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CABINET

USING PRIVATE ENTERPRISE IN GOVERNMENT

Memorandum by the Chief Secretary, Treasury

We are committed to reducing the size of the public sector. Although much is being done to 'privatise' public sector functions completely by transferring them to the private sector, many tasks must remain in the public sector. But this does not necessarily mean that they must all be done by public servants. Experience has shown that it is often more efficient to 'contract out' such tasks to private enterprise and that the possibility of contracting out stimulates in-house staff to perform more competitively. Much was done in the last Parliament. We must maintain the impetus. Cabinet on 16 December 1982 (CC(82) 53rd Conclusions, Minute 7) agreed on a drive to secure further contracting out in the public sector. As agreed then, I am reporting progress in this paper.

SCOPE

2. Many services have traditionally been contracted out, eg building and engineering works and management consultancy. The drive for efficiency during the last Parliament led to much more contracting out in central Government services (eg office cleaning) and in some local authority services (eg direct labour organisations (DLOs), refuse collection and street cleaning). Since I last reported Government departments have begun to consider more ambitious schemes, impetus in the local authority sector has increased and the Secretary of State for Social Services has launched a major initiative in the National Health Service (NHS).

CENTRAL GOVERNMENT

3. Most departments have contracted out some services, particularly in domestic areas like office cleaning, laundry, catering, security, typing and reprographics and computing. Up to December 1982 savings have been achieved of nearly 15,000 staff and at least £9 million net per annum. Further contracting out has been considered in the context of control of civil service numbers after 1984 [C(83) 24]. Those further proposals might save about 5,000 posts; it is too early to estimate financial savings. Some go beyond domestic services; examples include collection of statistical data in a number of departments, maintenance of police radios in the Home Office research and teaching at the Royal Military College of Science at Shrivenham and warehousing tasks in the Ministry of Defence.

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LOCAL AUTHORITIES

4. The 1980 Local Government, Planning and Land Act required local authority DLOs to bid for a substantial proportion of their work against competitive tenders from private contractors. In consequence DLOs undertook less than 10 per cent of a total of £21,000 million construction and maintenance work in 1981 and staff numbers fell by 11 per cent to 134,000 between April 1981 and October 1982. Regulations which will substantially increase the proportion of general highways, new buildings and maintenance work which must be put out to competitive tender (or given to contractors) have been laid before Parliament.

5. So far, apart from DLOs, our efforts have focussed upon exhortation to local authorities to contract out their services. In consequence a total of 46 have contracted out refuse collection and street cleaning with expected net savings of nearly £30 million. To go beyond exhortation will, for the most part, require legislation. I recognise the difficulties in that but I believe that we must acknowledge now the need for it in due course. I shall discuss with the colleagues principally concerned the best way to make progress on this issue.

NATIONAL HEALTH SERVICE

6. About £160 million worth of work is contracted out by the NHS (1981-82 figures). This includes building and engineering maintenance of £110 million, maintenance of equipment and vehicles of £30 million and domestic (cleaning, catering and laundry) services of £17 million. The scope for increased contracting out is illustrated by the fact that the total NHS expenditure on domestic services is nearly £400 million. In February the Secretary of State for Social Services initiated consultation on a draft circular proposing that all authorities should seek tenders for cleaning, catering and laundry services. The circular should be with health authorities in July or early August. Further extensions of contracting out are being considered in a number of areas.

NATIONALISED INDUSTRIES

7. Commercial pressures, and the requirement to keep within the External Financing Limits, lead management in the nationalised sector to contract out a wide range of services where this is cheaper than producing them in-house. For example, the energy industries alone contract out over £2 billion of activities each year. Our prime objectives with the nationalised industries are to increase competition and to privatise. However, it is clearly right that activities remaining within the public sector should be carried out in the cheapest possible way: in some cases this may involve further contracting out. The possibilities are at present being pursued industry by industry as part of the corporate planning and performance review procedures. E(NI) recently decided that in future collective Ministerial discussions of the nationalised industries should concentrate on strategic issues. I proposed, however, that Treasury and departmental officials should continue in the course of annual corporate planning discussions to press the industries to increase the amount of work contracted out, and report the results.

GENERAL

8. Under normal procedures, Value Added Tax (VAT) can only be refunded for business activities. This has been a disincentive to contracting out by Government departments and the NHS. (Local authorities can already reclaim VAT.) The clause to enable Government departments and health authorities to claim VAT refunds was dropped when the 1983 Finance Bill was shortened. There was not room to include it in the current Finance Bill. We intend to reintroduce the clause in 1984. In the meantime we propose to enable refunds to be claimed by extra statutory concession from 1 September.

9. The rights of staff transferred to a new employer when an undertaking is contracted out, are protected by the European Communities' Acquired Rights Directive. We have just received the Law Officers' Opinion on whether and how this Directive applies to the Crown. Treasury Ministers are consulting colleagues on this, and on the Public Services (Transfer of Functions) Bill, separately.

CONCLUSION

10. I invite the Cabinet to note the progress made so far and to agree that:-

- a. I should pursue contracting out in Government departments in my Public Expenditure Survey bilateral discussions;
- b. I should discuss with colleagues principally concerned how best to make progress on further contracting out from local authorities.
- c. The Health Service Ministers should continue the policy of increasing the amount of contracting out from the NHS.
- d. Treasury and departmental officials should continue in the context of the annual corporate planning discussions to press the nationalised industries to increase the amount of work contracted out where it is cheaper to do so.
- e. I should, together with the Ministers concerned with the Health Service, local authorities and nationalised industries, make a further report in twelve months' time.

P R

Treasury Chambers

18 July 1983