Treasury Sub–Committee

Oral evidence: Work of UKGI and UKFI, HC 923

Tuesday 26 March 2018

Ordered by the House of Commons to be published on 26 March 2018.

Watch the meeting

Members present: John Mann (Chair); Rushanara Ali; Mr Simon Clarke.

Questions 1 - 65

Witnesses

I: James Leigh-Pemberton, Chairman, UK Financial Investments Limited; Mark Russell, Chief Executive, UK Government Investments Limited; Justin Manson, Director, UK Government Investments Limited.

Examination of witnesses

Witnesses: James Leigh-Pemberton, Mark Russell and Justin Manson.

Q1 **Chair:** Gentlemen, good afternoon. We are clashing with the Prime Minister. I am sure we are far better off in here: less Punch and Judy, and more serious questions. Can I welcome you? For the record, could you just introduce yourselves, please?

Mark Russell: I am Mark Russell, the chief executive of UKGI.

James Leigh-Pemberton: I am James Leigh-Pemberton. I am the chairman of UKFI and deputy chairman of UKGI.

Justin Manson: I am Justin Manson from UKGI. I am a director there.

Q2 **Chair:** Welcome. Can I start, Mr Leigh-Pemberton, with the question of RBS shares? Is now the right time to start disposing of the remaining ones?

James Leigh-Pemberton: We keep all the opportunities to sell these shares under constant review. It is part of our mandate to do so. We are required to do so under the terms of the framework document that we have with HM Treasury.

For us, the key consideration in relation to timing is always whether the market price is at or above what we believe to be fair value for the taxpayer. Fair value for the taxpayer will be determined by our valuation work and is an outcome of the current and future prospects for the bank. It depends very much on market conditions. There will be times when the market price and the price at which we can make disposals will be above our fair value. There are many times when the market is not fully valuing the shares in our view and we make the decision on whether to proceed—or the recommendation on whether to proceed—fundamentally based on that valuation work.

Q3 **Chair:** How is this share sale going?

James Leigh-Pemberton: We have only made one sale so far, and that was in the summer of 2015.

Q4 **Chair:** You are making preparations now, of course, for the future.

James Leigh-Pemberton: We like to be ready at all times because, if the market conditions are conducive to a successful sale at good value for the taxpayer, we would like to be ready to take advantage of that. Yes, we keep our valuations constantly updated. We stay in close touch with market conditions. We monitor those closely. We like to be in a position to proceed whenever the opportunity presents itself.

It has been widely reported publicly, and it is very much covered in all the current research reports on RBS, that the resolution of one final litigation matter, namely the negotiations between the Department of Justice in the United States and RBS in relation to RMBS mis-selling in 2005 to 2007, is a pending item that would be very helpful to have out of the way to enable future sales, but it is not a necessary condition for future sales.

Q5 **Chair:** Has that changed investor sentiment towards you?

James Leigh-Pemberton: It varies enormously depending on wider market conditions. Clearly, that litigation had not been settled at the time of the 2015 sale so it did not prevent a sale then. In the current environment, there are many investors who would like to see that matter resolved before committing themselves to buying RBS equity.

Q6 **Chair:** What role did you play then in advising the Chancellor on the suitability of the schedule that he has set you? What concerns did you outline to him?

James Leigh-Pemberton: We did make clear that these sales are all dependent on market conditions. The schedule of sales that the OBR has in its most recent publication is based on conversations that the OBR had with us. In the end, the linear programme that the OBR has in its publication, £3 billion per annum, is highly unlikely to be the way that it actually happens. In the aggregate across the planning period, in our view, based on our experiences to date including those with the disposal of Lloyds Bank, it is a reasonable assumption that that scale of disposal could be achieved over that planning period.

Chair: The Chancellor has said £15 billion by 2023 and you have given him advice.

James Leigh-Pemberton: Yes.

Chair: Presumably your advice was, “Yes, we can do that”.

James Leigh-Pemberton: Yes, it was. Our view was that we would be able to achieve that. As I said, I am not sure that it will end up being five per annum blocks of £3 billion each. Based on our experience of Lloyds Bank and based on the progress that RBS has made in dealing with the great bulk of its legacy issues and the investability of the stock, our advice was that such a programme would be achievable.

Q7 **Chair:** Has it ever been perceived that it would be £3 billion a year, or was your advice to the OBR always that this would fluctuate and that it was unpredictable what the spread would be during that period?

James Leigh-Pemberton: Yes, we indicated to them that, in the aggregate over that period of time, a £15 billion disposal programme would be achievable. We were never asked to specify what amount in what year.

Chair: They are guessing.

James Leigh-Pemberton: No, they are making reasonable assumptions based on the size that we have achieved so far and the regularity with which we have been able to sell so far.

Chair: If you were giving them more detailed information, they would be able to change their forecasts and make them more predictable. They have simply averaged.

James Leigh-Pemberton: Yes, they probably have.

Chair: They have averaged including from now on.

James Leigh-Pemberton: Yes, but the assumption that we would be able to make disposals aggregating £3 billion in the course of this year, subject to the resolution of the litigation issue, is entirely fair.

Chair: We do not know when that will be resolved.

James Leigh-Pemberton: No, we do not.

Chair: We do not know, then, when we will be selling these shares.

James Leigh-Pemberton: We have had market conditions in the past where it has been possible to sell shares without the resolution of this matter. As things stand today, there is no question but that it will be much easier when this matter has been resolved, and it is likely that we will make our next sale only after that. That may change; it may not.

Q8 **Chair:** What has changed in that period of time, then?

James Leigh-Pemberton: The perception of the market is that we are closer to the moment where there will be certainty on this matter. The closer you get, the more investors will tend to focus on the matter.

Q9 **Chair:** There are very many different views on what will happen post leaving the European Union. What model are you using to factor in the impact of leaving the EU?

James Leigh-Pemberton: We have really taken the guidance of the management team in building our model.

Q10 **Chair:** What does that mean?

James Leigh-Pemberton: The management team provide guidance to the market.

Q11 **Chair:** What guidance?

James Leigh-Pemberton: They provide an outlook on their perception of what market shares they will have in what segments of the market, what they expect net interest margins to be.

Q12 **Chair:** No, what I meant was: what are you forecasting? What is your expectation?

James Leigh-Pemberton: For earnings and revenues?

Q13 **Chair:** Yes. We are about to leave the European Union. You are trying to sell a big chunk of shares, so you have to model in when you think the best-timed price is going to be. This is potentially a factor in it and I am just asking how you are doing that, or are you not doing it?

James Leigh-Pemberton: We take the guidance of management and we build our model in the same way as most other analysts build their model, based on the outlook provided by the company. The critical elements in all that, of course, are revenue growth and RBS's market shares in its chosen segments. We build it RBS-specific, market by market, rather than on the basis of a large macro view.

Q14 **Chair:** Will RBS take a hit in the 12 months after we have left the European Union, in your judgment?

James Leigh-Pemberton: Currently, it is not expected. The impact of the vote to leave has historically been felt really through its impact on monetary policy rather than on provisioning or future impairment. Most models see a normalisation of impairment over the next five years. They are at historically extremely low levels at the moment and the cost of risk is at an all-time low. They will revert to norms, but that is already reflected in the price.

Q15 **Chair:** You warned us in 2016 about the issue of the US litigation, so you had highlighted that very appropriately to this Committee and to Parliament at the time. But you are saying basically that everything is on track as before. There is the Chancellor's announcement, and we will reach that. What has happened to your chief executive, then?

James Leigh-Pemberton: Our chief executive has informed us that it is time for him to go back to the private sector. I have to say that, when Ollie agreed to join UKFI, it was originally planned to be for a period of three years. He has done a very good job for the thick end of four and a half years. Given the nature of our company, it is always the case that, in due course, people will move on. We are a company with a finite purpose and, when that purpose is complete, the job is done.

Q16 **Chair:** People are speculating publicly at the moment that there are other reasons, which is hardly surprising because the Chancellor has just given a very clear timetable. There is a job to be done and suddenly the chief executive goes. People are suggesting that perhaps things are not going as well as they should be.

James Leigh-Pemberton: I can assure you that that is not the case. Ollie's predecessor returned to the private sector and Ollie came in to succeed him. This is an entirely natural sequence of events for a company like us or for UKFI.

Q17 **Chair:** Are the press reports expressing concern in relation to this and the reason for it totally factually inaccurate?

James Leigh-Pemberton: That is correct, yes. They should not be expressing such concern.

Q18 **Chair:** Can I home in on one of the smaller but important issues? Your previous 2015 sale had negotiated competitive fees, with most advisers only charging a pound for their services. Do you anticipate that success again?

James Leigh-Pemberton: We have been cautious with the Committee in the past about the sustainability of these very low fees. We are hopeful that we will be able to repeat that. The competitive environment in markets and overall market conditions, we hope, have not changed so much that we will not be able to repeat it. Until we actually go out and test, we will not know for certain. We hope that we will be able to do so but there is no certainty that we can.

Q19 **Chair:** Are you considering a retail offering?

James Leigh-Pemberton: A retail offer is always part of our toolkit. We have said before the Committee in the past that, in the right circumstances, which would normally be when there is a price at which we would like to achieve large size in our disposal, a retail offer is the most appropriate way of capturing that additional size. It increases the pool of investable capital in the offering very significantly. We will always consider it but the method of sale from time to time has to be chosen to deliver the best value, and that will be very much dependent on market conditions.

Q20 **Chair:** Have the Government let you know that they will be comfortable with a retail sale?

James Leigh-Pemberton: It is not a topic on which we have really done any work recently. I do not know the answer to that.

Q21 **Chair:** In the first sale of RBS, a leak was found without the source being identified. What has been learnt from that?

James Leigh-Pemberton: We conducted a rigorous inquiry. We determined that the leak had not come from UKFI. We have always kept to a bare minimum the circulation of price-sensitive information. We observe rigorous procedures in terms of insider lists and confidentiality. As a result of that, we have reminded everybody of the necessity to stick to those procedures.

Q22 **Chair:** I will ask my questions as one, so I am going to jump rather than come in, dependent of course on your answers, a second time. There are a couple of questions in relation to UKGI. The first is whether the relationship with the Treasury in any way impedes your ability to optimise value for the taxpayer.

Mark Russell: I would say no. One of the things we were concerned about and careful about was that, when the Shareholder Executive was incorporated and became UKGI, a subsidiary of the Treasury, our relationships with the departments did not change and we kept the same operating model that we had in the Shareholder Executive. Pretty much, I would say that has worked. Our basic operating model is that we operate on behalf of 10 departments at the moment. When we act on behalf of a department, it is as though we are officials of that department. We observe the same protocols as officials of that department. We report up to the Permanent Secretaries and the Secretary of State.

The fact that the Treasury is our shareholder does not impinge on the operations of UKGI. It provides overall guidance but does not have any special access into our activity. We have established, just as UKFI had established, a good arm's-length relationship with the Treasury such that we can provide independent and impartial financial advice both to the Treasury and to the departments.

Q23 **Chair:** What about BEIS? How often does it stick its nose in and interfere with what you are doing? Should it be doing it more often?

Mark Russell: The Shareholder Executive was part of BEIS. We were a DG group in BEIS. Probably just under half of the wider UKGI activity is still for BEIS. We have a lot to do with it. Would I say it sticks its nose in? I would not quite put it like that. We see it as the most significant of our clients. At any one time we must be doing 10 to 20 activities for it. As I say, the model is very much as though we are part of the department when we do its work. It is absolutely intimately involved. It takes our advice but our advice is offered in that independent fashion.

Q24 **Chair:** My final question is back to you, Mr Leigh-Pemberton, just to reiterate this again, on these RBS share sales. We have nothing to worry about, then. This is going to go ahead smoothly over the timescale that has been announced. Is there anything at all of major significance that we should be worried about? Is there any particular timescale by which you will be hitting problems if court action has not been resolved? Is there any serious impediment that we should be aware of that we are not, so that we do not turn around at a future stage and say to you, or whomever, "You did not tell us"?

James Leigh-Pemberton: Yes, market conditions, for sure. In order to sell these shares, we must have markets that are conducive. We must have good investor appetite, and that is highly variable, particularly for financials. We have had periods over the last 24 months during which, effectively, markets were closed to the making of new issues of equity. We are always at the mercy of market conditions. A long period of muted risk sentiment and lack of demand on the part of investors to increase their exposure to equity markets could have an impact on the deliverability of this sale.

Over an extended period of time, one would expect that those market conditions would normalise, which is one of the reasons why I think we will not be doing even numbers of sales every year. That could be a constraint on the timetable. A long period of disturbed and difficult market conditions would be a constraint on our timetable. The operating strategy of RBS is headed in the right direction. It is clear for the period out through 2021. We do not anticipate any material change in that. The biggest constraint is market conditions that are not conducive to making large sales of equity.

Q25 **Rushanara Ali:** Good afternoon. My questions are focused around asset sales and governance. Can you start off by setting out what other Government assets UKGI is planning to sell next?

Mark Russell: It is fair to say that there are just two categories of asset at the moment: the assets that currently sit within UKFI, so those of RBS that we have been talking about, and the UKAR assets.

Rushanara Ali: Sorry, what was the second one?

Mark Russell: UK Asset Resolution assets. The other asset that we have traditionally dealt with in the Shareholder Executive and UKGI ex-UKFI is the student loan receivable. There are one or two much smaller potential transactions but, by and large, those are the three main assets that we are focused on at the moment.

Q26 **Rushanara Ali:** What are the smaller ones?

Mark Russell: There is, for instance, a residual holding. As you know, we sold the Green Investment Bank last year and retained an interest in some investments there. Over the next two or three years we expect to realise those, but these are relatively small amounts.

Q27 **Rushanara Ali:** What sort of criteria do you use when you are assessing sale of assets?

Mark Russell: The key one is that we can demonstrate value for money.

Q28 **Rushanara Ali:** Do the Government give you instructions on what to sell next?

Mark Russell: Departments do. The Student Loan book is owned by the Department for Education. The financial assets of UKAR and RBS are owned by the Treasury. But, be they owned by the Treasury or owned by an individual department, the Treasury is very much bound up into that conversation as to whether a sale should be triggered.

Q29 **Rushanara Ali:** Does the lead usually come from individual Government departments, rather than the Treasury? Does it depend on what it is?

Mark Russell: For something as large as the student loan transaction, it was talked about for some time. It had been on the Treasury's radar and it had been on the Department for Education's radar. Our client, as it were, for the sale was the Secretary of State for Education. The accounting officer who ultimately decided on whether a sale should proceed was the accounting officer for the Department for Education. Clearly, on such a large sale, the Treasury will be involved.

James Leigh-Pemberton: In our framework document, with respect to the assets that were required in the interventions of 2008—that is, what we now call the legacy UKFI assets—there is an acknowledgement that it is not Government policy to be a permanent owner of those assets. They were not acquired as a matter of policy so it is not policy that Government should be a permanent owner. There is therefore a small distinction between those assets and the rest of them.

Q30 **Rushanara Ali:** Do you want to say which ones are which, for the record?

James Leigh-Pemberton: For the record, that means the shares in RBS, and the mortgages and other assets held in UK Asset Resolution: the Northern Rock and Bradford & Bingley mortgages held in UK Asset Resolution.

Rushanara Ali: Student loans would not fall into that category.

James Leigh-Pemberton: That is correct; they would not fall into that category.

Q31 **Rushanara Ali:** That follows neatly on to my next question. The OBR has explained that selling assets such as student loans or other illiquid assets does not improve the public finances; it just exchanges one asset with another. Can you reflect on what you think of that and your response to that assertion?

Mark Russell: Can I call in Mr Manson, who led the student loan sales?

Justin Manson: The reflection I would have is it is swapping an illiquid asset for a liquid asset in the form of cash, depending on what you think is the important criterion when judging the public finances. We all have different ways of looking at it depending on our purposes, but essentially it is the exchange of an illiquid asset for cash.

Q32 **Rushanara Ali:** Moving on, can you say a bit more about the economic rationale for selling student loans? I hear what you are saying, but please expand on what the economic rationale is for selling off student loans.

Justin Manson: Starting with the point there, there was a determination that there was no strategic or rather policy benefit from continuing to hold the plan 1 loans. There was a determination that, if fair value could be achieved, those loans should be sold, cash realised and deployed for other government priorities.

Q33 **Rushanara Ali:** Let us move on to the Post Office. What involvement does UKGI have in the management of the Post Office?

Mark Russell: We do not directly manage it. The Post Office is one of the shareholdings that we advise on, on behalf of departments. The Post Office is owned by the BEIS department. When we carry out a shareholder role, we are involved in advising on: the governance of the organisation, so whether it has an adequate board; appointments to that board, which are typically Secretary of State appointments; whether it has a clearly defined strategy and business plan; and whether there is a proper delineation between what the department does and what the organisation does. One of our big things is that, if you have an arm's-length body, you need to get the benefits of an arm's-length body. It can get difficult where that dividing line is fudged.

We look at governance, we look at business plans and we look at financial settlements. We also try to ensure that communication between arm's-length bodies such as the Post Office and departments is as good as it can be. The flipside of ensuring that you have a discrete arm's-length body is that it could go a bit native. I am not saying that the Post Office has done that, but that has been known in the past where the boards of our arm's-length bodies maybe do not fully understand what Ministers' interests are. That is one of the key tasks and indeed one of the reasons why, in most cases, we put one of our own people on the boards of the arm's-length bodies. In the case of the Post Office, somebody from UKGI sits on the board. But it is a very pure shareholder-type activity, to try to drive the efficiency of the organisation.

Going back to a point that James was making, Government will typically only hold commercial organisations and arm's-length organisations if there is a policy reason for doing so. With something like the Post Office, there is a policy reason. Ministers have a clear wish to ensure that a certain number of post offices are kept open, which inevitably means that a proportion of those 12,000 offices will have to be subsidised because they are in more rural communities.

One of our key tasks as shareholder, in performing the shareholder role, is to make sure that those policy decisions are properly costed and that there is no confusion over them. Ultimately, it is for Ministers to do what they want but we must make sure that they understand the cost and that there is no fudging of that.

Rushanara Ali: In both directions.

Mark Russell: In both directions, absolutely.

Q34 **Rushanara Ali:** You have mentioned one of the key priorities. Do you have other priorities as representatives of the board in relation to the Post Office? Can you give some examples of where you might be at odds with the rest of the board, and how you settle those sorts of differences as you are trying to help them develop their strategy?

Mark Russell: You asked about other priorities. Ministers have an ambition for the Post Office to become as efficient as possible and to become profitable—profitable, that is, before the subsidy that goes into the chain of post offices that will always be uneconomic. The ambition is that the organisation makes enough profit to be able to cover that. There is a focus on that, and that is the other key focus.

You asked whether there are moments of tension on boards. Yes, there are moments of tension. A very obvious one would be around remuneration where you will often find—and I am not necessarily talking about the Post Office here in particular—that the more commercial arm's-length bodies are pushing for fairly high remuneration.

Q35 **Rushanara Ali:** At the top or across the board?

Mark Russell: It can be across the board.

Q36 **Rushanara Ali:** In relation to the Post Office, is it at the senior level?

Mark Russell: The Post Office has a number of highly paid people who are above the Prime Minister's salary. On the one hand, we have sympathy with this point that these are big organisations that need commercial skills that you can probably only get from the private sector. On the other hand, we recognise that the Post Office is in the wider public sector and we have an obligation to ensure there is some type of pay constraint.

You might get situations where boards are pushing for pay rises or remuneration structures that we think ultimately will not be sanctioned by Ministers, and that would be a point of tension for a non-exec that we put on our boards. The way we deal with that is simply to recuse ourselves from that particular decision. We are pretty clear that, when we are on the boards of companies, we must ensure that we are not in conflict with the wishes of our shareholder.

Q37 **Rushanara Ali:** I have one more question on the Post Office. What is the gender pay gap?

Mark Russell: I do not have it for the Post Office but that is something that I can get for you.

Q38 **Rushanara Ali:** Could you? Also, do you take an interest in that dimension of the organisation?

Mark Russell: Absolutely.

Q39 **Rushanara Ali:** How do you use your influence to try to, for instance, get it to look at steps to address the pay gap? There is a separate issue on the charter on gender pay.

Mark Russell: We absolutely pay attention to that. I do not know the gender pay gap at the moment. I can say that the board has a good male/female ratio. Of the nine board members, four are women. The chief executive is a woman. We look at, and have most control over, boards. When we are involved in the recruitment of non-executive directors, we are continually pushing that agenda.

We are deeply conscious that that is only part of the story here. It is further down the organisation, particularly within the senior management, that we have to promote that. The key to that, I think, is persuading the board and the executive of the importance of this, as well as the business sense of it. Yes, we are absolutely on this point.

Q40 **Rushanara Ali:** Are they not persuaded yet?

Mark Russell: Yes, many are.

Q41 **Rushanara Ali:** It is an interesting use of the word "persuasion" when the evidence is very clear. Do they need to be persuaded? Why should they be persuaded? Should they not be doing it?

Mark Russell: I think most are persuaded. It is a question of how they practically go about it. It is about things such as using head-hunters that are extremely tenacious in finding women candidates. It is about making sure that the benefits and the working deal that they give to employees are flexible, because, again, we know that that is a very tangible way of attracting diversity.

Q42 **Rushanara Ali:** Did anyone else want to add anything in relation to the Post Office? If not, I am going to move on to the next set of questions, which is in relation to the governance of Channel 4. How would you describe UKGI's role in relation to Channel 4 and governance?

Mark Russell: How would I describe it? It is relatively light touch. That derives from the fact that our role as shareholder can only be derived from the controls that the shareholder—in this case, DCMS—has over an organisation. In the case of Channel 4, DCMS is not technically a shareholder, but it is within the remit of DCMS. Under the Act that established Channel 4, DCMS has a locus on the organisation.

What does it actually boil down to? The particular interest in DCMS is to make sure that the organisation is a sustainable one that continues to perform the public service that it has been asked to do, given that its financial model and operating model is very skewed to the success of advertising revenue. In fact, there is no other broadcaster quite like that. That, in some respects, makes it vulnerable.

Going back to our role, we are not on the board, because DCMS does not have that option. We do, I believe, have a good working relationship with the management of the organisation. We look at the financials of the organisation to satisfy ourselves, and so satisfy DCMS, that it is financially sustainable.

Q43 **Rushanara Ali:** I am being told by the Chair that I have two minutes, so I have to compress everything. I will just give you some quick-fire questions. Can you explain why the Channel 4 gender pay gap is as high as it is, what it is, and how you will use your influence to address that? Start with that, and then I will move on to the next one.

Mark Russell: I am aware it is high. As to the reasons why it is high, I am not in the detail of that. I am aware it is high. I am aware that the new chief executive, Alex Mahon, is extremely concerned about this.

Q44 **Rushanara Ali:** It is nearly 30%. What will you personally do, given your role and remit, to address that gap? Can we have an undertaking that this is actually going to be dealt with?

Mark Russell: The simple answer to that is to ask for a plan from Alex as to how she will address it. That is what we will do.

Q45 **Rushanara Ali:** Are you going to make sure that that happens?

Mark Russell: Indeed, I am going to make sure that she delivers a plan as to how she is going to do it. Whether I can ensure the plan is implemented—

Rushanara Ali: You have a major role in the organisation.

Mark Russell: Yes, but our levers and the DCMS are levers are limited. Without a doubt, I know she is on this case.

Q46 **Rushanara Ali:** Okay. Let us get on to this one final question in relation to Channel 4. Considering UKGI piloted the Future Boards Scheme, can you say a bit about your view on Althea Efunshile being blocked for the appointment on the Channel 4 board in 2016? You mentioned DCMS. There are broader issues: not just the gender pay gap, but a capable ethnic minority person being blocked. How are we meant to have confidence that DCMS, and you by extension, will address some of these underlying problems both on race and gender? It does not send a very good message, does it?

Mark Russell: No. I do not have the answer to that but I can get the answer.

Q47 **Rushanara Ali:** Could you write to us explaining what you plan to do to address the lack of confidence?

Mark Russell: I certainly will. I am aware of that issue, but I do not know the detail.

Rushanara Ali: A lot of Members of Parliament wrote about this and we did not get a satisfactory response.

Mark Russell: Fine, I will get you one.

Q48 **Rushanara Ali:** I have one final question. Could you say a bit about the role and priorities in relation to Network Rail? Is there anything that you want to add to that on your involvement with Network Rail?

Mark Russell: It is relatively limited. One of my colleagues sits on the board of Network Rail. Network Rail, as you know, is one of DfT's three large arm's-length bodies. Our role, in large part, is to ensure that the relationship and communications between Network Rail and the department are as good as they can be because they have not always been great. As you know, the status has changed. It was a very independent organisation and it is now on the balance sheet of the Government. Getting that change, and the fact that the Government have a greater locus on how the organisation is run, has not been a particularly straightforward matter. Part of what we are trying to do is to ease that relationship.

Rushanara Ali: Thank you very much.

Q49 **Mr Clarke:** Mr Russell, if I may, I will take our questions on to UK Asset Resolution. How involved is UKGI in the day-to-day management of UKAR?

Mark Russell: Do you mind if I pass back to James? He has the more direct locus on that.

Mr Clarke: Yes, that is fine.

James Leigh-Pemberton: We are not involved in the day-to-day management. We have representation on the board. We have a very close and continuous engagement with it, but our mandate letter and our framework document provide that management and the board should be responsible for running the organisation commercially.

Q50 **Mr Clarke:** That is fine. There has been controversy around the fact that UKAR's disposal of part of its mortgage book was to consumer detriment. I am thinking here of the disposal of part of the former Northern Rock asset book to Cerberus on the basis that Landmark, which was the vehicle through which Cerberus purchased part of the asset book, was not a deposit-taking bank and therefore could not pass on interest rate changes in full to its customers. Is that something that UKGI can answer for?

James Leigh-Pemberton: Yes, we can. We received undertakings from Cerberus shortly afterwards that the borrowers would benefit from the decline in rates. We had included, in the terms and conditions of that sale, a requirement on Cerberus that it could not increase rates at a rate greater than the change in base rate. I regret to say that, at that time, we did not contemplate the possibility that, from the very low level of base rate, there could be a further decline in the base rate. We have learned that lesson and in all future UKAR sales there will a both-directional requirement to track official rates.

Q51 **Mr Clarke:** Let us hope that conditions continue to improve so that is not necessary but, yes, that would be extremely pertinent. There is also criticism of Cerberus's tax domicile, because it structured its vehicle through the Netherlands and the Caymans. In 2016, the Public Accounts Committee recommended that the Treasury should produce "unambiguous guidance, for both selling departments and potential bidders on if, and how, tax will be taken into consideration as part of a sale". Have you received any such guidance?

James Leigh-Pemberton: No, we have not. If this is in reference to the findings of the Public Accounts Committee in relation to the sale of Northern Rock mortgages to Cerberus, when the Treasury replied to the Committee to make it known whether it would carry out the recommendations, the point was made that it is a very difficult thing in the context of a competitive bid to exclude potential buyers on the grounds of their tax domicile, first, because it might not be effective—that is, they can always change their tax domicile shortly after the sale has been completed—secondly, because there might be some risk that it would be perceived as anti-competitive and even a litigation risk and, thirdly, because it could compromise the achievement of value for money for the taxpayer.

Q52 **Mr Clarke:** To quote the PAC report at the time—and it is always interesting when someone starts quoting a Committee that is not one's own—"We note that in response to a previous report of this Committee, HM Treasury formally agreed that it was legitimate to prevent offshore arrangements used in a transaction". The Treasury appears to have conceded that point but nonetheless I appreciate the legal and financial ramifications. In future sales, will you request that UKAR considers the tax domicile?

James Leigh-Pemberton: We intend to continue to apply those same principles, namely that our No. 1 objective when making these sales is to ensure that we have the most competitive sale possible—that is, the largest number of potential bidders with a view to achieving the highest possible price on behalf of the taxpayer. That is what we are required to do both by our mandate and in terms of managing public money.

In future, we will continue to use the procedures that we have used in the past, primarily because, as I said, it is very difficult to be certain as to the long-term impact of any undertakings that might be made in relation to the tax status of any particular buyer. It is very difficult to enforce those over the medium term; they can always be changed in the future. To sacrifice value at the outset in return for something that may be changed shortly thereafter seems to put best value for the taxpayer and best value for money at risk.

Q53 **Mr Clarke:** You would appreciate, however, that in a constituency like my own in Middlesbrough, or indeed in John's or Rushanara's, there is real angst about people being seen to play HMRC or any Government department in that way.

James Leigh-Pemberton: I fully understand that. As was explained at the PAC meeting in this particular case, as with many other funds that receive moneys from investors all over the world, the principal reason for incorporating them in these places is so that the returns can be sent back to the investors tax-free and they are then taxed in the country of residence of those investors. That is what happens in the case of the Cerberus fund in question.

Q54 **Mr Clarke:** Can I touch on help-to-buy loans and the disposal of those? What is the economic rationale for this sale?

Justin Manson: As far as I know, there has not been an explicit economic rationale pronounced by the Government or the relevant department. So far, there has been some speculation about a possible sale, but I do not think an explicit rationale has been set out.

Q55 **Mr Clarke:** These are products that are intrinsically vulnerable to a downturn in the residential property market. How could companies buying these loans protect against that? I do not want to see another asset bubble. This has echoes of 2008 and before, when you start speculating in this sort of field. How would companies protect themselves from the risk of such a downturn?

Justin Manson: When you say "companies", do you mean potential purchasers?

Mr Clarke: Yes.

Justin Manson: It is hard to do. There are not many places you can hedge that kind of risk. You have identified one very important aspect that would have to be contemplated in any potential sale, and there are others too. They are not straightforward instruments.

Q56 **Mr Clarke:** Indeed. Are you able to provide a guarantee that help-to-buy borrowers would not suffer from any such sale? This goes back to the point about Cerberus and the attendant risks that may not immediately be apparent.

Justin Manson: At this point, our involvement in looking at help to buy has been extremely limited and our influence on what comes out of that is still in very early stages. I am not sure that anything is being taking forward in any case at this time.

Mark Russell: To be clear on that, there is no exercise at the moment to look at the monetisation of that. It is an obvious asset that could be looked at but, a bit like student loans, it will have many challenges because it is a pretty contingent income stream.

Q57 **Mr Clarke:** For the second part of my question, I want to move on to the operation of UKGI itself and, in particular, the issue of remuneration. In your annual report for 2016-17, the median staff salary at UKGI was £78,045, which is very significantly higher than the median salary at UKFI, which is £37,110, and indeed at the Treasury, which is just under £46,000. How do you justify the fact that UKGI salaries are so much higher than at those other two organisations?

Mark Russell: I will start on that. They are two very different sizes of organisation.

Mr Clarke: I appreciate that.

Mark Russell: UKGI ex-UKFI is about 100 people. It is a senior group. In terms of senior Civil Service equivalent, of those 100 people, about 30 are senior Civil Service, so directors or executive directors. It is a very different profile to what you would see in a department. Half of UKFI staff are NEDs and that is the reason that it is pulled down: half of the employee count are non-executive directors, who will be drawing fees of £30,000 or so.

Mr Clarke: I see. It is distorted downwards, in other words.

James Leigh-Pemberton: We are a very small organisation. There are really only, on average, between 10 and 14 people at any one time working in UKFI. The fact that we have an independent board of directors who account for quite a significant proportion of our full-time equivalent headcount brings the pay level down.

Q58 **Mr Clarke:** How is the non-executive remuneration calculated?

James Leigh-Pemberton: They are paid NED fees in the order of £30,000 per annum.

Q59 **Mr Clarke:** Right. I will go on, at this point, to payments. Going back to the report, you spent £916,000 on "professional services" in 2016-17. That seems a very high figure. I just wanted to understand how that breaks down and how it relates to the £20,000, which is obviously a very small sum, on consultancy expenditure. I am just keen to understand what this entails. It seems a lot on professional services.

Mark Russell: The £900,000 refers to fees we will pay to professional advisers on our various transactions and for consultancy. The £20,000 I do not recognise but, in our budget of £14 million—this is within all UKGI—about £1 million is allocated for advisory expense. Typically, we do not spend anything like that but we have that budget available for things such as lawyers and investment bankers on our transactions.

Q60 **Mr Clarke:** Who provides those professional services if they are not contractors?

Mark Russell: They are all contractors.

Q61 **Mr Clarke:** Without exception?

Mark Russell: Yes.

Q62 **Mr Clarke:** Interesting. Rushanara touched on the Future Boards Scheme, which is a very important and positive initiative, and the Committee is holding an inquiry into women in finance at the moment, which is something we are keen to promote. Can you give us an update on UKGI's involvement in that scheme, and specifically whether you feel you could be doing anything more to encourage female participation on boards?

Mark Russell: The Future Boards Scheme was something we started with in the Shareholder Executive. It came out of an observation that a few of us, and me in particular, had made. We have this issue on the boards of companies where it is quite difficult to get non-executive work until you have done non-executive work. That is a gender-neutral point. Most people find that. But, in my observation, women had a particular issue trying to get on to boards. If you spoke to women who were trying to find non-executive work, they said the No. 1 issue when they went to head-hunters was they did not have the experience.

We thought that a potential way of breaking that was to devise a scheme to get women on to boards without them necessarily becoming directors or appointed as directors. We did not want to use the observer status name; we wanted them to fully participate. Because they were not directors, they would not make decisions but they would be parts of boards, experiencing the discussion and contributing to the discussion. The acid test would be: after that year, or maybe a little longer, would that get them into a position where they could then say to the head-hunter, "I have had experience"?

Q63 **Mr Clarke:** Have you tracked that?

Mark Russell: Have we cracked it?

Mr Clarke: No, tracked.

Mark Russell: We have not cracked it, but we have tracked it. At the moment, it is modest. I think I am right in saying that we have had six or seven instances where we have put women on to boards. I think two or three have been able to go on and get board seats. I am satisfied with the proof of concept, but some organisations are a bit resistant to it. It is another person in the boardroom. When they understand the benefits of it, I am hoping it will grow.

That was Women on Boards, a scheme that was run by the Shareholder Executive. We recognised that we were not really geared up to develop that, so we sold the idea, as it were, to the Future Boards Scheme, which is administered by the 30% Club and Board Apprentice. They are now taking over the administration of this. We are still involved and of course we are promoting the idea within our organisations. I would not want to overblow it, but it is a very practical way of breaking the cycle, because you need practical ways.

Q64 **Mr Clarke:** Thank you very much for that. My final question is about pensions. Staff who have been recruited to UKGI since April 2016 have not been enrolled in the Civil Service pension scheme, as I understand. I just want to understand whether you are concerned about the fact that you therefore have staff on two sets of schemes. What is the rationale for that?

Mark Russell: It is general Government policy, particularly when new organisations like UKGI are set up, that they should be set up without the benefit of the Civil Service pension scheme, potentially compensating them with a higher base salary, which is what we do within UKGI. That is a general Government policy.

Does it create an anomaly? Yes, it does. Is it helpful? No, it is not helpful. We have to have some sort of parity, and we try to have some sort of parity, recognising that employees who have TUPE'd over from the Civil Service might have a lower base salary but have a better Civil Service pension. We try to balance it that way. At the same time, we try to fulfil Government policy.

Q65 **Chair:** Mr Russell, I would like to tidy up one little anomaly on your website, or Network Rail's. You list a Michael Harrison as a member of the Network Rail board. Network Rail does not and he, in his LinkedIn profile, describes himself as a board observer.

Mark Russell: That is right. When I described him as a board member, that was wrong.

Chair: Your website might need to reflect that. In your letter, Mr Russell, it would be helpful if you could outline in writing to the Committee how you are using your leverage on the gender pay gap with the various organisations that you are working alongside. The full Committee, in its work, would find that useful.

Finally, Mr Leigh-Pemberton, I am sure that nothing will knock you off course with what you are doing. However, should there be a major shock to the system, either if Brexit is far more positive or far more negative than people seem to expect, which changes the market significantly, or if the court case ends up being a total disaster in terms of your work, it would be useful if the Treasury Committee heard about your change of strategy directly in a note from you, rather than picking it up from the media or politicians' statements in the House, which I am sure there would be. It may not be needed, but that would be appropriate, should a major change of strategy be required in your view and that of your colleagues. Other than that, thank you very much for your attendance.