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OK, But not last day
before recess. We
must avoid
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Mr. J. J. J.
any comments?
The 5th and 10th reports
seem the only ones of any
interest. I can see no
objection to what is
proposed.

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W F S Rickett Esq
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12 July 1983

Dear Willie,

TREASURY MINUTE REPLYING TO REPORTS OF THE PUBLIC ACCOUNTS COMMITTEE

Assuming the House does not go into recess before 27 July, we propose to present at 2.30 and publish at 3.30 on Tuesday 26 July the Government's response to those Public Accounts Committee Reports outstanding from the last Parliament, for which H M Treasury have the responsibility to reply. If the recess were to begin the previous week, we would have to advance the date to Thursday 21 July. It is not customary to publish replies to PAC Reports when the House is not sitting so if we were to miss the current opportunity we would have to delay publication until the Autumn.

2. The Financial Secretary has agreed to the reply to the PAC - in the normal form of a Treasury Minute - being presented in his name. I enclose (Annex A) a list of the PAC Reports to which we are replying with a summary (Annex B) of the main conclusions and recommendations appearing in the various reports.

3. These Treasury Minutes usually attract scant attention except from members of the PAC themselves. The media tend to pay them little attention as a rule. However, one or two things have recently occurred which might raise the odd ripple of interest.

4. The Public Accounts Committee is one of the few select committees so far appointed in the new Parliament (on 7 July). Also, although, as usual, there is little of significance in the Treasury Minute itself, it does refer to one particular matter of political and general public interest. This is the rate of profit obtained by firms in the defence and drugs industries.

5. The relevant PAC Reports (5th on Defence and 10th on the NHS) criticised what it saw as excess profits obtained by defence and drugs firms under the existing arrangements. The two reports received some publicity at the time they were published and defensive briefing on them was provided for your office accordingly. Further interest in the Government's reactions to those particular reports may well be stimulated by the Chancellor of the Exchequer's announcement last week which mentioned both defence and the NHS as needing to contribute to the proposed public expenditure savings. The remaining PAC Reports to which the Treasury Minute will reply are the usual mixed bag. They include a response to the report on Dog Licences (1st Report) where the text has been kept carefully non-committal in order not to

prejudice the future discussion in H Committee, currently being considered.

6. We are about to ask HMSO to arrange for printing and publication of the Treasury Minute on 26 July. We propose to arrange for pre-publication (CFR) copies as usual: for laying before the House, for supply to the relevant departments, to PAC Members and to the Lobby (the latter through the Treasury's Information Division).

7. May we have approval to proceed to publication of the Treasury Minute on 26 July as proposed? An early reply would be appreciated so that we can adhere to the printing timetable that HMSO are arranging.

8. I am sending copies of this letter to Bernard Ingham and Murdo MacLean.

Yours very

A J
A J SALVESON
Parliamentary Clerk

PAC REPORTS

	<u>Department(s)</u>	<u>Subject(s)</u>
1st Report	Department of the Environment	Dog Licencing
2nd Report	HM Treasury	Development of Internal Audit in Central Government
3rd Report	HM Treasury	Financial provision for and development of Exchequer and Audit Department
4th Report	HM Treasury	Excess Votes
5th Report	HM Treasury and Ministry of Defence	Storekeeping and accounting at Central Ordnance depots; effectiveness of Navy and Army equipment; fatigue damage to Buccaneer aircraft; pricing and post-costing of non-competitive contracts; development and production of Tornado aircraft; use of commercial insurance
6th Report	Department of Education and Science	Grants to voluntary colleges
7th Report	HM Treasury and Overseas Development Administration	Annual audited statements; remission of loans
8th Report	Department of Health and Social Security, Scottish Home and Health Department, Welsh Office	Joint financing of care by the National Health Service and Local Government; Disposal of surplus NHS land and buildings
[9th Report*	Northern Ireland Departments	Northern Ireland matters]
10th Report	DHSS, SHHD, Welsh Office	Dispensing of drugs in NHS
11th Report	Export Credits Guarantee Department	General work of ECGD

* not covered by Treasury Minute

SUMMARY OF MAIN CONCLUSIONS AND RECOMMENDATIONS OF PAC REPORTS1st Report

The report high-lighted the failings of the current arrangements: costs of collecting licence fees far outstripped revenue obtained through them; fewer than half dog population was licenced; central government bore most of the operating costs while local authorities received the revenue collected. Recommended temporary suspension of present arrangements until firm policy decisions taken.

2nd Report

General criticism of relatively low grading of internal audit staff and low numbers of professionally qualified staff. However, report concluded an encouraging amount of progress had been made and expected impetus to be maintained.

3rd Report

At the time a "trailer" for the then private member's Bill sponsored by Mr St John Stevas. The Bill subsequently became the National Audit Act 1983. The Report recommended the 1983-84 Estimate for E&AD should be approved without any cuts being proposed. by Treasury, a new headquarters building for E&AD, further expansion and development of E&AD, improved grading and pay prospects for E&AD staff and an indemnity against financial loss arising out of the activities of the C&AG and his staff.

4th Report

Formal examination of Excess Votes. No substantive comment.

5th Report(a) Storekeeping at Central Ordnance Depots

Stocktaking results at Bicester are not up to the expected standard. MOD should keep position under review. PAC supports "the continued search for streamlined and cost effective procedures".

(b) Effectiveness of Navy and Army Equipments

PAC supports efficient procedures for monitoring the effectiveness of all major equipments but doubts the wisdom of merging development and production of weapons systems.

(c) Buccaneer aircraft

The testing of this aircraft had clearly been improved by more sophisticated techniques but difficult for PAC to judge whether this might have been done earlier. Such testing is critically important and demands the allocation of the necessary resources.

(d) Non-Competitive Contracts

Last year's PAC Report (16th Report 1980-81) had expressed concern that 1980 Review recommended and Treasury accepted a target profit rate of 20%, rather than 17% suggested by straight comparability with industry generally; and that this assumed a 15% inflation rate (compared with the then rate of 11-12 per cent). E&AD had calculated that 20% instead of 17% was worth £30 million a year to defence contractors. Allowing for current (5%) rate of inflation PAC claims it is worth £75 million a year compared with the Review Board's calculations.

PAC finds this disturbing and expresses surprise that the Government have allowed the 20% rate to continue unchallenged. It means profits £150m 'too high' in 1980 and 1981 and continuing at that rate until the outcome of the present review.

PAC strongly recommends urgent completion of present review and subsequent negotiations; restoration of "the principle of comparability; proper reflection of inflation factors; and provision for review within the intended three years currency of the new arrangements if circumstances justify it.

(e) Tornado aircraft

Extra costs incurred through stretching out the production period for this aircraft. Due to budgetary difficulties in UK and Germany. This is not an "end year flexibility" problem as MOD appeared to claim. It was a case of overcommitment of prospective Defence Budget. The decision whether to stretch out Tornado deliveries or "to take some other step" should not have been left to MOD with the Treasury" only concerned that agreed limits should not be exceeded on an annual basis." Cost sharing arrangements should preferably be met by distribution of work and jobs rather than cash payments. Pricing of some contracts has been very late.

(f) Commercial Insurance

PAC is content with the experiment with commercial insurance for third party and employers' liability claims authorised for MOD.

6th Report

This (rightly) criticises DES for advancing grant to voluntary colleges before it was needed by them - mainly in order to avoid surrendering unspent money at the end of the financial year. The result was that the Colleges carried large, interest earning, balances in their books while the taxpayer was borrowing more than needed to in order to finance the issues to the Colleges. (These balances have since been recovered by DES.)

7th Report

(a) Annual audited statements

Previous PACs had complained about the delays experienced by ODA in receiving audited statements from overseas governments about local expenditure met by voted monies. The position appeared to be getting worse. ODA was advised to maintain its efforts to obtain audited statements more quickly and consider suitable alternatives when

such statements are badly delayed. ODA management is criticised for insufficient attention to records against which to measure how many statements were overdue.

(b) Remission of loans

This concerns a test case brought by E&AD to establish whether the PAC expected Parliament positively to authorise the write off of aid loans remitted or whether it was enough merely to inform them. ODA had done the latter. The PAC thinks it should have done the former.

8th Report

(a) Disposal of Surplus NHS land and buildings

There are long delays in this, despite some incentive arrangements which put the proceeds or part of them back into the NHS. DHSS have recently examined the problem and the PAC is in favour of "the most effective use of their estate, including carrying out realistic cost and benefit appraisals of land prior to making decisions on its retention or sale." The Treasury are invited to consider one recommendation, for notional rents, for wider application. The PAC endorses DHSS's attempts to allow departments to obtain full planning permission before selling land.

(b) Joint Financing of Care by the NHS and Local Authorities

This concerns an area at the boundary between DHSS and Local Authority responsibilities. The Government's policy is that most elderly, mentally handicapped and mentally ill people should be cared for in the community rather than, as many of them have been, in hospital. But it is difficult to engineer the change without incentives and encouragement to local authorities to accept the greater responsibilities and expenditure, which fall to them under the policy.

The PAC is concerned that there has been inadequate joint planning between health authorities and local authorities and that local authorities are therefore able to finance

schemes at the health services' expense without proper consideration for NHS priorities. They appreciate the need in the early stages to get the schemes off the ground and generally welcome DHSS assurances about closer control in future.

9th Report

This is the responsibility of the Northern Ireland Office.]

10th Report

The PAC complains that the target returns of profit obtained under the Pharmaceutical Price Regulation Scheme (PPRS) are considerably higher than those obtained by the rest of British industry. This is in similar vein to the comment on defence contracts (5th Report). It is unhappy about the element of subjective judgment of firms that is involved (though offers nothing better). It therefore welcomes the projected review of the PPRS and expresses the hope that it will "have regard to" current rates of return in industry generally, will examine efficiency indicators etc. etc. The PAC also expresses concern about the level of pharmaceutical wholesalers' profits and criticises chemists for not co-operating with the DHSS in examining their remuneration/profits.

11th Report

This covers examination of ECGD on the basis of a "management consultancy" type of report by the C&AG and also on the basis of their accounts for 1981-82.

There is nothing very critical in the first part - just recognition of the great difficulty in finding a satisfactory basis for measuring the department's financial performance and so setting a financial objective in volatile economic conditions.

So far as 1981-82 is concerned the PAC shares the C&AG's misgivings about the lack of provisions for unforeseen or unpredictable political or economic events. It emphasises the importance of good underwriting intelligence and wants premium increases to be minimised (while at the same time imposing no net cost on the Consolidated Fund). Finally, there is mild criticism of the technique adopted of an "interest free loan" from the national interest part of the business to the straight commercial business side.

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10 DOWNING STREET

From the Private Secretary

13 July 1983

Treasury Minute Replying to Reports of the
Public Accounts Committee

Thank you for your letter of 12 July. Subject to any comments from the Lord Privy Seal's Office, we have no objection to your presenting and publishing this minute on 26 July, provided that that is not the last day before the Recess.

I am copying this to Murdo Maclean (Chief Whip's Office) and Nick Huxtable (Lord Privy Seal's Office).

! W. F. S. RICKETT

A. J. Salveson, Esq.,
HM Treasury.

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