

Prime Minister (1)

Ref. A082/0542

Agree with this advice?

PRIME MINISTER

Yes - prefer

MCS 16/12

The 106 is in

para 4.

Appointment of the Comptroller and Auditor General

The Chancellor of the Exchequer sent me a copy of his minute of 10th December.

2. If the Comptroller and Auditor General were to be an officer of the House of Commons, then he would be appointed by the House of Commons, and The Queen need not come into it. If the office of Comptroller and Auditor General is to have independent status, however, and is to remain a Crown appointment, then I think it is difficult for anyone other than you to have formal responsibility for advising The Queen. There would be no objection to you accepting a non-statutory obligation to consult the Speaker, or the Leader of the Opposition, or the Chairman of the PAC, before advising The Queen. But I think that the statutory position would have to be that the Comptroller and Auditor General was appointed by The Queen and The Queen's adviser on appointments is you.

3. It is clearly important that The Queen should not be put into a position where she might get conflicting advice on such an appointment. I do not therefore think that it would be at all attractive to make statutory provision for The Queen to be advised by the Speaker on the appointment of the Comptroller and Auditor General. I do not think that such a provision could exclude the provision of advice by you, which could conflict with that of the Speaker; and I think that it would be undesirable to create a precedent for statutorily specifying some other source of advice to The Queen on appointments of this kind.

4. If a non-statutory obligation to consult is not sufficient to meet the demands of Mr St. John-Stevas and Mr du Cann, then I think a possible alternative is for legislation to provide for the Comptroller and Auditor General to be appointed by The Queen on the



advice of a Commission consisting of you and the Speaker whose advice must be unanimous. That is the solution envisaged in the annex to the Chancellor of the Exchequer's paper (it is one which I in fact suggested to the Treasury); and I think that it would be just about tolerable, if it was not possible to persuade Mr St. John-Stevas and Mr du Cann to accept a non-statutory obligation to consult as being sufficient protection for Parliament's interest in the appointment.

REA

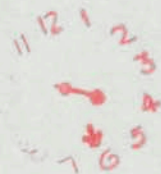
ROBERT ARMSTRONG

15th December 1982

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FRS SW



10 DOWNING STREET

From the Private Secretary

SIR ROBERT ARMSTRONG

Appointment of the Comptroller
and Auditor General

The Prime Minister has seen your minute of 15 December.

She agrees with the advice in the minute, and has commented that she prefers the solution in paragraph 4.

May I leave you to pass this on to the Treasury.

M. C. SCHOLAR

17 December, 1982

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Prime Minister

Would you like to
discuss with the

Treasury Chambers, Parliament Street, SW1P 3AG Chancellor at
01-233 3000

the meeting we have
arranged for Tuesday?

PRIME MINISTER

Yes please

APPOINTMENT OF THE COMPTROLLER AND AUDITOR GENERAL

MUS 10/12

We spoke on 8 December about the problems created by Norman St. John Stevas' Bill, and I have had an account from the Chief Secretary of the discussion in Cabinet yesterday.

.... 2. You may now like to see the attached draft by officials of my paper for Cabinet next week. I cannot pretend that I like its recommendation to allow a significant widening of the scope of C&AG access, and I shall be discussing it with officials on Monday. But I think they may be right in suggesting that we face a choice of evils, for as you know, I share the Lord President's view that there is a high risk that if we oppose the Bill on Second Reading we will lose the vote. John Biffen is clear that the best course is to seek an accommodation with St. John Stevas, Barnett, and du Cann. But this does not mean that we have to accept all the recommendations of the PAC, on which the first draft of the Bill is based, and the draft paper proposes some limitations on the range of the C&AG's functions.

3. I shall be working on the paper over the weekend, but before it is finalised I would find it very helpful to know what position you would like us to take, in our further discussions with the backbenchers, on the method of appointing the C&AG - an issue touched on in its Annex B.

4. This too is an issue on which I would prefer to give no ground, but suspect that we shall have to concede something. The question is how much. The considerations are complex, and I apologise for burdening you with some paragraphs of more general background.

5. On the status of the C&AG, which is relevant to the method of appointment, we should not accept that the C&AG should be an Officer of the House, and subject to direction.

6. Of course the C&AG works closely with the PAC and in the past he has met its wishes if it wanted a particular matter investigated.



But the Committee has known that the C&AG could refuse, if he thought he was being pushed into areas which were inappropriate. If he was subject to direction that restraint would be removed, and there would be a temptation to use him for political advantage. There would then be a real risk that the PAC would split on party lines, and its effectiveness would thus be reduced.

7. The PAC recognised that a consequence of its proposal would be that other Select Committees would have the right to direct the C&AG. It sought to limit this by proposing that all directions should be made through the PAC, and the C&AG should retain discretion as to how he carried out an enquiry. But these would provide only limited safeguards against the prospect of a large and unmanageable increase in the burden which the C&AG might be driven to impose upon the bodies concerned, and against the danger that he would be pushed into examining question, of policy or into studies of "efficiency" which had strong political overtones.

8. That in turn would raise a major question about the relationship between Government departments and the C&AG. The Government could face difficult and controversial decisions about the degree of access which the C&AG and his staff should be allowed to have to departmental papers.

9. Nationalised industries and publicly owned companies would find it that much more difficult to accept scrutiny, if they knew that he would be subject to direction.

10. From all this I draw the conclusion that we have a strong case for advocating an independent status for the C&AG, and that we would find support for this in the House. (I know, for example, that Edward du Cann and Peter Horder would agree with us.)

11. To maintain and enhance the C&AG's independent status we could make the following proposals. He should continue to be paid from



the Consolidated Fund. To facilitate attracting candidates from the private sector some provision should be made for flexibility in settling the salary attaching to the post, perhaps by way of a Resolution of the House. To emphasize his independence from the Executive all vestiges of Treasury control in the Exchequer and Audit Department would be taken out of the Civil Service. They would not be servants of the House, but employees of the C&AG. He would determine their numbers and salaries but, as is the case with the House of Commons staff, it would be reasonable to require him to keep broadly in line with Civil Service grades and other conditions. The Speaker would present the vote to the House. In our recent discussions Joel Barnett and Edward du Cann accepted that the cost should be cash limited and we would want to make this as effective as possible.

12. That is the context in which you will wish to consider the method of appointing the C&AG. The PAC proposed that he should continue to be appointed by the Queen, but on the recommendation of the House of Commons, on a motion proposed by the Chairman of a new Public Accounts Commission. This method of direct advice to the Queen from the House is not unprecedented. The Clerk Assistant to the House and the Sergeant at Arms are appointed by the Queen on the advice of the Speaker. But in the case of the most senior official of the House, the Clerk, the Queen is advised by the Prime Minister, who consults the Speaker. The appointment of the Parliamentary Commissioner for Administration is modelled on that of the C&AG, the Chairman of the Select Committee on the PCA being consulted.

13. It is apparent from our discussions with the backbenchers that they attach importance to the views of the House being at least more visibly taken into account than is the case under the present arrangements, under which you consult the Chairman of the PAC. Nevertheless, the method of appointment proposed by the PAC fails to recognise either the Government's interest in the C&AG, resulting from his access to departmental papers, or your own position as



adviser to the Crown. It is based on the view that the C&AG should be an Officer of the House, which I believe we should reject, for the reasons set out in paragraphs 5 - 10 above.

14. If you were prepared to consider some change, in order to give the House a more visible role, one possibility would be for the House to pass a resolution, while the Queen continued to take your advice on the appointment. But the difficulties with this are obvious. If the House passed a resolution before you had decided which name to put forward, it would represent an attempt to pre-empt your judgement; whereas a resolution after you had reached a decision; would be an empty formality - unless the House put forward a different nomination, which would produce an intolerable situation.

15. An alternative and perhaps more feasible solution might be to involve the Speaker. He would be seen to represent the views of the House and the close working relationship which the C&AG has with the PAC, while you would represent the legitimate interest which the Government must have in the appointment of the C&AG. The recommendation to the Queen might then be made jointly by yourself and the Speaker. Would you see any mileage in that?

16. I shall almost certainly be asked about this aspect when I meet the backbenchers again on 15 December. And I shall have to finalise my Cabinet paper early next week. It would therefore be very helpful if you could let me know, on 13 or 14 December, what you think.

17. I am copying this minute to Sir Robert Armstrong.

G.H.

10 December 1982

DRAFT CABINET PAPER

PARLIAMENTARY CONTROL OF EXPENDITURE (REFORM) BILL

Mr St John Stevas' Private Member's Bill is down for Second Reading on 28 January. It is intended to implement the recommendations of the Public Accounts Committee (PAC) in their First Special Report of 1980-81. (Other Committees had previously made similar recommendations.) The main principles of the Bill are that the appointment of the C&AG and his staff should not be in the Government's hands, and that the range of the audit should be "wherever public money goes" - in particular to include the nationalised industries and many public companies.

2. In the Government's reply to the Report (Cmd 8323) we accepted the need for new legislation to update the statutory description of the Comptroller and Auditor General's (C&AGs) functions; but were not convinced of the immediate need for the radical changes proposed by the PAC. Following an adjournment debate on 30 November 1981 an Early Day Motion collected nearly 300 signatures in favour of the PAC's recommendations. We have since been discussing minor concessions (within existing legislation) with Messrs Barnett and Du Cann and others following discussion in E Committee on 9 February 1982.

3. The initiative is however now with Mr St John Stevas. Although he has asked for co-operation in drafting the legislation, he is determined to proceed, with the support of the movers of the Early Day Motion. He is confident that his Bill will command very wide support; and the Lord President believes that this confidence is not misplaced. Our White Paper arguments were and are sound, but we cannot now expect that a majority in Parliament will accept them as overriding the constitutional argument about accountability which dominates their thinking. I believe therefore that we should now concentrate on seeking to negotiate with Mr St John Stevas and his associates a specification for the Bill which will be sensible and workable, and minimise the adverse consequences of moving too far in

/the direction

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the direction urged by some of the extremists; and if we can negotiate a specification, we should offer the services of Parliamentary Counsel to help with the drafting, working to agreed instructions. This will give us a much better chance of influencing the Bill, and ending up with a tolerable piece of legislation, than would be likely if we wait for the Bill to be presented in the form currently proposed by Mr Stevas, and then attempt piecemeal amendments against the mood of the House.

INDEPENDENCE OF THE C&AG AND HIS STAFF

4. The Comptroller and Auditor-General is at present an office holder under the Crown, appointed on the advice of the Prime Minister who consults the Chairman of the PAC. His staff are civil servants of the Exchequer and Audit Department. Any change in the manner of his appointment could involve constitutional considerations, and it is important that we should not concede that he and his staff should become employees of the House. They would then become liable to directions from the House which could include any of its Committees. That would raise serious problems about their access to the Government's files.

5. I believe we must seek to ensure the independence of the C&AG and his staff both from the Government and from Parliament (other than by Act of Parliament). The national audit should be conducted as a professional operation with proper audit objectives; it should not be made to react to particular and transient interests of Members or Parliamentary Committees or the press. The C&AG could not, of course, ignore representations made to him - from Government as well as others - but the decision on what he and his staff should do should be his and his alone.

6. On that basis it should be acceptable that he should retain his present powers of access to papers which have, by consent over many years, allowed not only for statutory certification audit but also for value-for-money and effectiveness studies. C&AG investigations, and PAC examinations, have always scrupulously avoided policy issues:

/they have

they have been audit-based, ie concerned with past, not future, expenditure. This must remain the case; for on any other basis we could easily find ourselves obliged to impose, and defend, restrictions of access for particular investigations.

SCOPE OF THE AUDIT

7. Annex A deals fully with the position of the nationalised industries. The arguments against involving the C&AG there and in such companies as BL, Rolls Royce etc are sound, but my judgement is that they will not carry the day, against the appeal of the simplistic PAC formula of "following public money wherever it goes". I therefore think we must now concentrate on how far, rather than whether, this should be accepted. As regards the nationalised industries, I suggest the following:

- a. Access to the books of nationalised industries and private companies should be through a separate branch of the proposed National Audit Office, to consist of staff with adequate qualifications and experience to understand the commercial scenario in which they operate. The MMC should be withdrawn.
- b. Studies in the nationalised industries should follow a systematic programme determined by the C&AG in consultation with the Government and others.
- c. For private-sector companies, I should prefer to confine access to those where the Government has a controlling interest (BL, Rolls Royce and possibly Cable and Wireless). There will be pressure to extend this to other companies where the Government holds shares, either directly (British Aerospace, Britoil, BP) or through BTG - but these are commercial concerns and we should resist E&AD crawling over their business if possible. There will also be pressure to "follow public money" into other companies which receive substantial assistance in grants, loans or guarantees

/eg the £200m

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eg the £200m guarantee to ICL). Again we should resist this if possible - but at worst I should want to try to find some way of distinguishing these cases of substantial selective assistance from the ordinary run of small-scale or automatic grants (Regional Development Grants, agriculture, and so on).

OTHER MATTERS

8. Other issues on which I believe we should seek to agree with Mr. St. John Stevas and his backers are listed in Annex B.

CONCLUSION

9. A lot of this is very disagreeable; and it will, in particular, be difficult to ensure that the change in respect of the nationalised industries is conducive to more efficient management. But I am convinced that if we do not go as far as is proposed in Annex B we shall be in a poor tactical position. We need to influence the initial drafting of the Bill. If it were to be tabled in a form which reflects only the PAC's proposals, we would, in moving amendments in Committee, appear to be trying to avoid full accountability to Parliament.

10. I therefore seek approval to negotiate with the backers of the Bill on the lines of the Annex B to this paper; and if successful to offer drafting assistance to and support for the Bill.

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Nationalised Industries

1. We have hitherto resisted giving the C&AG and his staff access to the nationalised industries on a number of grounds. First, C&AG activity would tend to inhibit the industries from acting commercially and lead them to adopt defensive attitudes. Second, the Government legislated in the 1980 Competition Act to enable the MMC to conduct efficiency investigations and they provide a more effective instrument. Indeed we have over the past year taken steps to increase the number of MMC references and to improve the follow-up to their reports. Third and more generally, we were concerned that the line of responsibility for the industries should continue to run through Ministers to Parliament and that the scope of C&AG activity should not therefore exceed that for which Ministers could be held responsible. Otherwise the relations between Parliament, Ministers and Departments, and the industries could be seriously affected.

2. These arguments were, and remain valid. We have already offered a number of concessions in order to maintain existing broadly arrangements. We have encouraged the C&AG to use his access to departmental papers to examine how Departments exercise their responsibilities for nationalised industries. We have agreed to encourage the PAC to become involved in the follow-up to MMC reports. And we would have been prepared (as a final concession) to consult the PAC on the selection of references.

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3. Leaving aside the current Parliamentary pressures, I would not want to change our existing arrangements. But it is quite clear that Mr Barnett, Mr Du Cann and their supporters regard full access by the C&AG and his staff to the industries as a crucial issue on which they are not prepared to compromise; and they are confident that they will be able, in the context of the Stevas Bill, to carry the House on this issue. I believe their judgment is correct, and that it is no longer possible to rest on our existing arguments. This view is broadly supported by the Lord President's letter of 8 December. A major concession on the nationalised industries is now unavoidable.

4. We can of course wait until the Bill comes before Parliament and seek then to resist its proposals for access to the industries. But, given the mood of the House on this issue, this course seems certain to fail; and our chances of influencing the Bill thereafter would be much diminished. We are more likely to be able to strike some sort of bargain with the Bill's promoters if we offer concessions early on.

3. In considering what move we should ^{now in response to the St John Stevas Bill,} make we should keep our underlying objectives towards the industries firmly in view. We want a mechanism for conducting investigations into the industries particularly where competition is absent or weak. We want to avoid being drawn into day-to-day issues ^{and} ^{undermine} thereby / the responsibilities of the management. We want the industries to act commercially; and we do not want to saddle them with two parallel systems of investigation - the C&AG and MMC - since this would be an excessive burden diverting the management from their main tasks.

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4. The key question is what moves we can make to satisfy the Bill's promoters which would at the same time offer the best chance of meeting our objectives. I have considered whether it would be possible to make a limited concession with the aim of preserving the present MMC system on broadly unchanged lines - for example by means of an understanding that the C&AG's powers would be used infrequently e.g. only when he had some prima facie reason to think there was misuse of public funds. Or possibly by associating the C&AG more closely with the industries' existing external auditors. But it seems quite clear that the C&AG and the PAC would not accept restrictions of this kind; indeed it is the C&AG's intention to have a permanent presence in all or most of the industries and to use their work as a means of deciding when to make a fuller enquiry. I do not think therefore that options of this kind are worth pursuing. They are likely at the end of the day to mean parallel systems of enquiry by the C&AG and MMC. This would be a most undesirable outcome.

5. The only realistic option in my view is to accept the principle of C&AG access to the industries and to seek to build an effective system on that basis. By making this important concession of principle we should be able to maximise the influence we can bring to bear on the shape of a new system and to see this reflected in the Bill. As a corollary, in order to avoid duplication, the use of the MMC for the purpose of efficiency investigations in the industries would cease (although it would continue to look into monopoly questions). We would either amend Section 11 of the 1980 Competition Act or simply restrict its use. The C&AG's remit would be limited to questions of efficiency and value for money, policy questions being

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reserved for departmental Select Committees. I think there would be no difficulty in agreeing this with the C&AG, although in practice the dividing line is not always clear cut.

6. The main risk under this option - and it is a real one - is of the C&AG's approach and methods inducing in the industries an uncommercial and defensive attitude. Our best hope of avoiding this is if we can encourage the C&AG to separate as far as possible - in terms of staff, expertise and methods of work - his task of examining trading bodies from his traditional work with Government Departments. Our aim must be to shift his approach into a more commercial direction. Ideally one would want to see the nationalised industry investigations carried out by a wholly separate command under the C&AG, using management consultants/as well as staff directly employed by him. However it will be difficult to embody this in legislation; and although we would try to reach an understanding with the C&AG, he may be unwilling to go as far in this direction as we would like.

7. There are two other major questions which this option raises: influencing the C&AG's programme of enquiries; and following up the results.

8. On the first question, it is important that the Government continues to have a major influence on the programme of investigations. We will want to ensure that all industries are periodically scrutinised. And we will no doubt want particular industries examined from time to time in response to events. We should therefore try to ensure that there is systematic consultation between the C&AG

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and Government Departments before a programme is decided. We believe the C&AG would agree to this. We should try to get the point clearly embodied in the legislation.

9. On the second question (follow-up) it is less easy at this stage to see the way forward. A good deal will depend upon the nature of the reports the C&AG makes. No doubt the PAC will itself initially want to respond by questioning the industries and Departments on the report's findings. But where some major deficiency is revealed Ministers will wish to satisfy themselves that remedial action is taken by the industry. It is vital that the clear line of responsibility from the industries to their sponsor Minister is not blurred.

10. We shall need an early meeting with the industries. I propose to arrange a meeting between sponsor Ministers and the Chairmen's Group as soon as possible. These industries have hitherto supported our attempts to hold off the C&AG and they will not welcome any change in our position. We shall need to convince them that there is now no choice but to make a move of the kind outlined above. Their main concern will be to avoid an increase in the number of external enquiries and bodies concerned in their affairs. My proposal, by substituting the C&AG for the MMC, should achieve this, although the question of the C&AG's proposed method of approach to the industries will also be important.

A POSSIBLE SETTLEMENTI. Appointment and Status of C & AG and his Staff

- (a) Appointment by the Crown (on recommendation of a Commission consisting of the Prime Minister and the Speaker). Retirement at 60 (or ?65).
- (b) An independent office holder under the Crown i.e. not subject to direction either by Government or by Parliament (except by Act of Parliament). Paid direct from Consolidated Fund, as at present.
- (c) Task is to conduct :
 - (i) certification audit (propriety of expenditure)
 - (ii) VFM audit (whether, accepting objectives, expenditure /collection of receipts is efficient)
 - (iii) Effectiveness audit (whether expenditure, although sound under (i) and (ii), has contributed effectively to policy aims)and report on them to House of Commons.
Task is NOT
 - (iv) to examine policies of Government (including future expenditure proposals e.g. Estimates).
- (d) Salary and conditions of service to be linked with those of the Clerk of the House, unless otherwise determined by the House on resolution proposed by the Speaker.
- (e) Staff of National Audit Office to be employed by C & AG on terms and conditions he thinks fit, having regard to the terms and conditions of civil servants and servants of the House. They will cease to be civil servants.
- (f) Budget of NAO to be controlled by House of Commons Commission (or a Public Accounts Commission). Estimates to be presented by the Speaker - with the consent of the Treasury to provide for a Cash Limit.

II. Range of Audit

Full audit :

- (a) All central Government accounts;
- (b) Other accounts as at present, as directed in legislation, or under a statutory instrument, subject to affirmative resolution, introduced by the Treasury.

Access to relevant papers :

- (c) Nationalised industries - on the understanding that there would be a separate part of the National Audit Office for this purpose and that there would be consultation with the Government about the C & AG's programme.
- (d) ~~All~~ Other bodies dependent or mainly dependent on Government, including public companies in which the Government has a ^[controlling] shareholding or where they are in receipt of substantial selective (non-routine) assistance from the Government.]

III. Minor items

- (a) Treasury to appoint auditor of C & AG's (NAO) Appropriation Account.
- (b) Repeal s.3 of 1921 Act (leaving II (b) above to cope).

IV. Not included

- (a) Local Authorities (covered by Audit Commission)
- (b) NHS statutory audit (C & AG already has access. NHS audit under review anyway. If C & AG took it over a new internal audit would be required by DHSS).