House of Commons

Committee of Public Accounts

PFI: The new headquarters for the Home Office

Eighteenth Report of Session 2003–04

Report, together with formal minutes, oral and written evidence

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The Committee of Public Accounts

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Mr David Rendel MP (*Liberal Democrat, Newbury*)

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Committee staff

The current staff of the Committee is Nick Wright (Clerk), Christine Randall (Committee Assistant), Leslie Young (Committee Assistant), and Ronnie Jefferson (Secretary).

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Summary

The PFI deal to provide new headquarters accommodation for the Home Office is a high profile, high value project. Over the life of the 29 year contract signed in March 2002, the Home Office will pay Annes Gate Property Plc[1] (AGP) £311 million (net present cost) for accommodation and services. The new building, designed to hold 3450 staff, will be built on the site of the old Department of the Environment building in Marsham Street, Westminster. Demolition began in March 2002 and Home Office staff are due to move into their new accommodation in January 2005.

The Home Office began the procurement in 1996 after a review of its accommodation concluded there were deficiencies in the existing estate and that it needed to be refurbished. During the competition for the refurbishment contract, AGP, however, made a developed and costed variant bid to build new accommodation at Marsham Street. This option was attractive to the Home Office because it avoided the business risk associated with moving into and out of temporary accommodation and it offered the opportunity to bring the Prison Service and the Home Office together on one site. Further competition demonstrated that a new building offered better value for money than refurbishment.

On the basis of a Report by the Comptroller and Auditor General[2] we took evidence from the Home Office and AGP on whether the new building will meet the Home Office's needs and on the negotiation of the deal.

1 A company owned by Byhome Ltd (which in turn is owned by Bouygues UK Ltd and Ecovert FM Ltd, both of which are owned by Bouygues Construction S.A., a major construction firm based in France) and HSBC Infrastructure Ltd.

2 C&AG's Report, *PFI: The new headquarters for the Home Office* (HC 954, Session 2002–03)

Conclusions and recommendations

1. **Under-forecasting of staff numbers leads to bad decisions on accommodation.** There is evidence of optimism bias in PFI projects for departmental accommodation: departments have assumed much lower staff numbers than they have subsequently employed. The buildings have then not been large enough to hold everyone. Yet such projects are often justified in part, as in this case, by the advantages of bringing everyone under one roof. The Home Office assumed that staff numbers would reduce due to outsourcing, efficiency gains and changes in working practices. Instead, numbers increased dramatically between 1998 and 2003 as the Home Office took on new responsibilities, although the total increase is not fully explained by these new functions. Similar stories arose at GCHQ,[3] the Ministry of Defence,[4] and the former Department of Social Security.[5]

2. **If, as is now possible, Home Office HQ numbers in London fall, the Home Office should identify other Government departments whose staff can fill up the new building.** Departments' roles and responsibilities, and therefore staff levels, are inevitably subject to change, yet PFI accommodation deals tie departments into paying for servicing buildings however few staff are accommodated.

3. **The Home Office should revisit their implausibly high assumption that 1300 of their officials plus support staff need regular access to Ministers and Parliament.** The greater part of their 3500 headquarters staff could probably be moved out of London, and the Home Office should take full advantage of the opportunity provided by Sir Michael Lyons' review of relocation.[6]

4. **There can be no operational reason why the Prison Service HQ needs to be in London at all.** Originally the Home Office wanted it in the same building as the central Home Office, though more for convenience than demonstrated business need.

5. **To get the softer, but important, benefits that the move to the new building is intended to bring the Home Office will have to set up a systematic management framework.** This is a deal that potentially offers real benefits to the Home Office and the taxpayer. Staff to be located in the Marsham Street building do not deliver services directly to the public as customers but by developing effective policies and programmes. This means that the intended benefits of the new accommodation which arise through better team working and flexibility may not be readily apparent

3 C&AG's Report, *Government Communication Headquarters (GCHQ): New Accommodation Programme* (HC 955, Session 2002–03)

4 4th Report from the Committee of Public Accounts, *PFI: Redevelopment of MoD Main Building* (HC 298, Session 2002–03)

5 19th Report from the Committee of Public Accounts, *The Contributions Agency: The Newcastle Estate Development Project* (HC 104, Session 1999–2000)

6 Independent Review of Public Sector Relocation, *Well Placed to Deliver? Shaping the Pattern of Government Service*. Report by Sir Michael Lyons to the Deputy Prime Minister and the Chancellor of the Exchequer, March 2004 (ISBN 1-84532-009-3)

and therefore difficult to quantify. Other departments that have faced similar challenges, such as the Treasury and GCHQ,[7] may be able to advise.

6. **We doubt whether the potential return from the Home Office's right to share refinancing gains is worth the £2.75 million price the Home Office paid for it.** The analysis done by the Home Office does not appear to relate the extra £2.75 million demanded by AGP for the concession to the probability that re-financing might take place. Given that subsequently the Treasury was able to negotiate far wider-reaching concessions on sharing re-financing gains without making any payment for them, it seems questionable that the Home Office should have agreed to any payment in this case.

7. **The Home Office should decide quickly on the future of Horseferry House, a building incapable of future economic occupation.** Since 2002 there has been a decline in the commercial property market and it is surprising that the Home Office does not know how much its freeholds are currently worth, particularly as it expects to sell them.

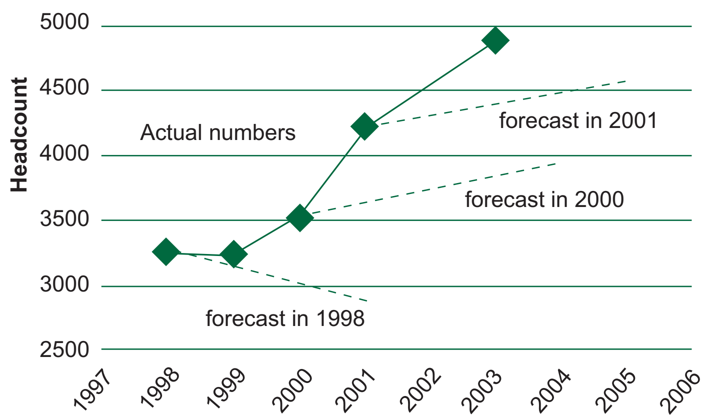
7 C&AG's Report, *Government Communication Headquarters (GCHQ): New Accommodation Programme* (HC 955, Session 2002–03)

1 Meeting accommodation needs

Poor planning of staff numbers

1. When Best and Final Offers were invited from bidders in 1998, the Home Office stated a requirement to accommodate 2950 staff based on a forecast reduction in its central London headquarters staff from 3200. This reduction did not occur and in fact, between 1998 and 2003, numbers increased to 4900 (**Figure 1**). Although the design of the building was adapted to provide for an additional 500 staff, further expansion was not possible due to the size of the site and planning restrictions. At present, total Home Office and Prison Service headquarters staff numbers are 1500 in excess of the capacity of the new building.[8] The Home Office has now had to change its working assumption that the Prison Service would be accommodated at Marsham Street. In the short-term, one option was for it to remain in Abell House and Cleland House, which were currently occupied by the Prison Service and were very close to the Marsham Street building. In the longer term, the Home Office was looking at whether it could get better value for money either elsewhere in central London or outside London.[9]

Figure 1: Home Office forecasts of staff numbers underestimated actual increases



Source: C&AG's Report

2. When it was making the original projections in 1998, the Home Office assumed that staff numbers would fall. Despite some machinery of government changes that have reduced Home Office functions, staff numbers have since gone up because of changes in the Home Office's role and the addition of some new responsibilities. **Figure 2** shows that some 800 extra staff have been employed to meet these new responsibilities. These additional staff do not, however, fully account for the total rise since 1998. In 2002, before the deal was signed, the Home Office considered whether the project still made sense. Although the building would not be large enough to accommodate all the staff, the Home Office considered that the deal still offered good value for money and decided to proceed.[10]

8 C&AG's Report, para 1.25

9 Qq 3–6

10 Qq 8, 34

Figure 2: Increases in staff numbers arising from new responsibilities

New role/responsibility	Additional staff
Creation of the National Probation Directorate	300
Creation of a trilateral criminal justice team working to the Department for Constitutional Affairs, the Attorney General and the Home Office	150
The Home Office has taken over the Drug Co-ordination Directorate from the Cabinet Office.	200
Increase in numbers working on policing, crime reduction and terrorism	Unspecified
Increase in the prison population leading to an increase in prison service headquarters staff	150
TOTAL	**800**

Source: Q 34

3. The Home Office acknowledged that it should have put more effort into ensuring that staff projections were as accurate as possible. There was currently no fixed projection for staff numbers in 2005 as the Home Office was working on a strategic plan for the whole Home Office group for the next five years. As part of that exercise, all headquarters numbers were being reviewed to see if more resources could be shifted into the front line. The Home Office also said that numbers were likely go up and down over the next few years and that it was having to plan for a degree of uncertainty. For example, there were major reviews underway of drugs policy and the structure and workings of prisons and probation. Both of these reviews could have significant implications for staff numbers.[11]

4. The Home Office considered that in the future it might have flexibility to increase the number that could be accommodated in Marsham Street. Home working, remote working and hot desking could enable a greater number of staff to be based in the new building, on the assumption that no more than 3450 would be there at any one time.[12]

Location in central London

5. Before proceeding with the Marsham Street solution, the Home Office's property advisers identified alternative potential properties in London **(Figure 3)**.[13] Although the Home Office looked at locations elsewhere in London it was felt at the time that any location outside Westminster was unsuitable, because Ministers would not want to be located outside the division bell area.[14]

11 Qq 8, 38, 146

12 Q 47

13 Q 40; Ev 14

14 Q 42

Figure 3: Properties and locations considered by the Home Office

Property and location	Reason why thought unsuitable
Stag Place, Victoria	More expensive and slightly smaller than 2 Marsham Street
Elizabeth House, Waterloo	Inaccessible to Parliament and the rest of Whitehall
Potential sites available in London Docklands, Paddington and elsewhere	Inaccessible to Parliament and the rest of Whitehall

Source: Written evidence provided by the Home Office, Ev 14

6. The Home Office is not entirely based in London. The majority of its staff are spread around the country in prisons and ports as well as major office developments in Liverpool, Sheffield and Leeds. The Home Office is now looking at whether its entire current headquarters staff needs to be in central London, following Sir Michael Lyons' review.[15] Given advances in Information Technology, the Home Office said that it should be possible to move some services out of London. However, a headquarters building close to Parliament was important because Ministers needed to be supported by staff. Other officials had dealings with Parliament and other Government departments located in London. The Home Office's previous experience of moving most of the Immigration Department to Croydon, Sheffield and Leeds had caused problems, with staff spending considerable time travelling or hot-desking in London.[16]

7. For the Lyons Review, the Home Office estimated that up to 1300 members of core Home Office staff might need regular contact with Ministers or Parliament. The number of staff in direct support of this group was not estimated but could be perhaps as many staff again. The Home Office did not estimate the number of other staff whose work required them to have frequent contact with other Government departments or major stakeholders.[17]

8. The Home Office did not always expect to require nearly 3500 staff in London and over a period of years, the number of staff needing to be accommodated in Marsham Street might drop below 3,450. The possibility of increasing the use of new technologies such as video conferencing to enable more staff to work outside London was being reviewed. The current review of staff location would determine whether it would be more financially beneficial for all headquarters staff to remain in London rather than incur the costs of travel, associated disruption and loss of services.[18]

Securing wider business benefits

9. Accommodation running costs in central London for 2001–02 had amounted to £33 million, around £6 million less than the annual cost of the PFI deal. The cost of running the existing estate was rising and the Home Office expected it to go up next year, depending on the level of maintenance required. The Home Office therefore felt that the PFI deal offered

15 Independent Review of Public Sector Relocation, *Well Placed to Deliver? Shaping the Pattern of Government Service*. Report by Sir Michael Lyons to the Deputy Prime Minister and the Chancellor of the Exchequer, March 2004 (ISBN 1-84532-009-3)

16 Qq 10–11, 53

17 Q 12; Ev 13

18 Qq 10, 54–57

value for money, compared with what it would have cost to remain in the existing properties.[19]

10. In the longer term, realisation of wider business benefits will be key to the success of the project. The Home Office have identified a business requirement to deliver an up-to-date, flexible workplace that provides an efficient and effective IT platform and the range and quality of facilities expected of an employer of high calibre staff in central London.[20] The Home Office said that its headquarters staff deliver service to the public by providing effective policy and programmes rather than delivering services directly to customers. The main benefit of the new building was a modern space which was more flexible, leading to better team working and better results.[21]

11. The Home Office was not concerned that increasing the capacity of the new building by 500 would lead to cramped conditions for staff, with implications for morale. Although the space per person was less than for other headquarters buildings such as the Ministry of Defence, these buildings were necessarily more generous because of their historical design **(Figure 4)**.[22] Space per person was also higher in the buildings the Home Office currently occupies. The Home Office felt, however, that at 15.6m^2 per person, the new building would still be an improvement over the existing conditions because the Marsham Street design made more efficient use of space along with improved amenities for staff.[23]

Figure 4: Space per person in 2 Marsham Street is lower than public sector benchmarks

	Net Internal Area (m^2) per person
2 Marsham Street	15.6
Home Office existing estate (on current numbers)[1]	16.2
Home Office existing estate (at Financial Close)[1]	19.4
MOD Main Building refurbishment[2]	19.0
HQ's all sectors[3]	18
DTI[4]	17

Source: 1 Written evidence provided by the Home Office 2 Report by the Comptroller and Auditor General, Redevelopment of MOD Main Building (HC 748, Session 2001–02). 3 Gerald Eve: A study of Occupational Densities in the UK 1999 4 Report by the Comptroller and Auditor General, MoD: Management of Office Space (HC 105, Session 1998–99).

19 Q 2

20 C&AG's Report, para 1.8

21 Q 49

22 Qq 36–37

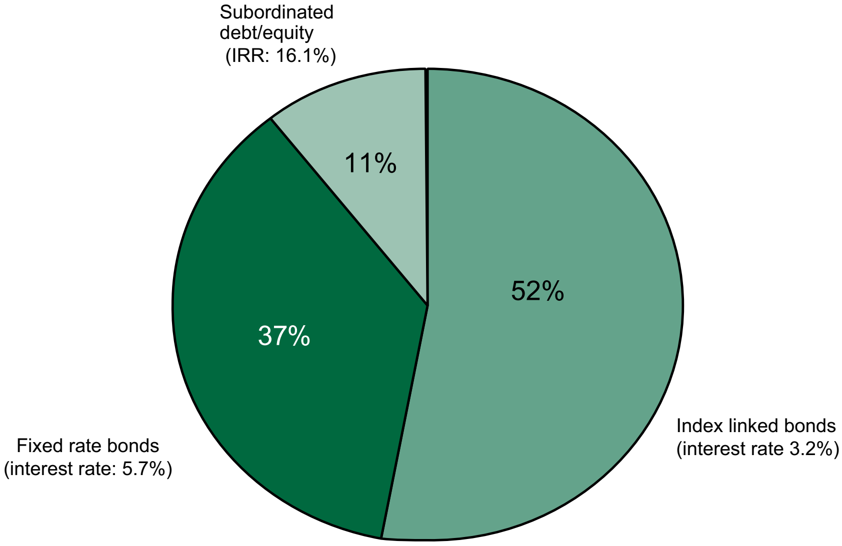
23 Q 37; Ev 14

2 Negotiation of the deal

Sharing refinancing gains

12. The bulk of the external financing for the construction phase of the project comes from two bond issues, supplemented by risk capital in the form of a subordinated loan and a small amount of pure equity **(Figure 5)**.[24]

Figure 5: Sources of external funding



Source: C&AG's Report

13. Ahead of its selection as preferred bidder, AGP had offered the Home Office a 20% share of any gain from a future refinancing of the project. During the period in which the Home Office and AGP were finalizing the details of the project, the Office of Government Commerce was developing guidance for all PFI deals that was likely to recommend that departments seek a 50:50 sharing of future refinancing gains. After consulting the Office of Government Commerce and the then Treasury Task Force, the Home Office decided it would be prudent to comply with emerging policy advice in advance of its publication in July 2002.[25]

14. The Home Office therefore decided to re-open negotiations with AGP with the aim of increasing its share of any refinancing gain from 20% to 50%. Following negotiations, the Home Office and AGP will be entitled to equal shares of any future gains on refinancing. In return, even though the Home Office had no idea what the size of any refinancing gain might be, it agreed to increase the payments to be made to AGP over the period of the contract by £2.75 million.[26] In October 2002, just over six months after financial close, the Office of Government Commerce published details of a voluntary code of practice agreed between the public and private sectors to share refinancing gains 30:70 on PFI deals agreed before July 2002.

24 C&AG's Report, Figure 11

25 Qq 21, 71

26 Q 69; Ev 14–15

15. In assessing potential refinancing gains, the Home Office considered that there was a low probability of refinancing the two bond issues owing to the potentially high cost of buying out the bondholders. If the existing bondholders were bought out, an interest rate reduction of 0.33% would be required to recover the £2.75 million paid to secure a 50% share of the gain. The cost of buying out the existing bondholders could only be ascertained at the time of refinancing. There was considered to be a greater prospect of refinancing by replacing the more expensive subordinated debt with cheaper junior debt. This would only be possible if the market perceived a reduction in project risk and would therefore be likely to occur in the period after successful completion of construction. In this case, the Home Office considered that refinancing would need to achieve an interest rate reduction of around 4% to recover the additional £2.75 million paid to AGP.[27]

Disposal of the existing estate

16. The Home Office still owns three freehold properties in central London, Horseferry, Abell and Cleland Houses. Abell and Cleland Houses, occupied by the Prison Service headquarters, required upgrading and the condition of Horseferry House was poor. The Home Office decided to dispose of the properties itself as the prices tendered by bidders as part of a PFI deal were not considered to offer good value for money.

17. Given recent decreases in the commercial property market in central London, the value of the properties is probably now less than estimated by the Home Office at financial close of the PFI deal in 2002.[28] The Home Office did not think that it would have got a better deal by selling the properties to AGP. The price offered by AGP was around £35 million compared to the Home Office's valuations of £50 million at the time and £68 million at financial close. Since then, the Home Office had not had the buildings valued but it expected their values to be above the price offered by AGP.[29]

18. The Home Office has not yet decided what it will do with the freehold properties. In the short term, accommodation will be needed for staff who do not move to Marsham Street and keeping some of the freeholds is one option. The Home Office was also considering whether the buildings could be sold and better value for money obtained by renting in central London or elsewhere. In any case, the Home Office said that it expected to sell the freeholds eventually.

27 Q 69; Ev 14–15

28 C&AG's Report, para 11; Figure 2

29 Qq 14–17

Formal minutes

Monday 29 March 2004

Members present:

Mr Edward Leigh, in the Chair

Mr Richard Allan
Mr Richard Bacon
Mrs Angela Browning
Mr Frank Field
Mr Brian Jenkins
Mr George Osborne
Jon Trickett
Mr Alan Williams

The Committee deliberated.

Draft Report (PFI: The new headquarters for the Home Office), proposed by the Chairman, brought up and read.

Ordered, That the Chairman's draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 18 read and agreed to.

Conclusions and recommendations read and agreed to.

Summary read and agreed to.

Resolved, That the Report be the Eighteenth Report of the Committee to the House.

Ordered, That the Chairman do make the Report to the House.

Ordered, That the provisions of Standing Order No. 134 (Select Committees (Reports)) be applied to the Report.

Adjourned until Wednesday 31 March at 3.30 pm

Witnesses

List of written evidence

List of Reports from the Committee of Public Accounts Session 2003–04

First Report	Tackling fraud against the Inland Revenue	HC 62
Second Report	The new electricity trading arrangements in England and Wales	HC 63
Third Report	The Sheep Annual Premium Scheme	HC 64
Fourth Report	Improving service delivery: the Forensic Science Service	HC 137
Fifth Report	Warm Front: helping to combat fuel poverty	HC 206
Sixth Report	Department of Trade and Industry: Regional Grants in England	HC 207
Seventh Report	Progress on 15 major capital projects funded by Arts Council England	HC 253
Eighth Report	The English national stadium project at Wembley	HC 254
Ninth Report	Review of grants made to the National Coalition of Anti-Deportation Campaigns	HC 305
Tenth Report	Purchasing and managing software licences	HC 306
Eleventh Report	Helping consumers benefit from competition in telecommunications	HC 405
Twelfth Report	Getting it right, putting it right: Improving decision-making and appeals in social security benefits	HC 406
Thirteenth Report	Excess Votes 2002–03	HC 407
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The reference number of the Treasury Minute to each Report will be printed in brackets after the HC printing number

Oral evidence

Taken before the Committee of Public Accounts

Wednesday 12 November 2003

Members present:

Mr Edward Leigh, in the Chair

Mr Richard Bacon	Jim Sheridan
Jon Cruddas	Jon Trickett
Mr Frank Field	Mr Alan Williams
Mr David Rendel	

Sir John Bourn KCB, Comptroller and Auditor General and **Mr Philip Airey**, Audit Manager, National Audit Office, further examined.

Mr Rob Molan, Second Treasury Officer of Accounts, HM Treasury, further examined.

REPORT BY THE COMPTROLLER AND AUDITOR GENERAL:

PFI: The New Headquarters for the Home Office (HC 954)

Witnesses: **Mr John Gieve** CB, Permanent Secretary and **Ms Margaret Aldred** CBE, Director-General Resources and Performance, Home Office, **Mr Henry de la Monneraye**, Chief Executive, AGP Plc, **Mr Olivier-Marie Racine**, Chief Executive of Bouygues Bâtiment International and **Mr Bryn Jones**, Director, HSBC Infrastructure Ltd, examined

Q1 Chairman: Good afternoon ladies and gentlemen and welcome to the Committee of Public Accounts where today we are looking at PFI, the new headquarters for the Home Office. I do not know whether I should declare an interest, but I live in Horseferry Road, so I see this building going up every day of the week and it is therefore of particular interest to me. We are all obviously impressed that the old three towers have come down, but we are here to discover whether we are getting value for money on the new building. We welcome Mr Gieve, who is the Permanent Secretary at the Home Office. Would you introduce your team at the table, please?
Mr Gieve: On my left, Margaret Aldred, who is Director-General Resources and Performance in the Home Office and oversees major projects and investments for the whole group. To my right Olivier-Marie Racine, who was Director of AGP, the company we are contracted with, and is now Chief Executive of Bouygues Bâtiment International. To his right, Henry de la Monneraye, who is the Chief Executive of AGP and next to him Bryn Jones, who comes from HSBC and is also a director of AGP.

Q2 Chairman: Thank you very much; you are all very welcome. May I start the questioning by referring you to page 11 and Figure 3, where we discover that you are paying an additional £6 million per annum on accommodation running costs. How can you justify this?
Mr Gieve: The comparison here is between what we paid in 2001–02, and what we were then estimating we were going to pay under the PFI deal. The main case for change has been that the £33 million was going up. The following year it was nearly £45 million, this year it has gone down again to £39 million, but we expect it to go up again next year, depending on how much we have to pay on maintenance and so on. Although it is £6 million more than the last financial year when we signed the deal, we think it offers value for money compared with what we would pay for staying in our current property and refurbishing it.

Q3 Chairman: One of the main justifications for moving into this expensive, brand new office block was that you wanted to have all the staff in one building, was it not?
Mr Gieve: Yes, we thought we could get all the staff in one office block.

Q4 Chairman: That is no longer the case, is it?
Mr Gieve: That is right.

Q5 Chairman: You are thinking of moving the entire Prison Service out, or, rather, not letting them in. Is that right?
Mr Gieve: Yes, that is right.

Q6 Chairman: Where are you trying to move them to?
Mr Gieve: We want to unify both the Prison and Probation Service headquarters and we think the rest of the London Home Office will fit in the new buildings. Where are we moving them to? We are considering our options. In the short-term one option is to leave them in Abell House and Cleland House, which are very close to the Marsham Street building and which are currently occupied by the Prison Service headquarters. That provides one obvious short-term option. We are looking at whether we can get better value for money either in

central London or outside London. As part of our review of the scope for relocation under Sir Michael Lyons we are looking at that as well.

Q7 Chairman: We were told originally, were we not, that one of the reasons why the Home Office did not want to be located at the end of the Jubilee Line—and I am rather sympathetic to your senior staff not wanting to be located in docklands, but there we are—one of the attractions, was that you wanted to be in the same building. We now discover that you cannot fit into the same building. Could you not have got your planning a bit better? Could you not have worked out in advance how to have a building which would actually house all your staff? You now say "Don't worry, we'll move Prisons out", but why were we not told this originally?
Mr Gieve: The Home Office has changed, its tasks have changed, its numbers have gone up.

Q8 Chairman: Remind me how much they have gone up by?
Mr Gieve: They have gone up from roughly 3,500 in 1998 to around 4,900 this year. In 1998 when we were making the original projections, we thought numbers were going to fall; in fact they have not, they have gone up. In 2002, before we actually signed the deal and reached financial close, we had to consider whether it still made sense, given that we were not all going to fit into this building. Should we still go ahead with this? We did our calculations and we thought it still offered, and we still think it offers, good value for money, although it is true that not everyone will get in. The only other thing I would say is that during those few years and no doubt during the next few years, the numbers required in the Home Office are likely to go up and down. For example, we have a major review going on at present of our drugs policy and how we should deliver that, we have a major review just coming to an end on corrections, that is the structure and workings of prisons and probation. Both of those are likely to have quite significant implications for our central numbers, as, for example, the changes in machinery of government had in 2001. We have had to plan for a degree of uncertainty.

Q9 Chairman: Sir Michael Lyons has done a review of public sector relocation, has he not?
Mr Gieve: He is in the middle of it.

Q10 Chairman: From what you know about the review and the work which has been undertaken, do you still think that these huge numbers of Home Office staff need to be so close to ministers? We are talking about a building housing 3,000 people for the next 30 years. How many of your staff actually have to deal with ministers, or how many of them are supporting senior civil servants who are actually meeting ministers? Is it 300, 400, 500? It is not 3,000 is it? Do they all need to be in central London?
Mr Gieve: We are examining that as part of the Lyons' review and you are right that there are some transactional services and so on which we can move out, especially if we can get modern IT to work. I do not think it is a question of a few hundred having to be in central London; it is not just ministers they need to talk to, it is Parliament, other government departments and so on. Looking 30 years ahead, I am certainly not going to say we will always require 3,500 staff in central London, but at the moment we are well above that. I could see us contracting in central London, I expect that to happen over a period of years, and we may go below 3,500. In that case, obviously we will be able to pull other people into the building.

Q11 Chairman: When we had the old Scottish Office in Dover House they had a lean, mean staff there, perhaps 30, 40, 50 people. They served ministers perfectly adequately, did they not, in central London while the bulk of the Scottish Office staff were up in Edinburgh?
Mr Gieve: I think it was slightly more than that. It is certainly true that the bulk of the Scottish Office was in Scotland, but London is the capital of England and Britain and we are in charge of England and Wales, so the equivalent to the Scottish Office being in Edinburgh is our being in London.

Q12 Chairman: It would be quite interesting to have a note from you, if I may, because you cannot answer us in any detail now, on just how many staff do need to service ministers and supporting staff of those senior civil servants or need to talk to people here in Parliament.
Mr Gieve: Okay.[1]

Q13 Chairman: Thank you very much. What decision are you going to take on the remaining freehold properties which you are going to get rid of now?
Mr Gieve: First of all, in the short-term at any rate, we have to find accommodation over and above 2 Marsham Street and keeping some of our freeholds is one option to do that. However, we are also considering whether we can sell them and find better value for money, either by renting in central London or elsewhere. In due course I expect to dispose of our freeholds.

Q14 Chairman: At the time a bidder offered to take these properties off you, did he not?
Mr Gieve: Yes.

Q15 Chairman: Since then the market has gone down, so you have lost out, have you not?
Mr Gieve: No.

Q16 Chairman: It would perhaps have been a lot better if you had sold at the time when the bidder made you a reasonable offer.
Mr Gieve: No, I do not think so. The price we were offered by AGP was around £35 million. At the time we thought the properties were worth over £50 million and by financial close we thought they were worth £68 million. That was the basis for that.

[1] Ev 13

Q17 Chairman: What are they worth now?
Mr Gieve: We have not had valuations since then, so far as I am aware, but I still think the price would be above the price we were offered. Obviously we took that risk. At the time we had to make the decision, there was quite a clear gap between our valuation and the valuation we were being offered.

Q18 Chairman: Do you think a refinancing gain is likely on this deal?
Mr Gieve: It is difficult to say. There is some subordinated debt, so in principle you could see some refinancing. There may be a chance to refinance some of the bond finance, although we got a good deal on that.

Q19 Chairman: This was quite unique and I think it is what the Committee would be interested in. You actually paid for this share of the refinancing gain, did you not?
Mr Gieve: Yes.

Q20 Chairman: How much did you pay for it?
Mr Gieve: I am told it was £2 million.

Q21 Chairman: The truth of it is that having paid for it, which is not something other people have felt it necessary to do, because interest rates were so low at the time, it is very likely, contrary to what you said, that there will be no refinancing gain at all. So you have paid for a pup, have you not?
Mr Gieve: You cannot win on that. The very strong recommendation from this Committee, I thought, and the Treasury, was that we should aim to get 50% at least of any refinancing gains. At the time we had done our original deal, we were being offered 20% and therefore we had to re-open the deal in order to get that up to 50%. We were not starting from scratch. We paid a little for that. Yes, there is a certain cost, but on the other hand there is a potential benefit and we thought that having half the potential gain on balance was the right thing to do.

Q22 Jon Trickett: Mr Racine, I understand you are the builder, is that right? Could I ask what you felt at the time of bidding for this were the risks in the construction process which you were taking on? What were the risks, having submitted your bid?
Mr Racine: On this project, as for any PFI project, there are two levels of risk: one is to make sure we deliver a building which is to the client's purpose, control through the design development process and all the iterative meetings we have with the Home Office to make sure what we design fits with what they want and that we stick to what we offered when we submitted our bid. The second major risk for such a project is obviously to deliver the project on time, because it has huge implications for the Home Office. This is critical to us. We have done a very detailed analysis of this risk to make sure we can deliver on time and hand over the building to the Home Office at the time the Home Office requires the building.

Q23 Jon Trickett: I am interested in the construction and demolition and associated risks of the actual building project itself and the comment you made about running to time. Any builder knows that projects can go out of control once you get on site. How do you insure yourself against such a risk becoming an eventuality? What do you do to prevent such an event? Do you defray your risk on the marketplace by insuring, or what do you do?
Mr Racine: No, we have not insured any particular risk associated with demolition. What we did during the bidding process, before and after the preferred bidder, was work out some Plan Bs in case we were delayed on the demolition. It is in fact what happened, because we were quite delayed in the demolition of the rotundas and we were able to reorganise the site to ensure we started the construction of the superstructure in parallel with the completion of the demolition and we also have other ways to make sure we can start the trades inside the buildings earlier to compensate for any delay in demolition. Our solutions are purely technical.

Q24 Jon Trickett: Do you use a process of due diligence in relation to the financiers in this particular matter? Do the financiers require you to do some kind of due diligence in terms of the timing so that things do not slip too badly?
Mr Racine: During the bidding stage, before the deal is closed, the financiers undertake a very detailed technical due diligence and they analyse all our programme for demolition. In fact, at the time we closed this deal all our method statements had been agreed, all the relations with the environment were agreed with Westminster, so we knew exactly what we had to do. This was done. During the works we had detailed reporting to the Home Office on the one hand, the financiers on the other hand, to make sure that demolition was on track.

Q25 Jon Trickett: Mr de la Monneraye, you were nodding in agreement when I was asking about this due diligence process, so probably you were more familiar with the financiers' requirements in relation to this matter.
Mr de la Monneraye: Yes.

Q26 Jon Trickett: I am specifically interested in the risk that the demolition or construction project might have gone badly wrong.
Mr de la Monneraye: To pay the sub-contractor Bouygues and the others I am helped by other consultants in checking the work each month to be sure that we are on time and we are paying the right amount of money and to ensure the funders that completion of the building within the programme is still possible.

Q27 Jon Trickett: So you employ technical consultants who do a due diligence process and then satisfy your sources of finance that the building will be delivered to time.

Mr de la Monneraye: Yes; exactly.

Q28 Jon Trickett: If the builder were to fail, you could take out an action against the people who had given you technical advice.
Mr de la Monneraye: Exactly.[2]

Q29 Jon Trickett: Thank you very much for that help. This is a theme which I have constantly tried to understand in successive meetings about PFI. I feel that the public sector comparator is consistently manipulated so it looks higher than the private sector bid. I believe that has happened in this particular case. Appendix 2 refers to the cost of the building contract and the additional costs which were added to the public sector comparator. Members will no doubt have noticed that £47 million of risk has been added, which by chance happens to make the public sector comparator bid higher than the private sector bid. May I ask Mr Gieve to confirm that actually the two directly comparable figures are the PFI cost and the public sector comparator cost and the public sector comparator would have been lower had it not been for the fact that the risk element was added to it.
Mr Gieve: Yes, that is right.

Q30 Jon Trickett: During the morning I contacted the C&AG, because I was interested to see that nowhere in here was there a reference to the financing costs, which is something this Committee has been interested in. The financing costs are often as high as or higher than the building and other related costs. It might be as well to ask the C&AG give us an indication. I asked two questions really. One was: what was the interest which might have been charged if we had used conventional public sources of finance and what was the interest being charged on the PFI, neither of which figure appears in this Report? Then I asked what the difference was in the financing costs in the aggregate between the public sector model and the private sector model. I wonder whether the C&AG could give us the response. I know there are several *caveats* to the analysis, but nevertheless I think it is instructive to get it on the record.
Mr Airey: That is a very good question. The figures I gave you are indeed very *"caveated"*. What we have here is a deal which is funded by the private sector at about 0.7% above a gilt rate. Doing a simple calculation on those terms and adding in the costs of fees for the private sector finance, we have come up with a very provisional figure of a maximum of £33 million additional cost for doing this deal as a PFI project rather than a conventionally funded project.

Q31 Jon Trickett: My understanding is that if we had used conventional public sector finance, it would have been in the ballpark of just above £30 million less than the private sector are charging us, but that is at present day prices. We then came back to ask you what the actual costs would be exceeded by between the two forms of funding. I think you gave us that figure as well. I just want to get that on the record, if you would not mind giving us that, please.
Mr Airey: Obviously the £33 million figure is a net present cost figure. We are dealing with cash flows going out 30 years from now, so the cash figures do not give you quite the right answer. It is a larger figure and I do not have it easily to hand. It is about £60 million.

Q32 Jon Trickett: Yes, £60 million was the figure I was given. It will cost more to finance through the PFI than it will to do through the public sector comparator, given all the equivocations which I do not want to spend time putting down. There are certainly some equivocations. I think it is in the order of £60 million additional cost and a £47 million figure which has been added as risk; maybe in the order of £100 million difference. On some of the matters, as I have just indicated by the discussions I had with the constructor, it seemed to me that the risk could actually have been defrayed in the way the private sector did. Had you considered that to a Member such as myself, it might well appear that the public sector comparator figure has been deliberately manipulated to make it appear higher than the PFI figure in order to justify you going out, perhaps for other reasons, to a private finance initiative? What would your comments be to me in relation to that matter?
Mr Gieve: It had occurred to me that you might think that, but it is not right. We have, the Treasury in particular, undertaken a large number of studies about the costs of doing public sector construction projects and the figures I have seen most recently, which were presented to this Committee, have shown that the average overrun has been 47% in capital cost and 17% in time. You are absolutely right that the PFI company, because it is a company not the government, has to pay a higher cost for finance than we do, but in return the reason for us going into private finance is that broadly we get a greater certainty on timing and cost overruns than we think we would with the public sector version.

Q33 Jon Trickett: I do not know how to achieve this, but could we get someone to provide us with a note as to whether the mechanisms on due diligence—and I have asked for this before and I have not received the information yet—which the private sector financiers use to secure certainty in the building projects might well be the same kind of tools which would be available to the public sector, thereby securing delivery on time and lower financing costs?
Sir John Bourn: I should be happy to provide that note and do it in consultation with the Treasury as well as with the Home Office in this particular case.[3]

Q34 Jon Cruddas: May I go back to one of the initial questions as regards staffing levels and the projections which have been worked on at different stages of the process? On reading the Report, as I

[2] Ev 13

[3] Ev 13–14

understand it, in 1998 it was estimated that the head count, including the Prison Service, would be 3,200. That was revised down to 2,920. At the time, the head count for the new building was assumed to be 2,950 and that was revised up in the year 2000 to 3,450. So far that is correct. Between 1998 and 2003, the head count was revised up therefore from 2,950 to 4,900. Could you just give us a flavour of why there was such a dramatic increase in the staff of the Home Office?
Mr Gieve: Yes. Starting with the figure of 2,900, that was a projection at that stage which was based on estimates by Derek Lewis when he was head of the Prison Service, among others, that we would see a further reduction from an actual figure of around 3,500 at the end of 1997–98 to a figure first of 3,200 in 1998–99 and then on down to 2,900. In fact, as far as I can find, we never got as low as 3,200. We stuck around 3,500 at 1998. What has happened since then? There have been some changes in boundaries and we have been given some new tasks. If I might just run through the main increases, we have created a National Probation Service with a National Probation Directorate in the Home Office; that accounts for about 300 of the difference. We have created a trilateral criminal justice team working to three ministers: the Department for Constitutional Affairs, the Attorney General and the Home Office. It is in the Home Office and has about 150 people in it. The prison population has gone up and so has the headquarters, by about 150. We have taken in the Drug Co-ordination Directorate from the Cabinet Office; that is about 200. We have increased our numbers both on policing and crime reduction. The Home Office has been given specific targets to reduce crime and we did not have many people working on that, as opposed to policing, before 1998, so we have increased those numbers and also the numbers working on terrorism. Those are the big increases I can give you, but there has been an expansion.

Q35 Jon Cruddas: From 1998 you were anticipating that the building would accommodate some 2,950.
Mr Gieve: Yes.

Q36 Jon Cruddas: Then in the year 2000, the specification was renegotiated to hold an extra 500. Figure 5, page 15, talks about planned space per person in 2 Marsham Street, compared with other public sector benchmarks. I assume that this table is now on the basis of the anticipated population of 3,450. Have you got a figure for the density or person per square metre of the initial 2,950? Would that have exceeded these benchmarks rather than come under? What I am saying is that I want to get into how these changes have been made in terms of the extra 500, in terms of the density of the people in the building. The initial objective behind the new build was a better working environment. What are the implications here, given that the densities here are quite significantly under the benchmarks for MoD Main Building refurbishment and HQs in other sectors, the DTI and the like? What do you think are the implications, for example, for staff morale or the nature of the work environment here compared with how you initially envisaged it?
Mr Gieve: The answer to your first question is that it would be just over 17 square metres. So it was anyway below the MoD and some other headquarters buildings. Buildings like the MoD or the Treasury are very spacious buildings and cannot but be given the historic design. The answer to that I suppose is that they are more generous because of their historic design. At 15.5 square metres, we think the building will still offer a massive improvement in staff conditions compared with the buildings we are currently occupying.

Q37 Jon Cruddas: Do you have an estimate for what the present Home Office density would be, because it is notoriously cramped, is it not?
Mr Gieve: We are spread over quite a number of different buildings and they all have different square metres. May I send you a note on that?[4] It is not just the space surround that matters, it is also the lighting, the atmosphere, whether it is hot when you want it to be hot and so on.

Q38 Jon Cruddas: Going back to the forecast in terms of employment levels in the Home Office, the actual growth exceeded the projected growth, or the decline you initially touched on, in both 2000 and 2001. Do you have a fixed projected head count for 2005?
Mr Gieve: No. We are currently working on a strategic plan for the whole Home Office group for five years. We hope to have that finished by the end of this year as the basis for our spending review bid. As part of that exercise, we are reviewing all our headquarters numbers, not just for the Lyons' review on relocation but also to see whether we can streamline the headquarters and shift more resource into the front line. I do not have a fixed projection. I would expect that to come down substantially, but I do not know by how much.

Q39 Jon Cruddas: In all of those three periods, the actual has exceeded the forecast quite dramatically. Do you anticipate any eventuality where you would have to get more people inside the new build in 2005 than the 3,450, which is 500 more than the initial estimate itself?
Mr Gieve: The capacity of the building at 3,450 is pretty fixed by the planning consents, as well as by the design of the building. I do not know about the margins around this, but I do not see us shoving more and more people in.[5]

Q40 Jim Sheridan: May I say at the outset that coming from Scotland I am a bit sensitive about lecturing anybody about new buildings, given that the Scottish Parliament was slightly over budget? May I draw your attention to paragraph 6, page 2, which says "The Home Office also identified other potential accommodation" but it was too expensive. Where was that accommodation?

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[4] Ev 14
[5] Ev 14

Mr Gieve: We looked at a number of other central London locations, including a big site which is being developed off Victoria Street at the moment. We also looked at the possibility of moving to docklands.[6]
Ms Aldred: I do not have a complete list with me, but I could provide one.

Q41 Jim Sheridan: Were all the locations in central London?
Ms Aldred: We did look at locations elsewhere in London, including in docklands, which may have fallen into the unsuitable category. I do know that at the time people felt that location outside the division bell area was not suitable.

Q42 Jim Sheridan: Why?
Ms Aldred: Because ministers would not want to be located outside the division bell area and the idea was to try to get from six buildings, as we were then, to one building.

Q43 Jim Sheridan: This building is to accommodate ministers.
Ms Aldred: Yes.

Q44 Jim Sheridan: Solely ministers.
Mr Gieve: And a few others.
Ms Aldred: And one or two others.

Q45 Jim Sheridan: Following on from the point the Chairman made earlier, given all the new technology, video conferences, *etcetera*, why do we need to be based in central London when the Home Office serves the whole of Britain?
Mr Gieve: We are not entirely based in London; in fact the majority of our staff are outside London, spread around the country in prisons, ports, major office developments in Liverpool, Sheffield and Leeds. Nonetheless, it is a good question: could we shift more people out of London? Would that offer value for money? That is what we are looking at at the moment. At the time we entered into these negotiations back in the mid 1990s, we did not examine relocation of a substantial amount of staff at that stage. We had done in the early 1990s and indeed we had been about to move the prison headquarters to Derby, but that was cancelled in 1993 because the then Home Secretary did not believe he could afford the upfront cost of moving. We had considered moving the Passport Service to York in 1996, but again the finances did not work out. That was the background against which we planned to keep the headquarters in London. That is what we are looking at again now.

Q46 Jim Sheridan: If I understood you correctly, you are looking at perhaps moving out of London in years to come and taking more staff out of London to the rest of the country. Is that correct?
Mr Gieve: Yes, we are looking at a number of possible options in the corrections area but also in other parts.

Q47 Jim Sheridan: Page 15, paragraph 1.28 is suggesting that in 26 years' time you will be able to move more people into Marsham Street.
Mr Gieve: I did not read it as saying that. The point there is about home working and remote working, hot-desking and so on, whether we can fit a greater gross number of staff in the single building on the assumption that only 3,500 are there at any one time. We do a bit of that at the moment, but that may expand.

Q48 Jim Sheridan: Do you understand where I am coming from? People from north of Watford have a perception that civil servants suffer a nose bleed if they go north of Watford.
Mr Gieve: We have many, many civil servants working north of Watford and they do not all have nose bleeds.

Q49 Jim Sheridan: May I take you to page 11, paragraph 1.8? Correct me if I am wrong. I have looked through this Report and it does quite rightly talk about staff, flexibility, Russian practices, *etcetera*, but I have still to find mention anywhere of improving services to the public and the customer. This paragraph says "Providing a better service to visitors and public by provision of fit for purpose fully serviced central conference and press facilities situated close to main entrance to enable good security with ease of access". They will be dancing in the streets of Inverness knowing that all that facility is there in London.
Mr Gieve: Most of our headquarters staff deliver service to the public by providing effective policy and programmes which issue in the front line. It is delivery that counts. The main benefit of this building—and my colleagues in the Treasury who have recently moved into their renovated building have been very encouraging on this—is having a modern space which is more flexible and leads to better team working and better results. The better results obviously should be apparent to the public. We do not have many services directly offered from the Home Office HQ, except for visitors and press and so on.

Q50 Jim Sheridan: I do not wish to be rude, but I do detect that there is a mental block there which suggests that you need to be located in central London for no other reason than to accommodate ministers. That is just a view.
Mr Gieve: I can see what you are saying.

Q51 Jim Sheridan: Those who send nuclear submarines to Scotland keep the Civil Service jobs in London and people get a little upset at that kind of thinking.
Mr Gieve: Yes, that is why we are looking at relocation at the moment. I expect, if we can raise the finance up front to finance the move, there are things we should move out of London and that is what we are looking at.

[6] Ev 14

Q52 Jim Sheridan: On the question of finance, paragraph 10, page 3 says this site will accommodate new residential and commercial developments, for instance affordable flats. How much will that cost the taxpayer and who will occupy these affordable flats?
Mr Gieve: It is not going to cost the taxpayer anything in that AGP are separately developing the residential property and have reached an agreement to sell that on to a private sector housing company, Galliard.
Ms Aldred: The affordable housing will be owned by the Threshold Housing Association.

Q53 Mr Rendel: May I pick up first of all the point Mr Sheridan was making about who needs to stay in London and who does not? As I understood it, when Ms Aldred was asked the question she indicated that the reason for needing to be very close to the centre of London was that you needed to be within division bell area and basically the only people who need to be within division bell area are actually Members of the House who have to get in for divisions. Therefore it seems, given that we have a few ministers in your department, we are accommodating now 3,500 people in a building within division bell area for the sake of the three or four ministers who are going to need to get into the House of Commons when a division bell goes. Is that correct?
Mr Gieve: No, that is not correct. Obviously Parliament's location is important because the ministers need to be supported by staff. There are in fact seven ministers in the Home Office and they do need to be within easy reach of Parliament. Other officials have a lot of dealings with Parliament and with other government departments, most of whom are located here. We have experience of this. We moved most of the Immigration Department out of central London to Croydon, Liverpool, Sheffield and Leeds and we would not reverse that, but it certainly does cause problems and we have people more or less permanently on trains or hot-desking in central London.

Q54 Mr Rendel: Have you ever done an analysis of what the cost of moving people around for meetings is as compared with the capital cost of building within division bell distance?
Mr Gieve: No, but it is not so much the cost of train tickets, it is the cost of disruption and lack of service that would be the problem.

Q55 Mr Rendel: You have not done a financing cost. You have not checked whether it is actually cheaper to have people moving around rather than building a building.
Mr Gieve: That is precisely the exercise we are engaged on now.

Q56 Mr Rendel: Are you considering also the possibility of using more hi-tech equipment and having video conferencing and so on?
Mr Gieve: We do have some video conferencing, yes. Yes, we do look at increasing that.

Q57 Mr Rendel: I have to say that it staggers me that in this day and age it could still be more financially beneficial to keep 3,500 people in central London just because you need to have the ministers there and perhaps a few officials who directly service them. I should be very interested to see the results of your review, but if it comes out saying yes, you do need those 3,500 in central London I shall be absolutely amazed. That will depend on the results of the review. May I turn now to Figure 3 on page 11? Where in this comparison have you, if you have, included the benefit of being able to sell off some of your current estate if you move from the existing estate into the new building?
Mr Gieve: The main difference is that we will not be paying a capital charge. If you look at the top half, we have a capital charge on our existing properties which we will not have under the new arrangement.

Q58 Mr Rendel: Is that capital charge effectively what you expect to be able to get in notional interest from the money you will bring in from selling off the buildings?
Mr Gieve: No, the capital charge is the conventional charge we pay off our estimates to the Treasury, which is a percentage of a valuation.

Q59 Mr Rendel: If the notional value of the interest you make on the value of the properties you are selling off is greater than that, that has not been included in this calculation. If it is less than that, then you have overestimated for the value.
Mr Gieve: Yes; that is right.

Q60 Mr Rendel: That seems to me to be a very odd way of doing it.
Mr Gieve: I will have to come back to you.[7]

Q61 Mr Rendel: If I may say so, you are using an artificial charging basis, this capital charge—and I understand how it is done and why it is done under resource accounting—but it seems to me that the real value of moving is going to be the value of that notional interest you could gain on the capital sum you receive when you sell the buildings rather than any notional capital charge which is a rather artificial figure in some ways. I am surprised you use that. I am therefore surprised in a sense: if that is the only capital cost you are putting in here, I now understand how you can work out whether it is worth moving or not without having the slightest idea what you are going to get back for the buildings you are intending to sell, or the freeholds of those sites. It struck me as very odd that you could work out which was the better value for money without knowing how much you were going to get back for those sites. I now understand why: because you have not actually included that in the calculation. It seems an odd way of doing it.
Mr Gieve: This comparison, which is a straight comparison of what we paid in 2001–02 and the estimate of the unitary payment, was not the basis of the value for money calculation. That was based on

[7] Ev 14

a projection of our costs over the 30 years of the contract, including the cost of refurbishment, decant and so on, which we will incur if we do not build a new building.

Q62 Mr Rendel: Half a second. When you were asked by the Chairman why you thought it was worth while, given that apparently the current costs were £33 million and the new costs £39 million, you said actually this £33 million goes up in future years and you did seem to be justifying the move on the basis of that comparison.
Mr Gieve: This particular figure is not part of the projection, but yes, absolutely, the point I am making is that we did model the cost on a comparable basis of getting AGP to build and then paying for the new building and being able to vacate other buildings, against the full costs of staying in those other buildings and that is the basis which is reported in this Report in paragraph 2.11.

Q63 Mr Rendel: Appendix 2, Figure 13, is saying that when you were doing that analysis that is a different analysis from the one in Figure 3 and in Figure 13 you included the actual cost of selling off the properties, as opposed to the notional capital charge.
Mr Gieve: Yes. May I just make that clear? Figure 13 compares the cost of building a new building on a conventional public sector procurement and a PFI deal. That was one comparison. There was also a comparison between getting a new building and sticking with the buildings we have. That is reported in here in paragraph 1.20 and the estimate of the net present cost is £578 million for not having a new building, compared with the cost of the PFI deal. That was based on calculations like the one you have pointed to, but for a different set of years.

Q64 Mr Rendel: May I move on to talk about the refinancing? What was the interest rate at which the financing was being done which was your basis for deciding how much the refinancing might be worth to you?
Ms Aldred: I am not sure I quite understood the question you want us to answer.

Q65 Mr Rendel: There is a financing cost for going ahead with the deal, which the company were presumably taking on, where you were financing it and there was then the possibility that they would do a refinancing, which presumably means that they would hope they might refinance at a lower interest rate. What was the interest rate you were using, that you were assuming they were taking on their original finance at?
Ms Aldred: I am not sure I do have that figure.
Chairman: It seems to be a pretty basic question.

Q66 Mr Rendel: The issue is clearly that you decided that it was worth putting into the contract a refinancing clause which says you are going to get 50% of the refinancing benefit, if there is such a benefit.
Mr Gieve: Yes.

Q67 Mr Rendel: Presumably, in order to work out whether that was worth it or not, you must have done a calculation as to the likely value of the 50% refinancing benefit you might get and in order to do that you must have known what the original financing was going to cost and what chance there was of that being refinanced at a lower value in order to balance that against the extra cost you were paying. To do that, you must have known what the original interest rate was and then you must have taken a guess as to what the most likely reduction in that interest rate was when a refinancing was done.
Mr Gieve: We do know what the debt charge was on the different tranches of debt and they are reported in this Report. Yes, we did model some variations. It is very difficult to foretell exactly which way the market is going to move, but we did do some illustrative models.

Q68 Mr Rendel: If it moves upwards, you have no refinancing gains.
Mr Gieve: That is right. You get a refinancing gain for two reasons: the market may move, but also, as the project becomes less risky than at the point of contract, the contractor may be able then to refinance at a lower margin. We did model that and there is a range of uncertainty and it was a judgment about whether it was worth paying a little bit more for a potential gain. Yes, we did do that modelling.

Q69 Mr Rendel: You said a moment ago that the cost of the refinancing deal was £2 million. We were told £275,000 per year but I suppose that is very faintly comparable. I guess it would be very interesting to see what you originally saw as the interest rate at which the original financing was done and thus what that would have had to fall to in order to make it worth while for you to go for 50% of the financing.
Mr Gieve: I will let you have a note.[8]

Q70 Mr Rendel: I should be grateful if you would and I should be grateful if you could prove to me that the likely refinancing gain you expected at the time was more than the £2 million you have spent on it. If it was not, I wonder why on earth you did it.
Mr Gieve: There is a range of possibilities.

Q71 Mr Rendel: Indeed; but you must have had some estimates of what was likely to happen in order to make it worth while doing that deal.
Mr Gieve: Absolutely; we did look at that. We also took account of the fact that at the point we were doing this deal, the Office of Government Commerce issued binding guidance that deals like this had to achieve a 50% share of refinancing gains. That was being issued at the time we were doing the negotiations. So there was a question over whether we moved or whether we did not.

[8] Ev 14–15

Q72 Mr Rendel: Is it correct that we said they had to? I thought it was our advice that they should try to?
Mr Gieve: I think it is Treasury guidance.
Mr Molan: The OGC promulgated advice in 2002.

Q73 Mr Rendel: But presumably if it is not worth it, if you cannot get a deal which makes it worth it, you would not do it.
Mr Gieve: Exactly.

Q74 Chairman: We are not going to have an argument about this. When this started, interest rates were much higher and companies were making huge profits from refinancing. Of course this Committee recommended departments should look at it and should proceed down that route. We never recommended that you should pay for refinancing if interest rates were so low that there was unlikely to be any refinancing at all. You cannot throw that back in our face.
Mr Gieve: I was not throwing it back in your face. I was just explaining how we approached this.

Q75 Mr Bacon: How much is the annual unitary charge?
Mr Gieve: The final annual unitary charge has yet to be determined because it will depend on inflation and on further variations.

Q76 Mr Bacon: Yes, I realise that. When you move in in 2005, what are you expecting to pay in your first year as a unitary charge? Page 11 says £39.2 million. Is that per year?
Mr Gieve: No, the unitary payment is part of that which is £30.3 million a year. It is the first column.

Q77 Mr Bacon: That is what you are expecting to pay as the annual unitary charge.
Mr Gieve: Subject to any variations.

Q78 Mr Bacon: Yes, subject to inflation. What is the inflation presumption in your model?
Mr Gieve: I think we are assuming 2%.

Q79 Mr Bacon: 2.5%?
Mr Gieve: We are not—

Q80 Mr Bacon: Treasury building was 2.5%, so was the MoD building. I am just asking whether it is the same.
Mr Gieve: I think it is a bit under 2%, but I will check that.[9]

Q81 Mr Bacon: Assuming the inflation assumption you have in your model, what is the total amount of cash? For how many years are you expecting to make the annual unitary payment? You are not moving in until 2005. Is it for 26 years?
Mr Gieve: It is for 26 years.

Q82 Mr Bacon: So you are expecting to pay £30.3 million per year for 26 years plus inflation. Is that correct?
Mr Gieve: Yes.

Q83 Mr Bacon: Using your inflation assumption what is the total cash you expect to pay out? Without inflation it would be £30.3 million × 26, which would be £787 million. I am asking, if you add on inflation, where would you get to?
Mr Gieve: We index by 75% of the RPI. I do not have the cash number.

Q84 Mr Bacon: I do not have a lot of time. In the Treasury building they are paying out £14 million for 35 years which comes out at £491 million; if you add inflation they are expecting £838 million. In the MoD building they are paying out £55 million over 30 years which comes out at £1.65 billion; if you add on inflation they are expecting to pay £2.514 billion. I am asking what your numbers are.
Mr Gieve: I do not have that number.[10]

Q85 Mr Bacon: If you could put in a note, that would be great.[11] What is your discount rate, 6%?
Mr Gieve: It was 6% when we did the deal.

Q86 Mr Bacon: So that is what is in this contract.
Mr Gieve: It has now changed.[12]

Q87 Mr Bacon: Yes, but what is in the contract, your working assumptions.
Mr Gieve: The working assumption is 6%.

Q88 Mr Bacon: May I ask you to turn to page 19, paragraph 2.8? It says that this payment, equivalent to a £275,000 increase in the annual payment to the consortium, allowed a 1.1% increase in the internal rate of return. What is the total internal rate of return now?
Mr Gieve: This is the internal rate of return on the equity.

Q89 Mr Bacon: No, no. I want the internal rate of return on the whole project.
Mr Gieve: The equity return was 1.1% which was additional to 16% which was the calculated return on equity.

Q90 Mr Bacon: So it is now 17.1%, is that right?
Mr Gieve: That is right. Sorry, 15% + 1.1% = 16.1%.

Q91 Mr Bacon: On page 17 it says that professional fees amounting to £9.1 million are payable. Is that little schedule there all the professional fees which will be incurred by the Home Office for this project?

9 Ev 15

10 Ev 15

11 Ev 15

12 Ev 15

Mr Gieve: Yes; I believe so.[13]

Q92 Mr Bacon: What are the fees to be paid by AGP? The Home Office is paying £9.1 million and I am asking what fees you are paying.
Mr Racine: Are you asking us how much it cost us to prepare the bid?

Q93 Mr Bacon: The Home Office incurred costs for professional fees and they are listed in this schedule here. When I asked the Treasury this question, they said that their costs amounted to £3.2 million and that the costs of Exchequer Partnership, which is the contractor for that building, were £22 million. On the same basis I am guessing roughly that the Treasury building's fees were 12.7% of the total fees, so the professional fees you are paying would be in the region of £62 million.
Mr Racine: No.

Q94 Mr Bacon: I am asking you what they are. I am guessing.
Mr Racine: In the region of £9 to £10 million.

Q95 Mr Bacon: In total? Is that for everything?
Mr Racine: Yes.

Q96 Mr Bacon: Is that including all the consultants, advisers, insurance, quantity surveyors, architects, accountants, legal advice?
Mr Racine: It is the external costs for our consultants, but it does not take into account our own internal costs for the bid, all the people from the company working on the bid.

Q97 Mr Bacon: Does it include the cost of the bond finance?
Mr Racine: No.

Q98 Mr Bacon: So the £9 million you have just referred to does not include the bond finance. The reason why I am asking for a total figure is that I want to know what the total figure is, not a partial figure. To give you an example, because what I am really looking for is the analogous figure, the Treasury's costs were a total of £3.2 million and the other costs, including bank finance when that company raised its money for the Treasury building, total costs, for everything, including the cost of raising the finance on the bond market, including the quantity surveyors and everything else, was £22 million. You are telling me that your costs are £9 million, but you have now told me that excludes the cost of the bond finance. What I am after is the analogous figure, the total for your professional fees payable to everybody, be they bank, insurance broker, engineer. Do I make myself clear?
Mr Racine: Okay. Including insurance it would add up to roughly £25 million.

Q99 Mr Bacon: In total £25 million.
Mr Racine: It includes the cost of finance and insurance.

[13] Ev 15

Q100 Mr Bacon: Would it be possible for you to send us a schedule with an itemisation?
Mr Racine: Yes.[14]

Q101 Mr Bacon: I should like to ask about risk. I found the chart on page 31 less than completely clear, especially compared with the one which was in the Ministry of Defence building report, which seemed a lot easier to understand. When it says the total risk is 9%, the first thing I want to ask is in the Ministry of Defence report on page 24—I know you do not have it with you—the key point is that the total risk as a percentage of the base costs was 17%. Why does the Home Office building have such a lower percentage risk. What is the analogous figure to the £311 million? In the Ministry of Defence report they talk about a net present cost of the project of £746.1 million, whereas the public sector comparator was £746.2 million. Here it says at the beginning that the net present cost of this project is £311 million. That is right, is it not? Page 1 says ". . . it will begin paying AGP a monthly charge for the building and associated services amounting to £31 million (net present cost)". I have a comparable figure to that £746.1 million, which is the net present value of the MoD building, as a public sector figure, but in this Report, it just says not available. Can you explain that? This is on page 31, down at the bottom, on the right-hand side. There is the £311 million, the cost of the PFI transaction, but it says the public sector comparator is just is not available. Underneath it says £460 million and £494 million. What actually is the net present cost of this project? Is it £311 million or is it £460 million?
Mr Gieve: The cost of the project is £460 million, that is the PFI comparator to £494 million public sector comparator.

Q102 Mr Bacon: So there is this big difference because there is a whole load of costs you are retaining.
Mr Gieve: That is right.

Q103 Mr Bacon: What are they?
Mr Gieve: There are public sector costs and there is also a risk adjustment on the PFI, a small one.

Q104 Mr Bacon: Do you think you could study page 24 of the Report on the MoD building and produce for us a schedule which shows the public sector comparator broken down by category, with the item and its net present value, the base costs, the risk, the risk as a percentage of the base costs and then totals at the bottom? It is a much clearer way of doing it than we have seen so far. It would be very kind, if you would do that.
Mr Gieve: Yes.[15]

Q105 Mr Bacon: Mr Racine, why are you willing to instal the IT infrastructure but not to maintain it?
Mr Racine: I am not sure I was willing to do it: I was asked to do it.

[14] Ev 15
[15] Ev 15–16

Q106 Mr Bacon: You decided you would.
Mr Racine: It was asked of us in the bidding process.

Q107 Mr Bacon: You are a construction company.
Mr Racine: Yes.

Q108 Mr Bacon: What experience do you have of installing IT infrastructure?
Mr Racine: Quite a lot of experience of installing IT infrastructure, because it is base infrastructure; of designing an infrastructure system, not a lot, because it is not our area of expertise.

Q109 Mr Bacon: It is not your area of expertise?
Mr Racine: Designing IT systems is not.

Q110 Mr Bacon: It is not; I would not have thought it was. Nonetheless you are installing the infrastructure.
Mr Racine: Yes, which is quite normal in the construction process.

Q111 Mr Bacon: But you are not going to maintain it.
Mr Racine: It is not part of our contract.

Q112 Mr Bacon: Is this part of a wider investment in IT in the Home Office? If so, what is the total cost?
Mr Gieve: We have a 12-year contract with a consortium called Sirius which provides our IT. We expect Sirius to maintain and move the IT from our existing building into the new building, although we have not yet completed those contractual negotiations. It will be part of a wider one. As to the full cost of the Sirius programme . . .
Ms Aldred: I do not know that because it has changed and it depends on how many people use it and the services.

Q113 Mr Bacon: A ballpark figure.
Ms Aldred: I do not have a ballpark figure.
Mr Gieve: Sirius supply us not just in London but in all the ports and Croydon, Liverpool and so on. We will give you a figure.[16]

Q114 Mr Bacon: How much is the cost of the IT infrastructure as part of this building which is being installed by Bouygues?
Mr Gieve: The £2.35 million is the cost we have agreed for installing the cabling and the patch management of the system.[17]

Q115 Mr Bacon: The total is £2.35 million.
Mr Gieve: Yes. That does not include the cost of all the boxes.

Q116 Mr Bacon: Are they installing that as well?
Mr Gieve: They are installing the cabling and the system for managing the cabling, but the actual boxes will come from someone else.

Q117 Mr Bacon: What I am really asking is: what is the total cost for what they are doing?
Mr Gieve: It is £2.35 million.

Q118 Mr Bacon: That is the cabling and the systems.
Mr Gieve: That is the cabling.

Q119 Mr Bacon: You just said the cabling and the system for managing the cabling.
Mr Gieve: I was referring to something I do not understand called the patch management system, which allows us to vary the cabling and the positioning of the boxes later on. Broadly, this is the cabling system that they are installing in the building.

Q120 Jim Sheridan: Back to the question about the site of the separate residential and commercial development. Just to clarify. When I asked the question, I think you said they would be the responsibility of a housing association. I also asked who, if anyone, would be living in the houses? What I really want to know is whether it will be civil servants, senior or otherwise, who will be living in these houses, or will they be open to the general public?
Mr Gieve: It is a mixture of private sector and low cost housing and full market rents and low cost housing. Civil servants will be able to apply like anyone else, but we are not reserving any of this for the Home Office.

Q121 Jim Sheridan: They are not exclusively for civil servants.
Mr Gieve: No.
Ms Aldred: There is no formal link between the two. The site is 75% commercial development and 25% social housing which is being passed to a housing association called Threshold. It, I assume, will be housing the people in accordance with its charitable aims.

Q122 Mr Bacon: Mr Jones, can you say why the index-lined bond market collapsed last summer?
Mr Jones: I cannot really comment on why that happened.

Q123 Mr Bacon: You cannot comment on why it collapsed.
Mr Jones: No. I think there was some linkage to some changes in the way pensions were calculated, but apart from that I would not really know.

Q124 Mr Bacon: Do you think the appetite of investors for index-linked bonds of this kind might have had something to do with it?
Mr Jones: If you are referring to some of the transactions—

Q125 Mr Bacon: I am thinking of the Derby Hospital one which has been restructured.
Mr Jones: There were various reasons why that happened. A large bond launch happened in the week before that occurred and therefore investors who were looking to invest in index-linked bonds

[16] Ev 16
[17] Ev 16

would probably have already made their allocation. Hence their allocation for Derby would have been lower.

Q126 Mr Bacon: How important do you think the fact that investors had a lot of this stuff and were getting a bit sick of not being able to see through and assess the credit rating of the underlying transaction for themselves, the lack of transparency? People like Standard & Poor's were saying that was an issue.
Mr Jones: I can only really comment on the Home Office transaction.

Q127 Mr Bacon: I am talking about in general in the market.
Mr Jones: Sure, but in my experience of the Home Office transaction, we were part of the road show of investors which went out to discuss—

Q128 Mr Bacon: Yes, but this was an early one, was it not?
Mr Jones: In some ways the point you raise in terms of transparency is a valid one. Certainly in the brochures we did, we got a lot of pressure and a lot of comment from investors that they did want transparency. What we are seeing is that they are becoming a far more sophisticated bunch of people. They do understand it and they understand what the underlying quality of the projects are.

Q129 Mr Bacon: If you were trying to get a bond like this away now, you could not, could you?
Mr Jones: The quality of the product here, the way this project was structured, I see no reason why the Home Office transaction will go away today.

Q130 Mr Bacon: Even now? Last week they did a bank loan for the Middlesex Hospital, did they not?
Mr Jones: We did.

Q131 Mr Bacon: They did not do an index-linked bond.
Mr Jones: No, we did not. AGP were part of that transaction as well.

Q132 Mr Bacon: But it was not a bond, it was a bank loan.
Mr Jones: No, it was not a bond. The reason why it was not was predominantly because of the size of that transaction; it was a transaction of about £80 million bank debt. Generally what we find is that there is a cut-off threshold at which the bank and the bond become better value for money. I would say above about £120 million the bond generally becomes better value for money and below that a bank deal.

Q133 Mr Rendel: When was the demolition originally due to be completed?
Mr Racine: November. Due to be completed? Sorry, August this year.

Q134 Mr Rendel: When was it completed?
Mr Racine: Let us say two months after August.

Q135 Mr Rendel: The briefing we have had from the NAO, Mr Gieve, tells us that you told them that AGP did complete demolition in August and that was nearly three months ahead of schedule. It sounds as though they did not complete it in August and that it was two months behind schedule.
Mr Racine: May I comment on this?

Q136 Mr Rendel: If you like, if you can get Mr Gieve out of his problem.
Mr Racine: Just to explain. When the demolition was completed in August, in the basement there are some huge rotundas which are very difficult to demolish.

Q137 Mr Rendel: I noticed them. I live close to the area.
Mr Racine: We were stuck in one particular area of the site for longer than this, but it did not prevent us from starting the works as planned in our schedule, which means that the information given is correct.

Q138 Mr Rendel: The demolition was later than expected. Mr Gieve, can you still explain to me why you apparently told the NAO that the demolition was completed in August and that was three months ahead of schedule?
Mr Gieve: It sounds as though that was a mistake, if that is what we said.

Q139 Mr Rendel: Would the NAO like to comment on that? Part C of your briefing appears to say that the Home Office told you that it was completed in August, three months ahead of schedule. Can you confirm that was what you were told?
Mr Airey: Yes, that is right.

Q140 Mr Rendel: Perhaps, Chairman, we might like to ask Mr Gieve whether he can go back to whomever gave that information and let us have a note on why wrong information was given.
Mr Gieve: Yes.[18]

Q141 Chairman: A couple of wrap-up questions. Mr Racine, what are the main challenges which face you in getting this building ready for occupation by 2005? What keeps you awake at night?
Mr Racine: The programme.

Q142 Chairman: The programme? Elaborate.
Mr Racine: It is a tight programme, so we have to be sure that everything happens on time, make sure that we can deliver the building in good condition in January 2005.

Q143 Chairman: Is there anything you would have done differently?
Mr Racine: From now? No.

[18] Ev 16

Q144 Chairman: You are totally happy with what you have done.
Mr Racine: So far, yes.

Q145 Chairman: Mr Gieve, will this building be ready, fit for purpose, meet your needs when you move in in 2005?
Mr Gieve: I hope so. It is currently on schedule and we have given AGP every financial incentive to complete on time.

Q146 Chairman: Is there anything you would have done differently? Have you learned lessons? Have you shared those lessons with other government departments?
Mr Gieve: There are some things we would have done differently. Obviously we would have put more effort into ensuring that our staff projections were right. NAO note here, and we agree, that we did not co-ordinate between the IT and the building planning as well as we could have done in the early stages. There are definitely things we would have done differently.

Q147 Chairman: Would you have done anything differently on refinancing?
Mr Gieve: No. We are going to send you a note on this and preparing it may change my mind, but at the time I thought we were doing the right thing and I expect to show that.
Chairman: Gentlemen and lady, thank you very much for coming this afternoon. We are very grateful.

Supplementary memorandum submitted by the Home Office

Question 12 (Chairman):

Around 80% of Home Office staff in central London are employed in policy areas, with around 20% in support functions, including finance, HR and IT. For the Review of Public Sector Relocation being undertaken by Sir Michael Lyons, it was estimated that up to 1,300 members of core Home Office staff potentially might need regular contact with Ministers or Parliament. The precise members of this group who at any one time would need such regular contact will vary as Ministers and Parliament focus on different issues. The survey did not investigate the number of staff in direct support of the group with regular contact with Ministers and Parliament. However, consideration of the functions needed, including administrative and secretarial help, the preparation and collation of research and statistics and corporate strategy and planning, suggests a requirement for perhaps [at least as] as many staff again. Nor did the survey provide any detailed information about the number of other staff whose work requires them to have frequent contact with other Government Departments or the Home Office's major stakeholders, many of which are based in London.

In the context of the Lyons Review, we are currently considering which functions from the core Office could be relocated out of London and the South East. These include around 5–600 posts engaged in various forms of caseworking. The decision whether to relocate any of these functions will of course depend on a full examination of the case for doing so, including value for money, affordability, and the wider balance of advantages and disadvantages.

Question 28 (Jon Trickett):

Clarification: The technical due diligence consultants would be liable to the funders to the extent of any failure in their duty of care in monitoring the project. They have no contractual duty of care to the PFI supplier AGP. AGP's main remedy would be against the builder Bouygues UK responsible for construction of the new building. Bouygues' performance is underwritten by their parent company Bouygues Construction SA. Bouygues also have warranties from their design consultants, sub-contractors and other suppliers.

Question 33 (Jon Trickett):

The due diligence process seeks to give the funders assurance that the project assumptions are robust, that there is no undue "optimum bias" in the consortium's plans and that all potential project risks have properly been taken into account. Due diligence will not provide certainty in the outcome of a building project—it is a mechanism for the funders to assess the risks associated with a deal.

It is possible for a department to commission due diligence on a preferred bidder's proposals before finalising a PFI deal. In the funding competition held for the redevelopment of the Treasury building in 1999, Exchequer Partnerships, the preferred bidder, in consultation with the Treasury, commissioned its own due diligence advisers. All the funding institutions involved in the competition agreed to use this one set of advisers.

Departments have a choice following the due diligence process. They can proceed with private funding with the associated risk transfer. Alternatively, they can decide to finance the senior debt themselves but still retain the risk that the due diligence process has not identified all risks and that the project cost overruns the project sponsor's assumptions.

Question 37 (Jon Cruddas):

At financial close, density of the Home Office estate was about 19.4m^2 per person. Since then, the estate has reduced in size by 5% and more staff have been housed. Density for the estate has reduced to about 16.2m^2 per person. Current conditions are cramped in places, with too little suitable support space. The 2MS design makes more efficient use of space, with improved amenities for staff such as more meeting space, a multi-faith prayer room and provision for breakout areas.

Question 39 (Jon Cruddas):

Clarification: The building size is fixed by planning consent, but the internal area is designed for flexible use. The number of deskspaces allocated is at its maximum size of 3,450 consistent with our other requirements for the building. The agreed maximum building capacity is 4,200 staff; should the type of work change and reduce the need for meeting space and other support space. In future we will increasingly look at hot-desking and other techniques for making good use of our space, which we will do in the context of overall effectiveness and delivery.

Question 40 (Jim Sheridan):

In 1999–2000 there were potentially three suitable sites available close to Parliament and other Ministerial HQs. These were Stag Place in Victoria, Elizabeth House site adjoining Waterloo Station, and 2 Marsham Street. Stag Place was more expensive and slightly smaller but we allowed the PFI bidders to consider it if they wished. Elizabeth House was ruled out by the then Home Secretary as being too inaccessible to Parliament and the rest of Whitehall. This is as mentioned in the NAO Report section 1.5.

We were aware that sites of suitable size but not suitable location were potentially available in London Docklands, Paddington and elsewhere. Precise site identification was not taken further than a list of suitable planning consents provided by our property advisers.

Questions 59–60 (Mr Rendel):

The capital receipts for disposal of the surplus buildings are excluded from Figure 3 Page 11 which compared running costs of the existing estate with the PFI estate. The calculated financial benefit of the capital receipts of the surplus property was included in the comparison of options in the business case in accordance with the Treasury Green Book guidance. The business case also took into account the possibility of a substantial under receipt from the sales owing to any fall in property values.

Question 69 (Mr Rendel):

The NPC of the agreement for sharing 50% of re-financing gain was close to £2.75 million. The respective costs of the financing at financial close were:

- Blended equity and sub-debt—16.1%.
- Sub-debt—14.75%.
- Fixed rate bond—£100 million at 5.66%.
- Indexed bond—£144 million at 3.24% (subject to the addition of RPI).

In considering potential re-financing profit, it was judged that there was a low probability of re-financing the bonds owing to the excessively high cost of keeping the bond holders whole (ie the breakage costs of buying out the bondholders). If the bonds were re-financed, the deal would have to have an interest rate reduction of 0.33% after breakage costs to clear the overall cost of £2.75 million on the basis of a 50% share. The costs of breaking the bonds can only be ascertained at the time of re-financing.

There was considered to be a greater prospect of re-financing by means of replacing more expensive sub-debt with cheaper junior debt. This could particularly arise if the market perceives a reduction in project risk and would therefore be likely to occur in the period after a successful construction completion. The process would have to be agreed by the bond insurers, AMBAC, on the bond holders' behalf, specifically in respect of the relationship between all the financing parties. In return for agreeing to a 50% share of re-financing gain the sub-debt interest rate increased from 13% to 14.75%. (This in turn increased the blended equity and sub-debt by 1.1% to 16.1%.) It was this change that led to the increase in cost.

In replacing sub-debt with junior debt, we considered at the time that re-financing would need to achieve a reduction in interest rate of around 4% to cover £2.75 million. We judged that a refinancing gain at this level or greater was possible. The potential gain was not incorporated in AGP's financial model and so would have been a receipt in excess of the modelled tendered financial proposal. Although AGP had offered a 20% share of any refinancing gain in their bid (AGP was nominated preferred bidder in July 2000), the essential legal terms of this were not fully clear. The detailed negotiations in autumn 2001 secured the 50% share with a robust legal mechanism supported by PUK. NAO noted at Section 2.8 that the approach taken by the Home Office was prudent.

Questions 78–80 (Mr Bacon):

The inflation assumption used was 2.5%. Funding is mainly by means of indexed gilts, but with an element of fixed rate gilts. The effect of the fixed rate gilt is that 24% of the combined charge does not increase with inflation. Overall the charge will therefore increase by about 76% of RPI, or 1.9% per annum if the RPI increases by 2.5% per annum.

Questions 83–84 (Mr Bacon):

The total cash with inflation was modelled at financial close at £1,088.1 million.

Questions 85–86 (Mr Bacon):

Clarification: The questions imply that the Treasury Discount Rate (TDR) of 6% was part of the contract. This discount rate is not in the contract. The 6% TDR was applied to the Home Office's business case, which is an internal mechanism used to assess the options. Government has since adopted a 3.5% TDR (since April 2002).

Question 91 (Mr Bacon):

Clarification: Figure 6 on page 17 covers fees on the project up to January 2003. The fees for February 2003 to occupation in April 2005 are expected to be £6.0 million. External specialist advisers, such as Turner & Townsend, the monitoring surveyors, will continue to support the project on Home Office's behalf until the building has been accepted and is fully occupied. The extent of that support will depend to some degree on events, but we expect it to diminish over time.

Question 100 (Mr Bacon):

AGP advises the following:

	£m
Development Costs	11.20
Pre-Operating Costs	0.44
SPC & Insurance Costs	2.15
Finance Fees	11.27
Total	25.06

The above total includes all consultants' fees but may not be comparable with other PFIs, because AGP's construction and FM sub-contractors (Bouygues UK and Ecovert FM) carry out a significant amount of professional work in-house.

Question 104 (Mr Bacon):

The following table re-works the figures in Figure 14, page 31 to show base costs as in the MoD report page 24:

	NPV (£mils at financial close, March 2002)		
	Base Costs	*Risk*	*Risk as % of base costs*
Property (including site acquisition, disposal of surplus land and residual value)	19.5	1.5	8%
Construction costs (including development, pre-operating & insurance costs)	189.9	9.1	5%
2 Marsham Street running costs (Note 1)	78.1	28.9	37%

	NPV (£mils at financial close, March 2002)		
	Base Costs	*Risk*	*Risk as % of base costs*
Pension & redundancy costs	3.0		
Cost of running existing buildings and for 2 Marsham St.	87.0		
2 Marsham Street running costs not included in PFI bid	14.0		
Rates for existing buildings and for 2 Marsham Street	108.0		
Sale of surplus buildings (Note 2)	−52.5	3.5	7%
Operating insurance (Note 3)	0.0	4.0	
Totals	**447.0**	**47.0**	**11%**
Total PSC		**494.0**	

Note 1: This risk includes under-estimation of running costs, under-estimation of specification of service quality, and risk of wage inflation being above RPI.

Note 2: This risk was applied equally to the PFI and the PSC as it was allocated to the Home Office under both scenarios

Note 3: This represents the value of the insurance risk allocation to AGP. Under the PSC self-insurance by the Home Office is not modelled as a cash cost.

Questions 112–113 (Mr Bacon):

The non-Agency Home Office provides its corporate IT and telephony through a service agreement with Sirius, a consortium consisting of Fujitsu services, IBM Business Consulting Services (previously PricewaterhouseCoopers Consulting) and Global Crossing. The Home Office pays an annual charge under this agreement, and does not own the IT or telephony provided. We expect to pay Sirius £67 million for delivering IT and telephony services to the Home Office in 2003–04. Of this, £36 million is for the Immigration & National Directorate (IND). The total service covers 12,500 users across 150 sites around the country (which includes users in the London, Croydon and Liverpool offices, Government Offices for the Regions (GOFRs), and IND offices at ports/airports).

Question 114 (Mr Bacon):

Clarification: The Home Office is not paying separately for the ICT infrastructure: It is included within the overall construction costs and being paid for through the combined charge. AGP have advised us that the underlying element of the construction costs attributable to the ICT infrastructure is £6.3 million. This includes an electronic patch system which has a higher capital cost than a manually operated patch panel, but will reduce the charges for moves and changes within 2 Marsham Street by our ICT supplier.

Question 140 (Mr Rendel):

Demolition was substantively completed in August 2003, as the Home Office told NAO in September 2003.

The last phase of demolition (the north rotunda) was scheduled to complete in mid-October, according to the indicative programme set out in the Project Agreement. As earlier phases of the demolition progressed very well AGP developed a detailed project programme with an earlier demolition completion date. While demolishing the north and south rotundas took longer than AGP's post-contract detailed programme allowed for, demolition of the former 2 Marsham Street was still completed ahead of the indicative programme in the Project Agreement. AGP is obliged to adhere to key milestone dates in the indicative programme but in complying with this requirement, has the commercial freedom to develop their detailed development programme as they choose.

Some non-demolition works, to prepare foundations and carry out excavations, were also carried out by the demolition sub-contractor Brown and Mason from August to November 2003. These were excavation, not demolition works.

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