2

Bound Volume

THIS DOCUMENT IS THE PROPERTY OF HER BRITANNIC MAJESTY'S GOVERNMENT

C(82) 8 COPY NO 83

2 April 1982

CABINET

THE INTERNATIONAL CONFERENCE CENTRE

Memorandum by the Chief Secretary, Treasury

1. Last year Cabinet considered the financing of the International Conference Centre. It decided, given that extra public expenditure was not available, that the Centre should be financed by a leasing arrangement with Pearl Assurance.

2. Since then circumstances have changed. Exchequer and Audit have examined the proposed contract with Pearl. They are highly critical of it. They point out that the Public Accounts Committee (PAC) have several times said they are opposed to this way of financing Government projects. They note that in the case of the Centre it would cost much more than direct public financing, but that the Government would bear all the risks associated with construction and operation. They point also to two particular features of the proposed agreement which are potentially very expensive. The first is the absence of a break clause, in a contract lasting for 125 years. The absence of a break clause is all the more risky in view of another provision in the proposed contract, that rent reviews must always be upwards. The second is the rent review provision itself. It now emerges that, for a reason summarised in the Annex, this would work in a way which substantially increases the cost of the contract, above what we expected last year.

3. Cabinet did not know when it considered the matter that there would be no break clause and that the rent review provision would take the very expensive form it has. The arrangement is now a much worse deal for the Government than we believed at the time. I now calculate that it would cost four times as much to finance the Centre in this way as by direct Government financing, as compared with the two to three times I estimated last year. The discounted cost of financing the Centre through Pearl would be some £120 million as compared with only about some £30 million through direct Government finance. The return to Pearl would also be much higher than the figure of just over 6 per cent we believed at the time. Although it will start at 6 per cent, it will rise to 8-10 per cent after only five years and stay at that level for the remainder of the 125-year contract.

4. I am sure that it would be wrong and damaging to proceed with this contract. We would be accused of saddling the taxpayer with an arrangement costing him several times more than it need. It would undermine all our efforts to get better efficiency and value for money in the Government and public sector generally. The Exchequer and Audit enquiries show that PAC will pick up these points. They could indeed make the matter a major embarrassment to us.

5. I am not seeking to reopen the decision to build the Centre. I accept that it should be built, in the timescale now planned. I propose that it should instead be built with public finance, and I am prepared to make the extra sums available accordingly. These would be £6 million in 1982-83, £13 million in 1983-84, £16 million in 1984-85 and £5 million in 1985-86. I would also be ready in principle to agree to some reimbursement of the abortive expenditure incurred by Pearl and the Government's advisers. The sums would be minute compared with the savings from giving up the contract.

6. The arrangement I propose would therefore enable us to build the Centre exactly as planned but it would avoid substantial unnecessary costs and highly damaging criticism of our failure to protect the taxpayer's interests.

L B

Treasury Chambers

2 April 1982

ANNEX

RENT REVIEW CLAUSE IN DRAFT AGREEMENT WITH PEARL

The initial rent will be fixed in 1986, when the Centre is due to be complete. There will be reviews in 1991 and at five-yearly intervals thereafter. But at the first review in 1991 the rent will be increased in line with rents in the area not since 1986 but since 1981. Subsequent rent reviews will start from this higher base. Inflation from 1981 to 1986, before the Centre was completed, will therefore be built into rents from 1991 and throughout the life of the contract.