. PSA has said that, on the basis of limited market testing that it has already done, the prices charged by Transport are broadly comparable to the charges that a private sector company would make to a large customer such as PSA. Mr Rowe believes that Transport's prices are generally competitive when comparing like with like except that the major motor manufacturers do offer slightly lower prices. If private sector companies would overall charge more to Government departments, there is an additional cost that should be taken into account. If such companies would overall charge less, there is a benefit that should be included.
2. There is an unquantifiable cost to departments of the disruption caused by having a change in arrangements.

3. Not all of Transport's vehicles are currently on hire to Government departments. TCS estimate that approximately 25% of vehicles are on hire to other entities with which TCS has a binding contractual commitment. Many of TCS' contracts do not include a provision for TCS to terminate the contract except on a breach of obligations by the hirer. The Government would therefore be obliged to continue to provide the vehicle to the customer until the end of the hire period which may be for up to 5 years (or, in a few cases, even more) unless the hirer agrees to terminate the contract or novate it to a private sector vehicle hire company. If the hirer does not agree to this, the Government could subcontract its role to a private sector operator. It can also under most of its contracts increase its prices to the customer to cover the costs charged by such an operator if this is necessary. The one exception to this is fixed price contracts which the Government has recently been entering into. However, on the basis that PSA has advised us that it believes it could obtain similar services from the private sector at a similar cost to that charged by Transport, there should not be a major risk of the Government being charged higher charges by the private sector operator which it cannot then pass on to the customers. Also the Government can either sell the existing vehicle and hire a new one from the private sector operator to provide to the customer or sell the existing one to the private sector operator and hire it back. In either situation the Government can still sell the vehicle immediately and fulfil its obligations. It is assumed that the Government can therefore fulfil its obligations on contracts it cannot terminate or novate without any material ongoing cost by passing on all costs to the customer.
4. TCS does hire some specialist vehicles (for example, vehicles with special lifting gear etc) to various customers, particularly PSA. PSA might find it difficult to obtain replacement vehicles at short notice. Furthermore, these vehicles have high costs. It may therefore be desirable for customers to take over these vehicles and retain them.
5. In the current climate in the motor industry, the sale and leaseback of vehicles to fleet operators may be just as impossible as it has been to find bids for the business as a going concern.
6. To achieve optimum value for the vehicles in a fire sale, the sale would need to be well planned with consideration given to timing, location and nature of sale. Mr Rowe has suggested that a special sale for TCS vehicles may be beneficial.

APPENDIX 2

LONG TERM RETENTION OF TRANSPORT

This alternative involves retention of the vehicle hire business in Government in perpetuity but closure of the workshops.

Costs/proceeds for comparative purposes

	Optimistic £m	Pessimistic £m
Closure of Workshops		
1. Properties (per Appendix 1)	3.5	3.3
2. Plant and machinery in the workshops - assume negligible sale value	-	-
3. Stocks in the workshops - assume negligible sale value	-	-
4. Redundancy - only for workshops staff (per TCSPU/GAD)	(1.3)	(1.3)
5. Losses for workshops for the period from date of commencement of closure to closure (per Appendix 1)	(0.3)	(0.8)
6. Costs of closure including 3 months salaries until staff can be made redundant and professional fees	(0.4)	(0.6)
Proceeds from closure of workshops	<u>1.5</u>	<u>0.6</u>
7. Debtors and creditors for Transport as a whole	1.4	1.4
Proceeds before ongoing profits of vehicle hire (see below)	<u>2.9</u>	<u>2.0</u>

Retention of Transport in perpetuity depends crucially on the ongoing profits that Transport can earn.

TCS' budget for 1990 includes the following for Transport division as a whole:

	£m
Vehicle hire	1.8
Workshops	0.3
IDS	0.2
	<u>2.3</u>
<u>less</u> Allocation of central overheads	(0.7)
Net profit	<u>1.6</u>



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Allocating central overheads pro-rata between the three businesses gives a budgeted net profit for vehicle hire of £1.3m. This compares with actual net profit for 1989, based on an estimated disaggregation of TCS' results, for vehicle hire and workshops of £0.8m.

At 31 May 1990, Vehicle hire's net profit for the 5 months was £1.2m against a budget of £0.7m. It is therefore significantly over budget per the management accounts. We understand that this is to some extent attributable to high excess mileage charges relating to 1989 but billed in 1990.

These figures all indicate that vehicle hire could be profitable at least in the short term and earn profits in excess of £1m. However, there are significant risks, including:

- About 50% of Transport's business is with one customer, PSA. Such a large proportion with one customer is of itself a major risk.
- This risk is increased because of PSA's own privatisation. Not only are major changes taking place at PSA but also, on privatisation, it may be that the Government would consider it inappropriate for Transport in the public sector to do so much of its business with the private sector. Transport might be restricted to providing vehicles only to public sector customers. This would dramatically reduce Transport's customer base.
- Mr Rowe has suggested that without redirection of Transport so that it provides a service similar to that provided by private sector companies, profits of Transport are likely to decline.
- Increased pursuit of value for money and market testing by Departments produces risks for Transport's future income stream.
- Achieving the profitability requires strict control of overheads. The possible closure of PSSD may cause some change in Transport's overhead structure.

There is therefore great uncertainty regarding Transport's future profitability. For illustration purposes, we consider four possible profit figures: £0, £0.5m, £1m and £1.5m.



On the basis of retention in perpetuity, this alternative can be evaluated as follows:

<u>Profitability</u> £m	<u>Optimistic</u> £m	<u>Pessimistic</u> £m
0	2.9	2.0
0.5	11.2	10.3
1.0	19.5	18.6
1.5	27.8	26.9

Using the profitability of £0.5m as an example, these evaluations have been arrived at as follows:

	<u>Optimistic</u> £m	<u>Pessimistic</u> £m
Proceeds before ongoing profits of vehicle hire (as above)	2.9	2.0
Profits of £0.5m in perpetuity discounted at 6%	8.3	8.3
	<u>11.2</u>	<u>10.3</u>



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APPENDIX 3

SHORT TERM RETENTION OF TRANSPORT

Under this alternative the vehicle hire business would be retained and would seek custom from the private and public sectors for 5 years at the end of which period it would be sold. The workshops would be closed within 6 months.

Cost/proceeds for comparative purposes

	<u>Optimistic</u> £m	<u>Pessimistic</u> £m
Proceeds before ongoing profits of vehicle hire (per Appendix 2)	<u>2.9</u>	<u>2.0</u>

Evaluation of this alternative then depends crucially on the profits that the vehicle hire business can earn over the 5 years. Appendix 2 considers the potential profitability of vehicle hire. Again for this alternative, we evaluate it on the basis of illustrative annual profits of £0, £0.5m, £1.0m and £1.5m.

Evaluation also depends on the value that would be realised on sale in 5 years time. We are unable to estimate what this value might be. The evaluation therefore includes "X" being the net present value of estimated proceeds in 5 years time. At 6% the relevant discount factor is 0.75.

The alternative can therefore be evaluated as follows:

<u>Profitability</u> £m	<u>Optimistic</u> £m	<u>Pessimistic</u> £m
0	2.9 + X	2.0 + X
0.5	5.1 + X	4.2 + X
1.0	7.4 + X	6.5 + X
1.5	9.6 + X	8.7 + X



APPENDIX 4

WIND-DOWN OF TRANSPORT

This alternative involves the orderly wind-down of the vehicle hire business. No new vehicle hire agreements would be entered into but Transport would continue to service existing agreements until expiry which would take approximately 5 years. The vehicles would be sold as the contracts came to an end. The workshops would as in previous alternatives be closed within 6 months.

Cost/proceeds for comparative purposes

	Optimistic £m	Pessimistic £m
1. Profitability of vehicle hire over 5 year wind-down period		
Budgeted turnover for 1990 (per Appendix 1)	15.6	15.6
Budgeted variable costs for 1990 (per Appendix 1)	(12.0)	(12.0)
Budgeted gross profit	3.6	3.6
For optimistic, assume gross profit 10% higher; for pessimistic, assume 10% lower	0.4	(0.4)
	4.0	3.2

Assume contracts are for 5 years and evenly spread. This will give gross profit for the 5 years as follows:

Year 1	3.6	2.9
Year 2	2.8	2.2
Year 3	2.0	1.6
Year 4	1.2	1.0
Year 5	0.4	0.3

Budgeted fixed costs for 1990 including allocation of central overheads

2.7	2.7
-----	-----

At optimistic, assume 10% can be saved

(0.3)	
2.4	2.7



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Assume fixed costs can be reduced by 10% each year from Year 2 so fixed costs are:

Year 1	2.4	2.7
Year 2	2.2	2.4
Year 3	1.9	2.2
Year 4	1.7	2.0
Year 5	1.6	1.8

Net profit/loss for each year is therefore:

Year 1	1.2	0.2
Year 2	0.6	(0.2)
Year 3	0.1	(0.6)
Year 4	(0.5)	(1.0)
Year 5	(1.2)	(1.5)

Discounted at 6%, the present value of these profits/losses is:

Year 1	1.2	0.2
Year 2	0.6	(0.2)
Year 3	0.1	(0.5)
Year 4	(0.4)	(0.8)
Year 5	(1.0)	(1.2)
	<u>0.5</u>	<u>(2.5)</u>

2. Vehicles - these will be sold as agreements come to an end over the 5 years

Assuming an average spread of vehicle lives between 0 and 5 years, the vehicles have on average been written down to about 40% of original cost at any point in time. At the end of 5 years, a vehicle has been written down to 12% of cost. Current net book value is estimated at £14.8m. Aggregate net book value at disposal (at expiry of agreements) is therefore $12/40 \times 14.8 = £4.4m$. Assuming vehicles are sold evenly over the 5 years at approximately net book value and discounting proceeds in the future at 6% p.a. gives estimated sale proceeds of £3.5m. Therefore assume a range of:

5.0 2.0

3.	Redundancy - cost of making non-workshops staff redundant immediately estimated by TCSPU/GAD at £0.8. Assume increase in benefit equates to discount over the five year period. Some staff will be made redundant earlier and so assume range	(0.7)	(0.9)
4.	Proceeds of closure of workshops immediately (per Appendix 2)	1.5	0.6
5.	Debtors and creditors (per Appendix 1)	1.4	1.4
Total comparative cost		<u>7.7</u>	<u>0.6</u>



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APPENDIX 5

CLOSURE OF IDS

Costs/proceeds for comparative purposes

	£m
1. Vehicles - assume sale proceeds equate to net book value (Note 1)	0.2
2. Debtors and creditors - assume net out to zero	-
3. Redundancy - all staff made redundant (per TCSPU/GAD)	(0.6)
4. Profit/loss in period between commencement and final date of closure (Note 2)	(0.4)
5. Additional 3 months salaries until staff can be made redundant and costs of closure	(0.4)
Total comparative cost	(1.2)

Notes

1. Sale proceeds of the vehicles are based on net book value as at 31 December 1988. Because many vehicles have been replaced in 1989 and 1990, the current net book value is estimated to be higher by perhaps £0.2m. Even allowing for the fact that the sale proceeds from a quick sale of relatively new but high mileage vehicles may be less than book value, the estimated proceeds should still be a prudent estimate.
2. It is assumed that the service would continue to operate for six months. During this time the Government would put the contract to provide the service out to tender. The service would then pass to the private sector contractor after 6 months and IDS would sell its vehicles and make its staff redundant.

IDS was budgeted to make a surplus, before allocation of central overheads, of approximately £200,000 in 1990. However, per the May 1990 management accounts, it only broke even in the first five months of the year and Mr Balderson has estimated net profit for the year of £30,000. With the announcement of closure there may be some deterioration in this position and so assume a loss for the six months of £400,000.



3. It is assumed that it would be possible to find a private sector contractor who would operate the network at the same price to departments as they currently pay to IDS. There may, however, be some unquantifiable cost to departments of the disruption caused by having a change of operator of the service.



APPENDIX 6

RETENTION OF IDS

Costs/proceeds for comparative purposes

Under this alternative there are no up-front costs or proceeds. No assets are sold and no staff are made redundant.

As for the Retention of Transport (Appendix 2), the evaluation of this alternative depends crucially on the ongoing profits that IDS can earn. In 1989, it is estimated that IDS earned a net profit of £0.2m. The 1990 budget (after allocating central overheads pro-rata between the three Transport businesses) indicates a net profit for IDS of £0.1m. However, the latest forecast at the time of the May 1990 management accounts is for only a small profit for 1990. For illustration purposes, therefore, consider profits of £0, £0.1m and £0.2m. On the basis of retention in perpetuity this alternative can therefore be evaluated as follows:

Profitability £m	£m
0	-
0.1	1.7
0.2	3.3

Coopers
& Lybrand
Deloitte



CIVIL SERVICE PSA PT 3

PART 3 ends:-

MOS DOE to Wanda NP

PART 4 begins:-

SS/DOE CH/EX

aka to RF 3/8/90