

BF
12/8 IF reportPrime
Minister :

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Prime Minister

I understand that the Chief Secretary will also be meeting you. Await his comments? VF 23/7

attached

I am now in a position to take the opportunity to respond to your note of May 17 on Financial Management. The paper you attached said that the main objectives of spending departments should be to have "a clear view of their objectives" and an ability to "measure performance in relation to those objectives". You also indicated that while the yardstick of profitability is lacking in most cases in government, nevertheless "the principle should be applied to the maximum possible extent".

In the context of PSA I recognise also the need to give individual departments a greater influence over their own spending programmes as far as property is concerned.

As colleagues will know, we are already moving to the PRS (Property Repayment Service) in April 1983 which goes part of the way to do this; but I am now considering the next step to go further in this direction and at the same time meet the objectives set in your letter.

The PSA is giving preliminary consideration to the possibility of establishing within it a Property Division - an outline of which is given at Appendix A.

As far as Departments are concerned, their relationship with PSA will essentially be an extension of the principles of PRS; and clearly there will need to be further discussion with Departments to take account of their views in working out the details.



As far as Government is concerned, the proposition would be in accord with your request and would hold out the prospect of tougher financial management in this important part of PSA's activity.

In order to make progress with this idea without risking wasted effort, I felt the need to inform colleagues in advance because if there is any disagreement in principle, I should like those issues resolved now. At this stage, therefore, I am merely asking for your reaction to the principle of a Property Division regulated by a trading fund. We would expect that it would take some 6 months before we were able to come back with flesh on the bones and to identify positively the costs and benefits.

Derek Rayner, who has been consulted, has said "I agree with the emphasis on incentives to rational economic behaviour likely in principle to flow from the more competitive environment of a trading fund."

I shall be grateful for your views, and those of Cabinet Colleagues to whom I am copying this minute. I am also copying this to Sir Derek Rayner and Sir Robert Armstrong.

MH

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22.7.82

POSSIBLE PROPERTY DIVISION WITHIN PSA

The essentials would be:

- i. the Division's portfolio would embrace those parts of the Government estate where there is a potential alternative use. It may cover 80% of the Civil Estate and maybe 20% of the Defence Estate and have an asset value of £3-5 billion;
- ii. the PD will negotiate a Memorandum of Understanding (see Note 1 attached) in respect of each property which will establish effectively a form of "contractual" relationship between itself and departmental tenants. This will build on PRS (Property Repayment Services) which starts in April 1983;
- iii. the object is to enable the PSA through the property division to act as closely as possible to a private sector property company and the individual departments to act as independently as possible in what they perceive as their best interests;
- iv. the PD would have Trading Fund status, which would enable:
 - a. the development of an objective measure of the financial utilisation of our property assets via a "Return on Capital"; the trend of which could then be compared with the private sector,
 - b. the real property costs of government decisions to be identified,
 - c. a longer term view to be taken of property matters,
 - d. a clearer distinction to be drawn between capital and revenue expenditure on property,
 - e. the introduction of more options or alternatives both for Departments and internally in the handling of maintenance,
 - f. more generally, a tougher commercial attitude to be developed both within the PD and by overspill in other parts of PSA.

Note 1 The "Memorandum of Understanding" would cover:

current market rent

rent reviews every 3, 5 or 7 years

extension of maintenance responsibility (including in
most cases internal decoration) to the tenant

tenure, ie period tenant expects to require the property

CS L-T Mangrove
Pt 11



22 JUL 1982

Coordinator