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PRIME MINISTER

CAPITAL EXPENDITURE CONTRACTS

The minute from your Private Secretary dated 23 April asked me to examine the evidence of time and cost overruns on major capital projects and to make recommendations for tackling the problem. You asked for a report on initial work by the end of June. This is attached. I have insisted that the report itself should be kept short and concentrate on principal recommendations; all the supporting material and comments on particular aspects are in the Annexes.

Some of the overruns on time and cost arise from the inherent nature of certain projects that the Government is involved in: for these tighter control can bring some improvements but it cannot eliminate the effect of fundamental uncertainties. However, it is clear that for many projects considerable savings, of the order of perhaps £50m - £100m a year in total, should be available by tightening up some aspects of the present control arrangements. These arrangements compare unfavourably with current practice in the private sector. Although in the time available for this initial work we have only been able to make a rather coarse study based on a limited, and probably not wholly representative, sample of 30 major projects, I believe the main conclusions stand out clearly and I see little purpose in undertaking further more refined investigative work.

The three main recommendations are:

1. A much tighter control over the initiation of projects, so that they are not allowed to go ahead until they are well defined with proper forecasts of cost and time. In practice this means a much more rigorous attitude towards "approval in principle" because once there is public commitment it is very difficult to regain proper control of a project if there has been slackness at the beginning. For major projects, say £25m or more, I believe formal approval of a Treasury Minister should be required on the basis of a short written case made by a Minister of the Department concerned. This would contain cost and time forecasts against which performance would be monitored.
2. Much clearer designation of the Project Manager within the Department concerned who should be held responsible for performance against the initial forecasts and for any variations



or additions. This means giving such Project Managers greater status and authority, and it will demand greater competence on their part. In some instances it will be worth recruiting Managers from the private sector with proven ability in this work - I understand the Head of Procurement in MOD already has this in mind. In other instances it will be necessary to improve the calibre and training of civil servants who do this work. The higher cost incurred from employing better Project Managers will show a good return.

3. Redefinition of the role of PSA in construction projects. I believe that Departments must "own" the projects and that PSA should be regarded as advisers and managing agents accountable for performance against initial targets. It follows that votes should belong to Departments, with funds then transferred for spending to PSA or private managing contractors.

I believe that tightening up in these ways will help greatly in making progress on the five specific points to which you asked me to give special attention. For example, Project Managers held clearly responsible for performance against initial targets will take trouble to ensure that design problems are thought through before targets are set and that competitive tendering is used effectively. When Departments "own" both capital costs and running costs they will have an incentive to get the right balance between initial capital cost and subsequent maintenance cost. Furthermore a clearly stated financial case prior to approval will enable the Treasury to probe this aspect.

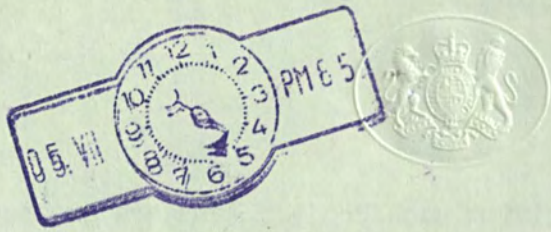
The practical problem is how to get the Whitehall machine to accept and implement these recommendations.

I suggest that as a first stage before the report is circulated generally I should have a discussion with Robert Armstrong, Peter Middleton and a few senior Permanent Secretaries before the Recess to get their advice on how best to take it forward. Thereafter I would recommend to you how the report itself should be handled and how you might formally react to it to ensure that it is acted upon promptly.

I am sending a copy of this minute to Robert Armstrong.

ROBIN IBBS

5 July 1985



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