



Treasury Committee

Oral evidence: [HM Treasury Annual Report and Accounts 2014-15](#), HC 805

Wednesday 10 February 2016

Ordered by the House of Commons to be published on 10 February 2016

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Members present: Andrew Tyrie (Chair); George Kerevan, John Mann, Chris Philp, Mr Jacob Rees-Mogg, Rachel Reeves, Wes Streeting

Questions 1-87

Examination of Witnesses

Witnesses: **Sir Nicholas Macpherson GCB**, Permanent Secretary, HM Treasury, and **Kirstin Baker**, Finance and Commercial Director, HM Treasury, gave evidence.

Q1 Chair: It is very good to see you, Sir Nicholas. It is not the first time you have appeared before the Committee. It is very good to see you, Kirstin Baker. Of course, this may be the last time you come before the Committee in your capacity as Permanent Secretary of the Treasury. You have been in the Treasury a very long time. You are a man and boy Treasury chap, Sir Nicholas. I was just wondering whether you might be prepared to write us a valedictory note setting out what you think has changed in the Treasury over the years and what challenges it now faces.

Sir Nicholas Macpherson: I have been at the Treasury for 31 years. I think my early years coincided with your tenure at the Treasury, Chairman.

Chair: I am that old, yes.

Sir Nicholas Macpherson: I will reflect on your kind offer to send a valedictory note. That is not normally the convention for departing Permanent Secretaries, but equally I am always keen to give the Committee what it wants.

Q2 Chair: Good, particularly the last bit where I elicited that response and I will pocket that. The best reply I can give is we look forward to receiving it then. The next point that I would like to raise with you is quite different. It is about EU

referendum contingency planning. *The Times* has very recently reported that this work is under way in the Treasury. Is that correct?

Sir Nicholas Macpherson: No, we are not doing contingency planning. The Government may or may not ask us to produce some analysis of the implications of various scenarios. The Chancellor announced that last June as a possibility, but, as of this minute, we are not doing contingency planning. You will recall we did not do contingency planning on the Scottish referendum either, but I think it is the nature of these processes that there is always a point where you start doing contingency planning on contingency planning.

Q3 Chair: We are only asking about the first round of that: the contingency planning.

Sir Nicholas Macpherson: We are not doing contingency planning.

Chair: We really want to know whether you are doing any and you are telling us categorically there is none whatsoever going on.

Sir Nicholas Macpherson: Unless in some deep recess of the Treasury someone is doing it without my agreement or without telling me.

Chair: Right, so there is not any.

Sir Nicholas Macpherson: There is none.

Q4 Chair: Just to read the report in *The Times*, you can tell me whether there is any fragment of this that is correct. It reads, “George Osborne is also preparing for the prospect of Brexit. Treasury Civil Servants are secretly looking at the impact on the economy and the Government’s bank balance if the UK were to leave”. Is that incorrect?

Sir Nicholas Macpherson: I think this is a misinterpretation. I have now got the piece of paper in front of me. The Chancellor said to the House last June, “I am sure that the Treasury will publish assessments of the merits of membership and the risks of a lack of reform in the European Union, including the damage that could go to Britain’s interests”. He said that eight months ago. First, you have to get an agreement and, quite frankly, all the Treasury’s, Number 10’s and the Cabinet Office’s efforts are—

Q5 Chair: I do not think we need to go through that. That has already been said on the record a number of times. I am sorry to interrupt, Sir Nicholas. I am just trying to clarify whether the sentence I read out is—

Sir Nicholas Macpherson: Can I just complete my point? If we are asked to do some analysis of various options we will do that, but at this stage we have not got a contingency plan.

Q6 Chair: You have not been asked to do any work with respect of the option of withdrawal from the EU.

Sir Nicholas Macpherson: Not a contingency plan.

Q7 Chair: You seem to be using the word contingency plan the whole time. Can I just read you the sentence again and see whether you want to say yes or no to this sentence? “Treasury Civil Servants are secretly looking at the impact on the economy and the Government’s bank balance if the UK were to leave”. Is that true or false, Permanent Secretary?

Sir Nicholas Macpherson: What at this stage we are doing is preliminary work that could, in time, inform published analysis by the Government, but that would be to inform the debate. It is not a secret contingency plan and, as far as I know, we are nowhere near—

Q8 Chair: I have understood the distinction. This is material that the Civil Servants think, at the discretion of ministers, in its entirety could reasonably and may end up being published prior to the referendum. It has nothing whatever to do with any work that might subsequently need to be done should a decision to leave be taken.

Sir Nicholas Macpherson: That is a very good description.

Chair: Is that correct?

Sir Nicholas Macpherson: Broadly.

Q9 Chair: It was a very good description, but it was only broadly correct. Which is the bit that is not correct?

Sir Nicholas Macpherson: I could just carry on repeating myself.

Q10 Chair: Do not do that. Let me move on to the next sentence and just get clarification on this one. I did not think this was going to be such hard work; I really did not. “The Treasury taskforce is drawing up contingency plans to cope with the potential end of free trade, the loss of structural fund grants for poor areas, the imposition of tariffs and the end of farm subsidies”. Is that correct?

Sir Nicholas Macpherson: It is the same problem. I do not think it is correct because that implies that we have a well-developed piece of analysis that will say what happens if Britain leaves the European Union, that we have a worked-up scenario and that we have done the work. In a sense, it comes back to my point of the contingency plan. We simply have not reached that stage yet.

Chair: Okay, I am going to move on without, I feel, having had a full answer. Colleagues might want to come in.

Q11 Rachel Reeves: Sir Nicholas, after the agreement is negotiated with our European friends about what the deal is, will you start to look at contingency plans then, ahead of a referendum, or would any contingency plans not be looked at until after a referendum?

Sir Nicholas Macpherson: I do not know. The precedent of the Scottish referendum was that the Government decided not to make or, indeed, instructed the Civil Service not to draw up contingency plans. I have had no instruction from either the Prime Minister or the Cabinet Secretary, so I simply do not know. However, at this stage I am operating on the basis that we are not contingency planning.

Q12 Rachel Reeves: Your job as a Civil Servant is to advise and implement. What advice would you give to the Chancellor? Would you advise him that it would be wise to draw up contingency plans or that it would not be wise?

Sir Nicholas Macpherson: My view is that the Civil Service needs to be prepared for any eventuality. It is the nature of political campaigns that when politicians, understandably, are campaigning around the country, the Civil Service occasionally needs to use that space to do a bit of thinking of the unthinkable—the better to be prepared when you wake up the morning after the referendum.

Q13 Chair: The answer is no, you have not been instructed to do any contingency planning, but yes you are going to do some anyway while the politicians are out meeting the electorate.

Sir Nicholas Macpherson: No, I am not saying that. If we are instructed not to prepare contingency plans we will not prepare contingency plans. We did not do that with Scotland, but occasionally when I was trying to go to sleep at night I would think through—

Chair: You might jot a few things down on the back of an envelope.

Sir Nicholas Macpherson: I would think through some of the issues, Mr Tyrie.

Q14 Chair: I want to ask one question about the reserves. The Treasury reserves have gone up quite a lot over the past 12 months, in fact a very large amount. I just wondered whether you were, as Permanent Secretary, closely involved in the decision to increase the Treasury's reserves.

Sir Nicholas Macpherson: There are two things going on here, Mr Tyrie. One is a few years back the Chancellor made a decision to build up the reserves year by year. The orders of magnitude were relatively small. There is no decision either by the Chancellor or the Bank or, indeed, anybody else to do any more than what has been stated in public, so if the nominal value of the reserves has gone up that will reflect wider events. I have not prepared the precise explanation for why the reserves have gone up and rather than say something on the hoof—

Chair: I have understood.

Sir Nicholas Macpherson: I would be happy to give you note.

Chair: I am grateful for that answer.

Q15 Mr Rees-Mogg: I just wanted to say a bit more on the planning or otherwise. There was a report in the newspaper saying that Ministries were not doing contingency planning on paper because it might be subject to a Freedom of Information request; they were merely doing it in their heads. Is this consistent with your answer that you are doing it when you go to bed at night.

Sir Nicholas Macpherson: No, I do not think it is consistent because that would imply that there was an officially authorised instruction that it was okay to do contingency planning as long as you do not write it down. As I understand the current situation, the Government are not at this stage doing contingency planning. They do not want their officials to do contingency planning. My experience of being an official is it is very important to follow instructions like that to the letter, but, coming back to my earlier point, my experience of being an official is also that you have to be ready for anything and the Civil Service has to be ready to do whatever work is necessary.

It comes back to my point about doing contingency plans about contingency plans. You might not be preparing the policy at this stage, but you need to start thinking through where the pressure points are likely to be. For example, I know we are probably not allowed to talk about this, but if Britain were to leave the European Union there would be a very big agenda in terms of negotiating trade agreements. You would have to negotiate the exit, but this would actually transform the Department for Business, Innovation and Skills. If I were responsible for the Department for Business, Innovation and Skills, which I am not, that would be concentrating my mind a bit.

Q16 Mr Rees-Mogg: You said to Mr Tyrie that you had not received instruction from the Prime Minister or the Cabinet Secretary not to make contingency plans, but you implied in the answer you have just given that there is an instruction not to do contingency plans. Have I misconstrued what you have been saying?

Sir Nicholas Macpherson: I may not have been clear. My sense, not least informed by what happened in Scotland, is that Ministers do not want us to work on contingency plans. I know Mr Tyrie pointed out it is almost all over, but we have yet to get an agreement and a lot of my colleagues, as of this minute, are on their way to Brussels to continue the detailed negotiation. It is fair to say that all our effort has been focused on securing an agreement. When an agreement is reached, the Prime Minister will no doubt make a statement to Parliament. Parliament will decide what happens next and, in light of that, I should think I will get further instructions.

Q17 Mr Rees-Mogg: But you do not have instructions at the moment. It is your assumption on what the instruction would be had there been an instruction.

Sir Nicholas Macpherson: I think that is right, but for all I know the Government have issued a statement and I have somehow absorbed the statement without recognising it.

Mr Rees-Mogg: It has come through the ether.

Sir Nicholas Macpherson: It often does.

Q18 Mr Rees-Mogg: Excellent. In terms of contingency planning with our continued membership of the European Union, as you know our opt out from monetary union is to Stage 3—to join the euro. It is not from Stages 1 and 2. However, since we signed the Maastricht Treaty there has been very little effort to enforce Stages 1 and 2 on the United Kingdom. Do you have any contingency plans in case the Commission took a more forceful line in that regard?

Sir Nicholas Macpherson: My recollection of Stages 1 and 2, as agreed at the time, was membership of the ERM was pretty central to it. Indeed, one reason why Sweden, which does not have an opt out, manages to avoid joining Stage 3 year after year after year is by not being in the ERM. The Danes are in the ERM but have an opt out. I had the privilege of working with Norman Lamont, who did a lot of work on the opt out at the time and one of Norman Lamont's prime objectives was to ensure that Stage 2 did not carry additional obligations on Britain.

There are some bits in the treaty around things like monetary financing, but those are hardly onerous. The Commission can make recommendations on fiscal policy, but it cannot fine us or force us to do anything we do not want to do. I would very much expect that to continue. Extracting from this negotiation, I think there is a common understanding of Stage 2, which, looking back on it, had very little meaning indeed. Europe likes stages and dates. I seem to remember it started on 1 January 1994, but I do not think it has had much impact on Britain.

Q19 Mr Rees-Mogg: Viewing the European economy as a common interest and so on, you think that is gently language that will not really matter. When the opt out was negotiated we were of course still a member of the Exchange Rate Mechanism and that does seem to be an assumed condition of Stage 2 that nobody had tried to impose upon us.

Sir Nicholas Macpherson: Yes. I do not know whether technically we are still a member of the European Monetary System. There were a whole lot of issues at the time. We were in the European Monetary System, but we were not in the ERM. We were in the broad bands in those days; the next stage was to go into the narrow bands as part of that flight path. Apart from anything else, Mr Rees-Mogg, I do not see how we could manage in the modern, global economy with a fixed exchange rate. It is no wonder that these countries had to go into their own monetary union and even they found it hard enough to sustain. Trying to manage an exchange rate when you see the huge amounts of money flowing through the foreign exchange markets I think would just be impossible.

Q20 Mr Rees-Mogg: I think you are absolutely right. My concern is that we have treaty obligations that the European Union has not sought to enforce, but that does not mean that they will not try to enforce them at any time in the future. It is a pity that in this renegotiation we have not got ourselves out of those.

Sir Nicholas Macpherson: My experience of the European Union is that, certainly on monetary matters, it is really quite difficult to impose things on a large country like this. I understand your concerns and, on readership of the treaty, there are quite a lot of quite strange things in the European treaties which somehow have fallen into abeyance but are still sitting there. I am reasonably confident that even if you had an extraordinarily powerful central European institution they could not impose it on us, but I understand your concerns.

Q21 George Kerevan: Sir Nicholas, are you going to retire back to Scotland?

Sir Nicholas Macpherson: I have not made up my mind where I will be retiring to. I hope I am not retiring and I am going to start a new life; I have a reasonable amount of working life ahead of me.

Q22 George Kerevan: I have been reading with interest your Strand speech last year on the Treasury's involvement with the independence campaign in Scotland. There is a word you constantly use throughout the speech, "the Treasury's position", and "the Treasury's position" hardens in certain respects—for instance, regarding the currency. This appears to be the Treasury's position, not the Minister's or the Chancellor's position, but the in-house position. What is your in-house position on British membership of the EU?

Sir Nicholas Macpherson: I do not think that the Treasury has an in-house view.

Q23 George Kerevan: It had one in Scotland.

Sir Nicholas Macpherson: No, I do not agree with that. The Treasury was representing the British Government. I did make the point that Her Majesty's Treasury is an institution that covers the whole of the United Kingdom. Coming back to that speech, the Treasury also has a huge interest in a robust and manageable currency, which is why, picking up on Mr Rees-Moggs point, the difference for the current negotiation on Europe is it does not feature the currency. Mr Rees-Mogg was trying to put it on the table.

Q24 George Kerevan: Forgive me, you are wandering off my question. You are refuting the fact that the Treasury had a position on the referendum question in Scotland and you are refuting the proposition the Treasury had a strong position on the currency.

Sir Nicholas Macpherson: No, the Treasury advised the Chancellor on the currency.

Q25 George Kerevan: It had a position.

Sir Nicholas Macpherson: It advised the Chancellor on the currency. As you know, I took that view that this was an issue that was so fundamental to the nature of the British state that it was very important that people understood that position before the referendum rather than waking up the next day and find it out ex post.

Q26 George Kerevan: You leaked your letter of advice to the Chancellor in January 2014.

Sir Nicholas Macpherson: No, I did not leak it; I published it.

George Kerevan: I am happy to take your point—

Sir Nicholas Macpherson: I could have been sneaky. I could have got a mate to ask for an FOI request and released it that way, but I thought that would be bad form.

Q27 George Kerevan: Forgive me; I do not want to be diverted down another track. You had a strong position. You felt so strongly about your position on the currency union, and I respect that, that you felt it had to be in the political domain before the referendum date. That is a highly unusual position to take for senior Civil Servant and I think you are validating my point that the Treasury had a position. I am merely asking: what is your position and what is the Treasury's position on Brexit? For instance, just before the referendum, will you feel before you leave your office impelled to publish another letter on what the position should be on the referendum? You have done it once.

Sir Nicholas Macpherson: That is a perfectly good question. I suspect I will not be here in the run to the referendum since I am leaving at the end of next month. I come back to the point I made earlier. There are issues around the nation's currency that are so fundamental that there are risks in asking voters to take decisions in the absence of all the information. The European referendum is not about the currency. It is not as fundamental as that. This was something—

Q28 George Kerevan: It is a different level of existential crisis.

Sir Nicholas Macpherson: Yes, that is my view. The European Union has existed for a ridiculously short time. The United Kingdom has lasted many hundreds of years and that currency union going back to the Act of Union is fundamental to it.

Q29 George Kerevan: I am happy to accept you feel you have a God-given right to decide what the strategic issues in which the Treasury position should be revealed to the British public are.

Sir Nicholas Macpherson: No.

George Kerevan: You have just said that.

Rachel Reeves: He did not say that.

Sir Nicholas Macpherson: Just to make myself clear, I take what underpins your question very seriously. On the whole, officials should be incredibly cautious about sharing their advice and I think it is a good thing in the British constitution that, generally, there is a private space where officials advise, Ministers decide and Ministers are accountable and responsible for that decision.

My view on Scotland was that this—what the opponents of the Union were arguing was that somehow the British state was bluffing. This was the position of the then leader of those advocating independence. How do you respond to that? The only way you can respond to it is by showing what all arms of the British state are saying—the Treasury, the Bank of England and the politicians. In that very rare occasion, just as if I can envisage in certain circumstances in 1940 it might have been sensible to publish advice, this is something very fundamental.

Q30 George Kerevan: I am intrigued that you categorise the rather peaceful and democratic referendum in Scotland with 1940. I am seriously shocked, Sir Nicholas, that you have taken upon yourself this political decision.

Sir Nicholas Macpherson: Breaking up the state is quite a serious issue and very different from whether or not you are in some single market trading club.

Q31 George Kerevan: Let me accept that. Therefore, let us go down the road I am trying to go to, which is not to go back historically but to look forward to the next referendum. All your arguments to date seem to imply that you should be giving the British public the Treasury advice on the advantages and disadvantages of EU membership, because it seems to me that is an existential issue when it comes to the future of the British state and the British people.

Sir Nicholas Macpherson: No, I think you have misinterpreted me. I have never gone out and opined on whether Scotland should or should not stay in the Union. That was a matter for the Scottish people and it would be unacceptable for me to do that. All I commented on was a very narrow issue of the currency. It was alleged that Britain was bluffing when it said it would not enter into a currency union with an independent Scotland. I took the decision to set out the reasons why the Treasury would not recommend that, and that is very different from a broad issue such as membership of the European Union.

Q32 George Kerevan: I appreciate that. I am challenging whether that was your right as a Civil Servant to make that decision. Let us go a little bit further, since you are trying to narrow the debate simply to the currency. Let me again quote from the Strand speech: “I think it can look back with some satisfaction with the events of last year”—that is the Scottish referendum result; it seems pretty partisan—“Not only has the Union been preserved”. Sir, you, as a Civil Servant, are taking it upon yourself to position the Treasury and use the Treasury for a very partisan, political point of view. Again, what is your position, and what is the Treasury’s position on British membership of the EU?

Sir Nicholas Macpherson: I do not think we are going to make much progress on this. As a Civil Servant, I represent Her Majesty's Government. When Her Majesty's Government achieve their objectives, rather like hitting an inflation target, you can take some satisfaction from it as an official. I do not think what I was saying there was some grossly political statement and I do not think I need to give an opinion of whether Britain should or should not stay in the European Union.

Q33 George Kerevan: You reserve the right on any future issue of the scale of, say, the currency, that you as a Civil Servant will, on your own repugnance, issue publically the advice that you gave to Ministers.

Sir Nicholas Macpherson: As I said at the time and I have said since, I would set a very high bar before making a habit of publishing advice. Equally, as I said earlier, there was nothing to stop me engineering an FOI request and then putting it out claiming that I had to under FOI. That would have been open to me. I thought the best thing to do was to play this straight. This is the first and only time as an official I have felt it necessary to take a position like that, and that is because I thought it went to the heart of the integrity of the Treasury. The leader of the Scottish independence movement was arguing that the Treasury was bluffing; it seemed reasonable to do something to underline that the Treasury was not bluffing.

Q34 George Kerevan: Can you list some other examples where you did in fact engineer an FOI to put in?

Sir Nicholas Macpherson: I cannot give any examples.

George Kerevan: You just said that—

Sir Nicholas Macpherson: No, I could have done. That is one mechanism through which you could do it but I am not in the business of—

George Kerevan: Have you ever engineered FOI?

Sir Nicholas Macpherson: No.

Q35 George Kerevan: The final point is perhaps on less partisan or heated issues. The Treasury is involved in the negotiations with the Scottish Government on the fiscal framework. What is your view on what index might be applied in the ongoing use of the Barnett formula?

Sir Nicholas Macpherson: Negotiations continue. The Chief Secretary to the Treasury met the Deputy First Minister yesterday. I do not think getting into a public discussion of those negotiations is very helpful. I hope we can reach an agreement. There are difficult issues in reconciling various formulae with the Smith agreement, but discussions continue.

Q36 George Kerevan: I appreciate that, but in terms of the technicalities of indexes, which index do you prefer?

Sir Nicholas Macpherson: I would like to see an index that can be agreed between the Scottish and Westminster Governments, but whether that will happen while I am still Permanent Secretary time will tell.

Q37 Chair: Those may have been difficult questions and, as it happens, you know, because I have stated a public view very firmly about the currency at the time and so gave private advice to the Prime Minister about it, that I agreed with what eventually—actually I did not know it was your view—surfaced as to what the Treasury viewed in respect of the currency. Having said that, I think there is merit in these questions and I want to clarify a couple of other points about it. It is an extremely unusual thing for a Civil Servant to come out from the shadows and offer a view in the interests of the country as a whole and that is what you have just said you did. Was that your decision, acting alone?

Sir Nicholas Macpherson: Yes, it was.

Q38 Chair: Did you consult the Cabinet Secretary?

Sir Nicholas Macpherson: No.

Q39 Chair: Did you consult your immediate deputies?

Sir Nicholas Macpherson: No.

Q40 Chair: Did you consult the Chancellor of the Exchequer?

Sir Nicholas Macpherson: I told him that I intended to do it, but he did not instruct me to do it and he did not seek to influence me in any way. I thought, under the very difficult circumstances of the time, given what was being said by the leader of the independence movement, it was necessary to set the record straight.

Q41 Chair: There is one other thing I would like to ask you. Perhaps it is a remark you want to qualify, but you described the EU as a single market trading club a moment ago.

Sir Nicholas Macpherson: Sorry, I may have used the wrong term. I wanted to emphasise the difference between an organisation that we joined 43 years ago from a very fundamental economic and political union that was agreed between two sovereign countries in 1707.

Chair: I would think most people would agree there is a difference of degree between those two.

Q42 John Mann: I wonder what your predecessor would have said in 1933 about Gandhi's proposal for India and the Empire. Your lectures on organisational culture, if you choose to do them, are going to be packed out

because, just to follow up on that, you are saying that the organisational culture in the Treasury is so strong that the person at the head of it feels able to speak out about the union with Scotland. However, it is not so strong that people who have worked in it throughout their entire working life with us inside the European Union do not feel that is taken as a given. That is a really interesting organisational culture if that is the case. Is that what you are saying?

Sir Nicholas Macpherson: No. Coming back to what I said earlier, the decision to publish my advice was my decision alone. For all I know, many Treasury officials might have taken a different view and done a different thing.

John Mann: It is the organisational culture that I am interested in.

Sir Nicholas Macpherson: To pick up on the organisational culture point, a huge amount of debate goes on in the Treasury. There is not some single, imposed line. As organisations go, once a decision has been made the Treasury is pretty good at getting behind the line and ensuring that that line can be defended. It has partly historically had to do that because of when we had things like fixed exchange rates every single word of ministerial statements was pored over lest it affected the markets. Mr Tyrie will remember when we were in the ERM any statement could have a very strong effect. In making public pronouncement about the economy, by Ministers in particular, a lot of care is taken. However, that does not mean that there is some Stalinist culture where debate is frozen out. I am quite sure that there are people, just as there are up and down the country, who have different views on the European Union, so there will be different views within the Treasury.

Q43 John Mann: Most of the academic work on organisational culture, of which there is a lot, would not suggest that a Stalinist approach has much to do with culture of an organisation. The culture of an organisation originates by how it recruits people, how people develop within it, how long people stay within it, the kind of building it is in and the ethos within it. It would be remarkable if there was not a strong organisational culture in the Treasury. That would be remarkable and worthy or a huge amount of investigation of why not. I put it to you that there is a strong organisational culture. That may well be a very healthy thing and you are a product of it, and that organisational culture would have to be strongly presuming that British membership of the European Union is taken as a norm, as a given, for better or for worse.

Sir Nicholas Macpherson: I am going to be very cautious about what I say. The first thing about culture is that we have some evidence through staff surveys about the culture in the Treasury. 68% of people in the Treasury reckon that it is safe to challenge the way that things are done in the Treasury. That is in response to a question. It is 22% higher than the Civil Service average. This is an organisation that encourages debate and a lot of debate goes on. Obviously, we serve a democratically-elected government and although differences of views are always welcome, in the end the job of the Civil Service is to deliver government policies. There will be a range of views in the Treasury. Insofar as you can draw anything from history, it is generally thought in the 1950s and 1960s the Foreign Office was always rather more pro the European Union than the Treasury, but I do not think there is a uniform view of the European Union in the Treasury.

Q44 John Mann: No, I am sure there is not, but that is not what an organisational culture is. Is there not a likelihood, therefore, that there will be a sympathetic approach taken in the mind-set of those preparing any advice, any documentation or any information on it. Some might say, “Thank goodness for that”, but is that not the reality?

Sir Nicholas Macpherson: I do not recognise that statement. One thing that you have to realise about the Treasury is, although I have been there for 31 years, there is really quite high staff turnover. It is quite a youthful organisation. Something like 20% to 25% of people change every year. It is one of the challenges in terms of running the organisation. In that respect, it is harder to embed some common view of the world than it would be in an organisation that had 3% or 4% staff turnover. I am not making this up to be evasive. I genuinely think that there is not an in-house view on the European Union.

Q45 John Mann: I was going to come to the turnover because, of course, what categorises the Treasury now is that there are people, like your good self and senior colleagues, who have been there the vast majority of their career and there is plenty of new people. However, unlike perhaps 20 years ago or 10 years ago, as you and other leaders of the Treasury were working your way through, there is that churn in the middle. You are saying that is a good thing. Let us look at the flip side of that. That means that the development of real expertise like, say, in taking on the new multinational corporation accountants, gets lost because there are not the people who have been there man and boy, girl and woman, all the way through. Therefore, the churn itself is leading to a skills deficit for the next generation of leaders and those key implementers in the middle. Would that be a fair categorisation of some of the problems the Treasury now has?

Sir Nicholas Macpherson: It is definitely a characterisation. If I wanted to create some terribly strong, cohesive view I would say that turnover is an obstacle to that. There are costs to turnover, as you say. The challenge in running an organisation like the Treasury is to retain enough expertise whilst also ventilating the organisation with people who bring new expertise to the party. Somebody who has just got a really good PhD from the LSE is probably going to bring far more economic insights than me, who got his MSc in economics 34 years ago.

You want to ventilate the organisation. You want challenge. You want a relatively democratic environment where people are encouraged to speak their minds and I think the Treasury has always been good about that. I remember reading a Roy Jenkins biography where he contrasted moving to the Treasury from the Home Office. In the Home Office everything came through the Permanent Secretary; in the Treasury he would often be having meetings with quite young officials.

Your point is an important one. At any point in time you need to have enough serious expertise and you do not want to become too reliant on one or two individuals. That is something that we continue to work on. We are a very market-facing organisation, which means that our staff are very attractive recruits to private sector organisations. We have to balance those issues.

Q46 John Mann: Compared to other great government departments, the MoD and the Foreign and Commonwealth Office do not have that level of churn. They are maintaining that consistency the Treasury had in the past in terms of continuous employment. Does that leave you in a weaker position, particularly when it comes to 10 Downing Street, in that they have people who have got the contacts, learned the systems and understood the cultures of other competing interests at times and other voices? Is the Treasury, as you leave it, now at a bit of a disadvantage because of turnover?

Sir Nicholas Macpherson: No—and it is nothing to do with me; it precedes me—I think many aspects of the Treasury are highly successful. If you look at where the Treasury has colonised, the Cabinet Secretary Jeremy Heywood is a former Treasury official, Tom Scholar, who has been leading the negotiation in Europe, was a Treasury official and Ivan Rogers, who is our man UKRep in Brussels, is a former Treasury official. The Treasury is quite good at colonising Whitehall and I would argue that our approach to promotion, which allows people to get on faster, is fundamental to the Treasury's success. You can get to the top of the Treasury in your late 30s. In somewhere like the Foreign Office you have to wait until your early 50s.

Chair: They have got their sleepers everywhere; that is what you are saying.

Q47 John Mann: I suppose my retort to that would be would that be the case in 10 or 15 years' time because of the churn, or will it be in fact other government departments who grab those senior positions. I am only allowed one other question. I would love to ask and the public would like to know which of the Chancellors you have worked with you would regard as the most capable and competent, but I appreciate this is too early for you to comment on.

Chair: You can put it in your valedictory note that you are sending us.

Q48 John Mann: In many ways, aside from the political difference, that would be fascinating for people to know why you drew a conclusion on that rather than what the conclusion was and what their qualities were, because that would inform other politicians, and no doubt some of the younger ones in this room who are eyeing up such jobs in the future. You came in at a time of what was widely seen as a lot of turmoil between 10 Downing Street and the Treasury that was pretty brutal and hard at the time. In the time that you have been there, has Downing Street grabbed more influence and more control on Treasury matters, or do you think the situation in reality is no different to what it was in 2005 when you came in in terms of the power balance between Downing Street calling the shots and the Treasury calling the shots?

Chair: You are allowed 60 seconds to answer this question.

Sir Nicholas Macpherson: My general view of all governments, whether Labour, Tory or Coalition is that if you have got a strong, constructive relationship between Numbers 10 and 11 life is a lot easier. There is only so much creative tension you really want to take

on, but the Treasury will always—the Prime Minister is the Prime Minister, the clue is in the name, and he is the First Lord of the Treasury. However, the fact that the Treasury has 1,000-1,100 officials at any point in time and Number 10, apart from ever increasing numbers of special advisors, has quite a small number of officials, probably 10 to 20, means that in the end the Prime Minister is going to rely on the Treasury quite a lot. If you can harness the leadership of Number 10 with the analytic heft of the Treasury, you can have quite a powerful organisation.

Q49 Wes Streeting: Given the number of Treasury sleepers across Whitehall that we have been talking about, it is a bit disappointing that there is not more cross-departmental working. I noticed the recent NAO report found that in the previous Spending Review the Treasury did not direct departments to identify cross-departmental savings through joint working or support integrated cross-government allocation of spending. How is the Treasury going to ensure better collaboration between departments over this Spending Review period?

Sir Nicholas Macpherson: That was a reasonable criticism. Getting Departments to work cooperatively in pursuit of public expenditure savings has always been a challenge. In the last Spending Review I think the Strategic Defence Review, which looked in the round at our overseas aid effort, the Foreign Office, and the security agencies was quite successful, and I hope we can build on that in that space to embed greater co-operation. On the ground I think the Department for International Development and the Foreign Office work far more closely and far more efficiently.

It is hard work and my view on this is that you have got to incentivise departments to do it. We put a lot of effort under the Government before the last into creating crosscutting funds, crosscutting units and so on. Sometimes you can make quite good progress, for example, on criminal justice and so on, but it does require relentless effort. The temptation for Ministers and officials is that when the going gets tough you retreat into your departmental structure. It is something that Parliament should continue to push for and the Treasury should provide a leadership on when it comes to spending. The Spending Reviews themselves are important, but what is far more important is when you come to implement them, and it is creating the structures, particularly in the finance area, which embed cooperation.

Q50 Wes Streeting: What progress is being made in that particular area of getting finance co-operation?

Sir Nicholas Macpherson: There is quite a lot of progress on the finance side. We had this big review of financial management two years ago. We have Julian Kelly who is in charge public spending and in charge of the finance function across government. Finance Directors now work far more co-operatively. They meet regularly. Kirstin is involved in that. I am not claiming we have solved every problem but we have just got to continue to work at it.

Q51 Wes Streeting: You mentioned incentives. One of the primary incentives for local government, where I come from, and as a councillor in a

London Borough, has been deep cuts and the necessity to change the way we do things because the money is not there. In fact there is not sufficient money to do things that, by statute, we are required to do. The Treasury obviously does not have to negotiation for its own budget; its own budget is set by itself. How do you arrive at a budget cut in the early 20s, in terms of your percentage cut, whilst local government and front line services are clobbered with deeper cuts?

Sir Nicholas Macpherson: Spending Reviews are the ultimate in political priorities. Generally when you have to make big cuts, the Treasury, left to its own devices, will try and pursue the line of least resistance. The Treasury does not determine Spending Review outcomes. This is the most political of decisions and that is down to the Prime Minister, the Chancellor and the Cabinet. You will have your views of why local government comes out worse, and I cannot comment on that, but in terms of the Treasury there is long standing view that the Treasury should play its part in any reductions. It has not happened in every country; Ireland and the Netherlands, as a result of the crisis, concluded that their finance ministries ought to be bigger. As Permanent Secretary you always end up having a discussion with the Chancellor about, “If you go beyond this point we are going to have real difficulties delivering on this priority and that priority”.

In my time at the Treasury I think it got just below 900 officials in about 2001, but generally once it got rid of the Civil Service Catering Organisation it has tended to be something like between 900 and 1,400 in size. We are due to get smaller again. We have taken in quite a lot of new functions and that is one of the reason why we have still got quite a lot of officials—and I can explain all those functions if you are interested. In terms of the core Treasury, I would get quite worried if the organisation went much below 900 with its current breadth of responsibilities. At that point it would have to step back from a whole lot of areas and the problem with recent governments—not the problem; it may be the right thing—is that Ministers have wanted the Treasury to operate on quite a wide front. There have been massive reforms to financial regulation over the last five years. If I look how small the financial service side of the Treasury was back in 2007, I can say without doubt that we had got too small in that space and that was a mistake. You are trying to balance conflicting demands, conflicting objectives. I am biased; I think the Treasury is an important department and it needs to have the basic resources to do the job.

Q52 Wes Streeting: I agree it is an important department and it is fascinating that, given the complexity of the work that the Treasury does at the heart of Government and obviously your own experience in public service that has taken you right to the top of the Civil Service, many of your answers are justifying why Treasury could not be cut further are remarkably familiar to local government finance directors that I have worked with. I do not just want to go on a local government—

Sir Nicholas Macpherson: I am talking my own book.

Wes Streeting: Rather than get side-tracked with my own personal bugbears about local government, I want to move on to the similar theme about efficiency and reform. Why were these single departmental plans not published alongside the Spending Review and why have they still not been published three months later?

Sir Nicholas Macpherson: They are not ready yet. It seemed to be sensible not to publish them before the Spending Review so that you know what the Spending Review outcome was before you could publish the plans. If I am brutally honest I think it is because the Prime Minister and Chancellor need to sign them off and they have been rather preoccupied on other issues of late, but I hope they will be published soon.

Q53 Wes Streeting: They need to do their homework before blaming them.

Sir Nicholas Macpherson: No, I think they are working very hard.

Q54 Wes Streeting: I am relieved to hear your ringing endorsement of their productivity, but there is a serious point, which is: is there not a case for closer alignment between the two given the relationship between them?

Sir Nicholas Macpherson: If you are going to have a sensible plan you want to know what your resources are, what you are trying to achieve and you want to publish it before the financial year in which it takes effect. We are still in early February, so I would hope they would be published shortly.

Q55 Wes Streeting: How will the single departmental plans be different from the structural reform plans in the 2010 Spending Review?

Sir Nicholas Macpherson: That is a very good question. Kirstin, do you know the answer to this?

Kirstin Baker: Do you want me to have a go on that? The idea is that single departmental plans are supposed to bring together a variety of different things. In the previous Spending Review we had a number of different products and we are trying to bring it all together in one place. The idea is that a department will have one plan that covers efficiency, but also covers the big objectives.

Sir Nicholas Macpherson: Yes, the last time round we had a business plan and we had a structural reform plan, and this is just trying to make it simpler.

Q56 Wes Streeting: I know that this may be semantics, and maybe you will reassure me, but single departmental plan versus structural reform plan sounds like there is a very different emphasis. Have we done all the reform now? Is it job done and we are just plodding along?

Sir Nicholas Macpherson: I have always had a bit of a problem with the word “reform”.

Wes Streeting: The Civil Service has a bit of a reputation for that.

Sir Nicholas Macpherson: No, sorry, I mean in the wider sense of the loose way it is used, especially when combined with “radical”. When I hear those two words together I am always slightly suspicious, but things have to change. There is no doubt about that. If we are going to live with the public spending totals which are being set out, departments

and public services will need to change if they are going to continue to deliver services to a high standard. I suppose the fact that we are not mentioning—apart from the fact that structural reform is not a very good adjective, I would hope the concept of reform is now so embedded you no longer have to refer to it.

Q57 Wes Streeting: We would hope so. One of the things that the NAO said was that departments' budget discussions with the Treasury should not be a separate exercise from ongoing discussions about efficiency, reform and transformation.

Sir Nicholas Macpherson: I totally agree with that.

Wes Streeting: In terms of the process of negotiating the Spending Review, how were those two things aligned as part of the reform process?

Sir Nicholas Macpherson: They were better aligned than I have seen for some time. The Cabinet Office and the Treasury were at the table with the departments. There is a guy called John Manzoni, who is the Chief Executive of the Civil Service. He was very much involved on the transformation and efficiency front and we have worked very closely with him.

Q58 Wes Streeting: One final question, Chairman. You mentioned earlier the rise of officials and we are clear on the way in which the Treasury has extended its reach over various things. Thinking about the process we have just gone through in terms of local government devolution and the way in which those plans have been directly negotiated with the Treasury to such an extent that leaders of local authorities involved in the discussions were instructed that they were not to discuss the process of the devolution deals, even with fellow elected colleagues, is it not time to simply abolish the Department for Communities and Local Government? I hesitate to use the word “reform” in case you get upset, but to radically change the relationship between the Treasury and local government, and recognise that the scale of what we are now asking local government to do means that we do not need the middle man we just want the direct route to the Treasury.

Sir Nicholas Macpherson: Sometimes the Treasury has to get actively involved in things just to ensure that there is real force behind whatever the Government are seeking to do. However, I would be very worried if the Treasury, on a permanent basis, got involved in managing the relationship with local authorities because we are very small and we cover a very broad waterfront. Although we can sometimes make a difference, you want to manage these relationships on a long-term basis.

Q59 Rachel Reeves: Sir Nicholas, I wanted to ask some questions and the sale of financial assets and then about corporation tax. In the OBR's economic and fiscal outlook for November 2015 they forecast that the Government's planned sales of Lloyds Banking Group shares in this financial year would total £12.9 billion. The Chancellor has since announced that that will be delayed, with the

share price now at 58 pence. I wondered when you think they might be delayed to and what implications that would have for public finances.

Sir Nicholas Macpherson: Clearly, if they are not sold this year that has implications of several billion pounds on its own. In terms of when to make the sale, the critical thing is that market conditions are currently very volatile. I do not think the Chancellor has set a timetable about when we will come back to this issue. Obviously, if everything has settled down and the share price looks a bit stronger then it is quite possible the Chancellor might decide on a reasonably rapid sale, so we are in the hands of the markets. The Government have made clear it is committed to a retail sale and I think if you are going ahead with a retail sale you have to be particularly sensitive to what goes on in the markets. I can remember when BP was sold in the late 1980s, the share price fell hugely between the point the price was set and the actual share sale itself, so we are just going to have to see what happens.

Q60 Rachel Reeves: Will the Chancellor come back in the budget with a revised timetable and will there be a revised expectation of the yield?

Sir Nicholas Macpherson: The OBR will have to make a forward projection and it will have to make a projection on the basis of what the Government's plan is for asset sales. That includes both Lloyds and RBS. As I say, the decision has been made not to go ahead with a retail sale right now. Further decisions will be made in due course.

Q61 Rachel Reeves: Two more questions on the sale of financial assets. You mentioned RBS. The assumption in the same document was that sales in RBS shares would raise £5.8 billion a year for four years over this forecast period. The Chancellor has not yet said anything about RBS, but can we assume that will also be delayed given the turbulence but also the weakness of share prices. Then the other question that I sort of asked at the beginning was in terms of the implications—and these are big numbers: £12.9 billion for Lloyds this year and about £24 billion for RBS over this forecast period. If the money does not come from those sales over the Spending Review period where will the money come from?

Sir Nicholas Macpherson: First on the Royal Bank of Scotland, clearly the OBR will make a forecast and my understanding of their forecasting approach is it will be based on the price of the share at the time they make the forecast. Almost by definition, if the share price is a lot lower, you have to assume if you do go ahead and said, “Sell the shares over a four year period” the proceeds will be lower.

Q62 Rachel Reeves: Sorry to interrupt, but would not the more likely scenario be that if the share price is below the breakeven point the sale will not happen?

Sir Nicholas Macpherson: The Government have never made a fetish of the breakeven point. My hope remains that we will make money on RBS in the end. Obviously, a decision will have to be taken as part of the budget process, but this is simply a projection,

albeit one which is satisfied by the OBR, and like all projections and plans it is subject to change. The Government have always made clear that value for money will be an important consideration in share sales. Now, if the events of the last two months have made RBS intrinsically worth 25% less than we thought it was worth two months ago then that will force the Treasury and the Chancellor to reappraise what is value for money. We have owned RBS now for seven and a half years and over that period I have seen pretty big movements in the share price, and the one thing that I would say to any Minister is: “Share prices go down: they go down up”, and in the end this is a good asset which should command a reasonable price”.

Q63 Rachel Reeves: However, it does seem likely that over this Spending Review period we will not raise the revenues that were previously expected just in November from the share sales of RBS and Lloyds, which presumably will mean to fill that black hole either by spending cuts, tax increases or potentially missing the targets for the deficit.

Sir Nicholas Macpherson: The main impact of the share sales is more on debt than on borrowing, but all governments I have worked for have had asset sale plans and they tend to move around. I would not get too depressed at this point. We just had a couple of bad months in the stock market; it does not mean that the world has fundamentally changed.

Q64 Rachel Reeves: On corporation tax, we had in front of us last week John Whiting, a Tax Policy Director at the Chartered Institute of Taxation. When we asked him about corporation tax he said, “The country does have to be prepared for it decaying”—i.e. corporation tax revenues—“We have to be prepared to look at alternatives. We are slipping down the international league in terms of how much we take”. Do you think that corporation tax has a future or that we should be looking at other ways of raising money from corporations?

Sir Nicholas Macpherson: Taxing capital in an era of globalisation is difficult. Capital moves around; people develop ever more sophisticated structures; and the Government are always trying to catch up with those structures. Recently there have been a lot of very sensible initiatives provided by the United Kingdom in a form of the base erosion and profit-shifting initiative and so on, and the Government have introduced a diverted profits tax and so on that should have some effect. However, there is a massive secular force at work here. Getting tax in has always been difficult, but in a world where capital can move freely it is a hell of a lot more difficult than in the days of exchange controls and capital controls. Corporation tax still brings in a decent wedge of money and so we should stick with it, but we should be mindful of our tax competitiveness. Coming back to the issue of contingency planning, the Treasury and HMRC should continually keep under review whether there are better and easier ways of generating revenue, but it is hard work.

Q65 Rachel Reeves: Do you have any views on what those other ways of raising revenue would be, Sir Nicholas?

Sir Nicholas Macpherson: Corporation tax is ultimately an income-based tax; it is a tax on profits. Generally in life if you do not tax income you are left with taxing sales or

using a VAT system, or you tax the employees of corporations or you tax property, hence business rates. None of these are wholly satisfactory. The problem with taxing is that no one likes paying tax and they do not half cut up rough if you seek to impose some new tax on them. Usually when you are shifting taxes you have the gainers who are very happy to take the money and the losers who shout very loudly, so it is a difficult business. The current debate generated by the way certain multinational companies arrange their affairs will mean that there will be pressure on governments across the world to think through how you can develop a more effective tax system.

Q66 Rachel Reeves: One of the risks to corporation tax is the behaviour of the UK's overseas territories. What practical powers do we have over Crown Dependencies in British Overseas Territories in terms of taxation?

Sir Nicholas Macpherson: Over the years we have tried a number of techniques—moral suasion, and sometimes we have got a bit more belligerent than that and tried to bludgeon these territories into submission. You tend to make most progress when there is genuine international cooperation, because you can do what you like to your own dependencies, but if other countries are not acting the money just heads off in that direction. There was quite a good effort through the G7 and G20, and there has been more cooperation and that is a good thing. However, in a world where there is a dominant power, namely the United States, which has always regarded its approach to taxation really differently from the rest of us, it is always quite complicated and difficult.

Q67 Rachel Reeves: This is a genuine question. If an overseas territory got into financial difficulty would we be liable?

Sir Nicholas Macpherson: It depends on the precise arrangement. The strange thing about British Crown Dependencies is just the different forms each of them take, some of which reflects history and so on. As a general matter of course, sitting in the Treasury, I would argue, no, the British Government are not liable.

Q68 Rachel Reeves: If Bermuda, for example, were to get into problems with its public finances—

Sir Nicholas Macpherson: I think that is a matter for Bermuda.

Q69 Rachel Reeves: You have talked about the different powers that we have and you talked of moral suasion and of bludgeoning people into submission. Do we have more powers to bludgeon into submission, to use your language, overseas territories than we would other countries?

Sir Nicholas Macpherson: I suspect we are not so quick to do the bludgeoning as we were in the 19th century. Palmerston would have sent a gunboat down to wherever it was and sorted them out. With the development of current international law it gets a bit trickier. It is precisely the point that because we do not bail out these countries and they are on their

own, and we do not, generally, pay for their services or their security, we do have a huge amount of leverage.

Q70 Rachel Reeves: When the overseas territories started to comply with the international standards of transparency and exchange of information, which in the Treasury document in April 2012 we said was welcome, was that just through moral suasion and international efforts, or was there anything more that Britain was able to do to get them to comply with those standards?

Sir Nicholas Macpherson: I am sorry to say that I cannot remember the precise circumstances. My recollection is more about persuasion but I mean if you want a more considered view I would be happy to volunteer a note. I risk just saying something that is wrong.

Q71 Rachel Reeves: I would be interested in what formal powers we have, if any, and what successes we have had and why you think they have been successful.

Sir Nicholas Macpherson: I would be very happy to.

Chair: Perhaps you would like to describe the bludgeon. We would be very happy to have that described in three dimensions.

Sir Nicholas Macpherson: I think you are being a bit too optimistic.

Q72 Chris Philp: Sir Nicholas, you mentioned the very beginning in answer to the Chairman's questions that you do not plan to be retiring, that you have got some good yards left in you yet. Do you have any thoughts as to where the future might lead?

Sir Nicholas Macpherson: No, none at all. I am required to take three months off unpaid in April, May and June, so while you are all working I am going to run down my savings and perhaps leave the country for a bit.

Rachel Reeves: Go campaigning on the European Referendum.

Q73 Chris Philp: Are there any other external jobs which you would be prevented from taking under the code, or that you could take but you would consider to be inappropriate because it would be some sort of conflict of interest or would run counter to the national interest, bearing in mind all the confidential information?

Sir Nicholas Macpherson: You have to look at each thing on its merit. There is a well-developed code. Anything I do would have to get approved by that. Personally, I would feel pretty uncomfortable going and working for one of the banks that we have put money into or we have been trying to persuade to stay in the UK. You have to look at each case on its merits.

Q74 Chris Philp: You mentioned persuading banks to stay in the UK. Have we been fairly active then in trying to persuade HSBC to stay? Your last remark would imply that we have.

Sir Nicholas Macpherson: No, I just think that you might—obviously, there has been a dialogue between HSBC and the Government, but it is HSBC's decision.

Q75 Chris Philp: Have you won them over?

Sir Nicholas Macpherson: It all comes to some board meeting. It is a matter for them.

Q76 Chris Philp: I was intrigued by John Mann's question about a comparison of Chancellors, but I am not going to press it because you cannot possibly answer it. What I would ask is a slightly different spin on the same question which is—

Sir Nicholas Macpherson: A comparison of membership of the Treasury Committee over the years.

Chris Philp: No doubt.

Sir Nicholas Macpherson: Compare and contrast John Mann with David Ruffley, or whoever.

Chris Philp: I am sure that John Mann is without comparison. If there is a one piece of advice you could give to an incoming Chancellor of the Exchequer, what would it be?

Chair: Listen to your Permanent Secretary.

Sir Nicholas Macpherson: That is a very good suggestion. It is a long game and when things are going badly invariably the cycle turns, and equally in the good times they get carried away.

Q77 Chris Philp: Do not claim to have abolished boom and bust, for example?

Sir Nicholas Macpherson: I am not sure whether that statement was ever made. It is one of those classic statements, which I am sure if you looked at the wider context it might look a bit different. If you are responsible for the economy—and ultimately the Treasury has got some responsibility for the economy—do not get carried away. Do not think that what you are doing is the reason the economy is growing. Generally, governments do more harm to the economy than good and you should trust the market where you can. Markets can be very frustrating, but in my experience bureaucrats and politicians are not terribly good at second guessing them. Those are the sorts of suggestions.

Q78 Chris Philp: That is interesting. That sounds like a small government philosophy to me. You have been at the Treasury for 30 years and

you have got about eight weeks to go; I am presuming there is nothing big you are going to do in the next eight weeks. Is there is one thing, looking back, that you wish you had done but for whatever reason did not have the opportunity? If you could wave a magic wand, what would you change?

Sir Nicholas Macpherson: I am in no doubt about that. I would love to have completely anticipated the financial crisis, and having anticipated it ramped up Treasury resources to deal with it, and then to have persuaded the other members of the Government, the Bank of England and the FSA that we had to take the relevant action. Equally, I am very proud of our action after the crisis hit us. I think the Treasury and the Bank of England played a difficult hand well, but my big regret is not to have seen it coming. In my defence, there were other people who did not see it coming either, but I do not think that is a good enough defence.

Q79 Chris Philp: Okay, that is an interesting point. Rachel Reeves was asking earlier about OBR targets in the context of asset sales, and, of course, that was speculation. In terms of the OBR targets for the fiscal deficit reduction, do you see the risk as to the downside or the upside?

Sir Nicholas Macpherson: We are going to have another forecast in a matter of weeks, so it would be idle to speculate about what it would show.

Q80 Chris Philp: On the topic of corporation tax, which again Rachel Reeves touched on, do you think HMRC has staff with sufficient experience to deal with very highly paid lawyers and accountants for the likes of PwC or Deloitte, or tax lawyers from Freshfields or Clifford Chance, when it comes to negotiating extremely arcane and complex tax affairs of multinationals? To continue on, without wanting to lead you, do you think there is a case for relaxing the Civil Service pay code and letting HMRC hire a small number of very well paid people to properly take on the well-paid advisors on the other side of the table who often run rings around them?

Sir Nicholas Macpherson: That is an interesting suggestion, and I would certainly not rule it out. My guess is that if we adopted it we would start saying, “Look, you have got these people who have come from the tax avoidance industry. They are going to go back to it and you are letting them become even more expert”. There is a genuine tension there.

Q81 Chris Philp: Could I propose a solution to that? That is a very valid concern; you could deal with that one of two ways. You could either say, “Look, we are going to pay you a significantly more than Civil Service salary bands; therefore, you cannot go back to the private sector for five years”, or, more interestingly, partners in these firms—both accountancy firms and the tax practising law firms—tend to retire quite early. You could pick somebody up who is a recently retired partner aged 55 to 60, who by definition would not go back into the private sector and do it relatively cheaply as well.

Sir Nicholas Macpherson: Funny enough, the guy who is the Tax Assurance Commissioner at Revenue and Customs, Edward Troup, is probably the leading tax lawyer of his generation. He is a brilliant tax lawyer and a huge asset to the Revenue. I recruited him to the Treasury in about 2004 when he was about 50, I guess, and in his case we did not have to pay him any more because—

Chris Philp: He had made enough money already.

Sir Nicholas Macpherson: He wanted to do it and he had probably made enough money already. Now, the question, which is a legitimate question, is could we do that on a wider and bigger scale? I spend a lot of time moaning about how difficult it is retaining Treasury staff because they go off and earn lots more money elsewhere. However, on the plus point side there is increasingly a market of really good people who get in the private sector, get to about 50 and they are bored and they want to make a difference. They are no longer interested in money and they will come and work for us. Another very good example is Charles Roxburgh on the financial service side.

Chris Philp: Is he an ex-McKinsey partner?

Sir Nicholas Macpherson: He is indeed.

Chris Philp: I started my career at McKinsey. I think I used to work for him about 15 years ago or 20 years ago.

Sir Nicholas Macpherson: There you are you see, some of this is happening already. The question is whether we can do it on a bigger scale. In some shortage areas, provided that we can really quarantine the area, we should be prepared to pay more but on the understanding that there is a different contract. What I do not want to do is then recast lots of existing employees as tax experts and give them a whopping great pay increase, because I do not think they probably merit it.

Chris Philp: Absolutely. If you can push this idea in the next eight weeks I would encourage you to do so. There is also another very good guy who was a PwC partner who has now joined Oxford University's Centre for Business Taxation. He is exactly the same mould. These people are out there.

Rachel Reeves: Send his CV in.

Chris Philp: These people are out there and, as you say, they do have an appetite to put something back, entering into public service. Having spent the first 30 years of their career making cash, they do now have a different set of incentives. I do think we are getting outgunned by very highly paid, high calibre experts, tax law firms and accountancy firms.

Chair: These are points that you will be able to put in your valedictory note, which of course will be of use to your successor.

Q82 Chris Philp: On the question of corporation tax...

Chair: Briefly, if you would.

Chris Philp: Yes, Chairman, I think there is a vote in five or six minutes. It has recently been contended by a large multinational they do not have a permanent establishment in this country despite employing 2,200 people on an average salary of £160,000 and being on the verge of moving to a £1 billion office near Kings Cross. Do you think our tax policy, for which the Treasury is responsible, needs amending if that claim can seriously be made and upheld by HMRC?

Sir Nicholas Macpherson: Potentially, by which I mean there is a horrible arm-to-arm wrestling match that continues where well-advised, footloose companies, where it is very difficult in a digital world to identify the substance of their business, argue their case in one way. We then are forced into changing the law. They then get around that change in the law. Coming back to corporation tax, one reason why—and this is not an ideological position—I genuinely believe in this space there are benefits in lower tax rates if only to ensure that the companies who pay their tax do not get discriminated against. It does not mean we should give up in terms of trying to extract some revenue from some of these companies.

Q83 Chris Philp: Does our tax law need to change around transfer pricing and permanent establishment? It does not seem to be working.

Sir Nicholas Macpherson: We have changed the law quite a lot in this space already, and obviously we have to remain alert. I have seen all sorts of different tax regimes over the years, but it is extraordinary how revenues remain in a very narrow range whatever the tax regime. That is not that I am being defeatist; it is just that I am trying to be realistic that it is hard word.

Q84 Chris Philp: We need to work harder because Google have got away with murder. On your watch the tax code has grown to 20,000 pages, roughly, the largest in the world.

Sir Nicholas Macpherson: The reason why it is 20,000 pages is there is this endless attempt to chase after the people who are trying to avoid the tax.

Q85 Chris Philp: There are also hundreds of reliefs, literally hundreds.

Sir Nicholas Macpherson: Who gives reliefs? The Treasury is an institution that instinctively quite likes low reliefs and low rates, but Chancellors have to make budget speeches and they have to fill it with things.

Q86 Chris Philp: Can I finally just clarify a point Rachel Reeves was touching on, on overseas territories and Crown Dependencies? Can you just confirm what I think is the case that the UK Government cannot issue instructions to overseas territories and Crown Dependencies on matters such as how they run their tax laws?

Sir Nicholas Macpherson: It depends on the precise constitution, but generally, yes, we cannot. They would be part of the UK.

Q87 Chair: We have ranged very widely this afternoon, but you predicted that, Sir Nicholas, before you began. Thank you very much for coming to give evidence, not only this afternoon but on so many other occasions. They have always been enjoyable exchanges and sometimes illuminating as well. We are looking forward very much to your further thoughts that you are going to provide, and it is very kind of you to offer.

Sir Nicholas Macpherson: I did not offer it. I said I wanted to be helpful.

Chair: It was very kind of you to offer in the way that you did. In the meantime, I think we should wish you a happy—not retirement, but a happy further career which you are going to move on to. Kirstin Baker, I would just like to say thank you very much for coming along. You were able to make a brief but valuable contribution to the hearing and I have no doubt we will be hearing more from you in the future. Thank you very much indeed.

Sir Nicholas Macpherson: Thank you and can I just say I think accountability does matter, and long may you summon Treasury officials before you because we do take it seriously and it forces us to perform better than we otherwise would.

Chair: We will take that thought to heart, that grenade with the pin out that you have left behind for all those poor Civil Servants that are now going to be called as we pick up your