National Audit Office

Report
by the Comptroller
and Auditor General

HM Revenue & Customs

Managing the HMRC estate

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HM Revenue & Customs

Managing the HMRC estate

Report by the Comptroller and Auditor General

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Comptroller and Auditor General
National Audit Office

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This report examines whether HM Revenue & Customs is well placed to deliver its new estates model, which meets its changing operational needs.

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Key facts

£269m
total running cost of the HMRC estate in 2015-16

30%
reduction in HMRC's annual estate running costs since 2010-11

£83m
expected reduction (31%) in annual running cost of HMRC's estate by 2025, compared with its current estate

£3.2bn	HMRC's latest estimate of its estate costs over the next 10 years
£588m	HMRC's forecast investment in its new estate
137	HMRC's offices planned to close by 2021
38,000	employees will need to move offices to regional centres, or leave HMRC
27%	reduction in the size of HMRC's estate since 2010-11
£354m	total savings achieved on its estate between 2010-11 and 2015-16
15 m^2	average space per person in HMRC's estate in March 2015 as outlined in HMRC's strategic outline case for its new estate strategy
8 m^2	target for average office space per person in the government estate by March 2018

Summary

1 HM Revenue & Customs (HMRC) has a strategy to redesign and significantly reduce its estate over the next 10 years. It plans to move from a current estate of 170 offices to 13 large regional centres, supplemented by four specialist sites and a headquarters in central London.

2 As of November 2016, HMRC had nearly 1 million square metres of buildings. It spends around £269 million each year running its estate to accommodate its 58,600 staff. It sublets 15% of its estate to other government departments.

3 HMRC has been reducing the size of its estate for six years. Across its whole estate, it has moved out of almost 300 buildings and cut its estate by 27%, reducing its annual running costs by £102 million and saving a total of £354 million since 2010-11.

4 HMRC has achieved more than half of this reduction by moving out of excess space under the terms of its STEPS (Strategic Transfer of Estate to the Private Sector) contract. STEPS is a 20-year private finance initiative (PFI) deal set up in 2001 with Mapeley STEPS Contractor Ltd (Mapeley). Under the deal, HMRC sold its freehold properties, which comprised two-thirds of its estate, to Mapeley for £370 million. HMRC immediately leased back the properties from Mapeley, with Mapeley providing facilities management and maintenance services. As HMRC has reduced its workforce over this period, it has moved out of some of these buildings each year. The remaining third of HMRC's current estate is managed under smaller PFI deals and individual leases with landlords.

5 We reported on HMRC's management of the STEPS contract in 2004 and 2009.[1] In our 2004 report, we identified significant risks with STEPS that HMRC needed to manage carefully. In 2009, we found that HMRC had not been managing those risks effectively, and it had not realised the benefits available from the contract. In particular, HMRC had not made all the savings possible by moving out of as many buildings as the contract allowed. We recommended that HMRC should have full access to Mapeley's financial data to give it a better understanding of Mapeley's profitability and that it should negotiate more effectively to achieve better outcomes through the contract.

1 Comptroller and Auditor General, *HM Revenue & Customs' estate private finance deal eight years on*, Session 2009-10, HC 30, National Audit Office, December 2009; and Comptroller and Auditor General, *PFI: the STEPS deal*, Session 2003-04, HC 530, National Audit Office, May 2004.

6 HMRC's strategic business case identifies three main reasons why it is seeking to move from a widely dispersed estate to regional centres:

- it considers a different estate is necessary to support the wider transformation of its business. It sees regional centres as offering the right infrastructure and working environment to enable new digital ways of working for its customers and staff;
- HMRC's programme will support the wider civil service agenda to move to shared government hubs, supported by a regional network of mini-hubs; and
- the end of the STEPS contract in 2021 provides an imperative for HMRC to act and an opportunity to reconfigure its estate on a large scale.

7 HMRC's programme to rationalise its estate is one of 15 major programmes it is implementing concurrently to transform how it operates and administers tax. It aims to become "one of the most digitally advanced tax administrations in the world". HMRC's transformation is large and complex, and many of the programmes within it are interdependent. **Figure 1** shows the strategic aims of HMRC's transformation programme and how the plans for its estate support its wider objectives.

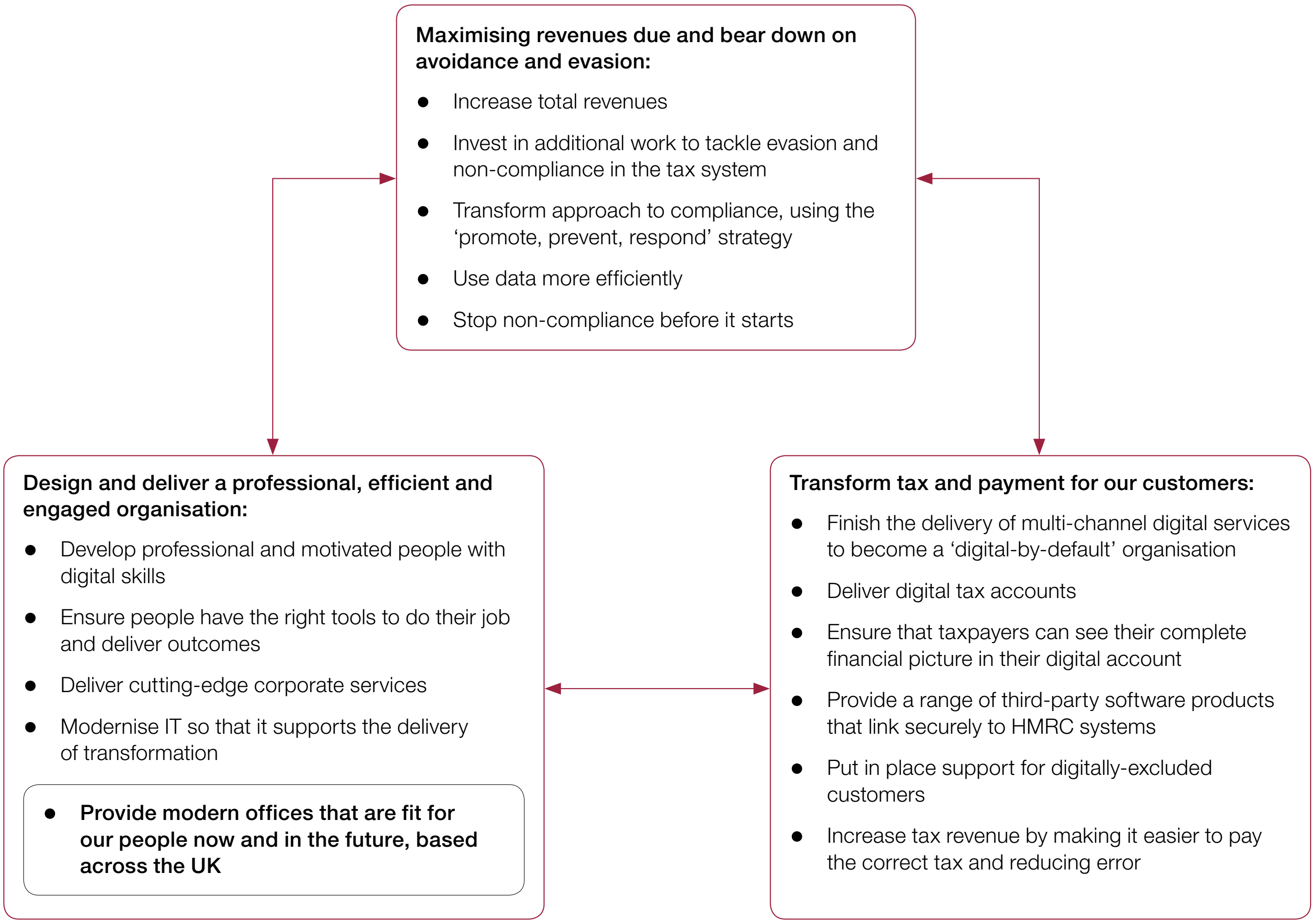
8 This report takes an early look at HMRC's plans for its new estate and the actions it is taking to implement them. First, we consider the strength of the strategic case for HMRC to move to regional centres. We then evaluate how well HMRC has managed the STEPS contract since our last report in 2009 and how effectively it is preparing for the end of the contract in 2021. Finally, we look at early indicators of the challenges HMRC faces in implementing its strategy and identify some of the risks it has to manage over the next five years.

Key findings

On the strategic case for the move to regional centres

9 HMRC has concluded that moving to regional centres will provide the flexibility necessary to modernise and transform the way it works. HMRC has more space than it needs and much of it is in poor condition, which HMRC considers reduces morale and productivity. It has assessed that large regional centres will help it work more efficiently and flexibly with fewer staff, supporting collaboration, knowledge sharing and economies of scale. They should also give its employees more career options and help it to recruit high-quality graduates with the skills HMRC will need to change the tax system to a primarily digital service. HMRC's plans for regional centres are therefore integral to its strategic aims to increase tax revenue by bearing down on tax evasion and avoidance and to transform the service it provides to its customers (paragraphs 1.5 to 1.9, 1.14, and Figures 2 and 3).

Figure 1
HMRC's strategic aims and transformation



Source: National Audit Office analysis of HM Revenue & Customs' single departmental plan 2015–2020

10 **HMRC has assessed that the move to regional centres will mean substantially lower running costs in the long term.** While HMRC has reduced the size and cost of its estate over the last six years, the scale of the changes it could make has been limited by the terms of its long-running STEPS contract with Mapeley, which expires in 2021. In its November 2015 strategic outline case for moving to regional centres, HMRC estimated that it would continue to make savings over the next eight years as it leaves most of its existing buildings. Beyond 2024-25, it estimated it would achieve a sustainable reduction of between £80 and £100 million in the annual cost of holding and maintaining its estate (paragraphs 1.15 to 1.18, 2.11 to 2.13 and Figure 4).

11 **HMRC has designed its strategy to support government's objectives to create government hubs that will be shared by government departments.** The government intends to modernise and rationalise the estate occupied by central government departments by moving civil servants to shared government hubs, allowing departments to collaborate more effectively and achieve economies of scale. The timing of HMRC's plans, created by its imperative to take decisive action before the end of the STEPS contract, place it in the vanguard of government's proposed move to shared hubs. It is working with the Government Property Unit (GPU) to ensure its new centres align with the locations chosen for cross-government hubs and meet the expected design standards (paragraphs 1.11 and 1.12).

On the management and the end of the STEPS contract

12 **HMRC's ability to achieve the outcomes it wants from its estate has been impaired by the STEPS contract.** Our 2009 report on the STEPS deal identified features of the contract which reduced its value for money, including the actions necessary for HMRC to understand the risks it would face should the contract end prematurely. HMRC has assessed that Mapeley's performance under the contract has fluctuated since then: while it had recovered from a low point in 2013-14, Mapeley's performance in 2014-15 remained below the quality standards HMRC had set. HMRC's payments to Mapeley for facilities management were reduced by just under £700,000 to compensate for Mapeley's underperformance in that year. This equates to around 2% of what HMRC pays to Mapeley annually for this part of the contract (paragraphs 2.3, 2.4, 2.7 to 2.10 and Figure 5).

13 **HMRC's regional centres need to be up and running and its estate plans settled before the end of the STEPS contract in March 2021.** HMRC's business case identified that if it stayed in STEPS properties beyond 2021, its rental and service costs would increase. Its aim is to occupy regional centres before this happens, and it has sought to make decisions about its choice of locations early in order to negotiate with Mapeley about the time frame for leaving existing buildings. Its aim to occupy regional centres quickly has meant in some locations having to balance the need to achieve timely occupancy against cost and quality (paragraphs 1.15, 2.14 and 2.17).

14 **HMRC has significantly improved its management of the STEPS contract, achieving cumulative savings of £354 million since 2011.** It has responded to the recommendations of the NAO and the Committee of Public Accounts by using almost all of the allowances within the contract to move out of buildings. It has closed 160 buildings managed under the contract, and reduced the annual cost of the contract by £54 million (paragraphs 2.11 to 2.13 and Figure 6).

15 HMRC has also improved its working relationship with Mapeley and achieved a better understanding of the performance of the contract. In 2009, the NAO found that HMRC did not have full visibility under the contract of Mapeley's gains and losses, particularly on renegotiated leases that may ultimately affect its liabilities in the event of contractor default. The Committee of Public Accounts recommended that HMRC should insist that Mapeley provides much greater transparency about the financial performance of the contract and its profitability. Since 2010-11, HMRC has had open access to Mapeley's books, giving it a good understanding of the operational and financial performance of the contract (paragraphs 2.4 to 2.6, and Figure 12).

16 HMRC continues to manage the risk of the STEPS contract ending prematurely. We reported in 2009 that Mapeley's finances would continue to be finely balanced for the foreseeable future and profits would remain low for the lifetime of the contract. HMRC has continued to monitor and manage the risk to Mapeley's financial health since then, and has established a team to oversee the period until the end of the contract. Should the contract not run until 2021, some buildings within the STEPS estate would revert to HMRC's ownership and responsibility, potentially leaving HMRC with properties in poor condition that it no longer needs. In these circumstances, HMRC would be faced with the costs of maintaining and improving buildings it does not intend to stay in long term, and would need to manage the disposal of properties which might not have a ready market (paragraphs 2.16 to 2.20).

Early indicators of the risks and challenges HMRC faces in implementing its strategy

17 HMRC's original plan has proved unrealistic. During the transition to regional centres, HMRC must ensure that its service to taxpayers and its ability to collect tax revenue are not impaired. It has concluded that suitable property will not be available in some of its chosen locations within the time frame set out in its 2015 spending review settlement. HMRC now estimates it may lose up to 5,000 staff as a result of the move to regional centres. It will therefore need to recruit to its new centres and train new staff, while managing redundancies and the moves of existing employees and operations into new buildings. It has concluded that its original plans were over-optimistic about the availability of suitable properties and carried too high a risk of disruption to its business, as they involved moving or replacing too many staff too quickly, while delivering other major change programmes in parallel (paragraphs 3.7, 3.8, 3.14 and 3.15).

18 HMRC is reconsidering the scope and timing of its moves to some regional centres to reduce costs and delivery risks over the next five years. Since its spending review settlement in November 2015, HMRC's estimate of its estate costs over the next 10 years has risen by nearly £600 million (22%), more than half of which is due to higher than anticipated running costs for its new buildings. It has also identified that slippage in the timetable for some regional centres had led to an unmanageable peak of activity scheduled for 2019-20. HMRC is considering the actions necessary to reduce this peak and stay within the funding it has secured between now and 2020-21. It tells us that it will reach this decision shortly. (paragraphs 3.4 to 3.6 and Figure 8).

19 HMRC has reduced its estimate of the benefits of the programme and now expects them to come later. As some of the moves to regional centres will now happen later than HMRC had planned, it will be longer until HMRC starts to realise savings. In the long term, it still expects its new estate to reduce its running costs. It now estimates cumulative efficiency savings by 2025-26 of £212 million, reduced from the £499 million estimated in its strategic outline case in November 2015. By 2025-26, HMRC expects its annual running costs to be £83 million lower than they are now (paragraphs 3.12 and 3.13).

20 Changes to reduce costs and delivery risk could diminish the long-term value of the strategy. HMRC is now considering actions to reduce the costs and the risks of disruption over the next four years. It is looking at a range of options, including: changing the timetable for opening and filling regional centres; reconsidering the functionality, location and size of individual units to determine the best mix of staff to undertake some work; adding a transitional site in East London to ease the disruption in the South East; changing where to focus its recruitment effort; and reassessing how and when to introduce flexible ways of working. HMRC must manage the risk that such changes compromise its objectives to improve the engagement, morale and productivity of its workforce while achieving sustainable savings in the cost of running its estate in the long run (paragraphs 3.7 to 3.11).

21 HMRC has yet to define fully how regional centres will support better customer service and more efficient and effective compliance activities. HMRC has signed the contract for its first regional centre in Croydon, but faces a demanding timetable to occupy the site as it plans in 2017. HMRC's move to regional centres will require good coordination across HMRC to ensure that everyone involved in the moves understands what is expected of them. It must therefore clarify what changes in working practices are necessary to support digital services and its future compliance model, and coordinate its design of regional centres to achieve these outcomes (paragraphs 1.9, 1.10 and 3.19 to 3.22).

22 **HMRC must manage the risk that it locks itself into long-term property deals which limit its flexibility to change its future business model.** HMRC is now implementing its third major change programme since the merger of the Inland Revenue and HM Customs and Excise in 2004. While the move to regional centres is consistent with its wider transformation plans, it should not assume that the business model it designs now will remain its optimal state indefinitely. HMRC therefore needs to weigh the cost of property deals against the benefits of having the flexibility to make future changes. It has not negotiated any break points in the 25 year leases it has signed so far for regional centres in Croydon and Bristol. HMRC aims to provide flexibility through a mix of lease terms across the estate, maintaining the ability to sublet to other parts of government, and by working with the GPU to provide for future flexibility in the design of cross-government hubs (paragraphs 3.26 and 3.27).

23 **HMRC's decisions and what it learns from the relocations are critical to the success of the government's plans to reconfigure its estate.** HMRC's decisions about the buildings it will occupy will affect the choices other departments will have. It is early days in implementing HMRC's move to regional centres, but important that HMRC takes stock of what it learns over the next few years, both to optimise its own decision-making and to inform the plans of the GPU and other government departments (paragraph 1.14).

Conclusion on value for money

24 It is important to see HMRC's estate strategy in two ways. First as a major programme in its own right, and second, as a component in HMRC's wider business transformation. From the standpoint of the estate strategy itself we can conclude that the handling of HMRC's STEPS contract has improved, and is more likely to deliver value for money though significant risks remain. As far as the new programme is concerned, HMRC has already recognised that its original plan was unrealistic and it is considering how it can adjust the scope and timing of the programme to reduce the cost and delivery risk. It is, of course, better management practice to recognise cost underestimates early and to consider options for recovery early as well. However, we think it important for HMRC to step back and consider the benefits afforded by the wider business transformation, and whether they might be reduced or placed at risk by cutting back on, or delaying, the estate plans, before going ahead.

Recommendations

25 HMRC is seeking to implement an ambitious estate strategy alongside 14 other major programmes designed to transform the way it administers the tax system. Many of these programmes are interdependent. It is inevitable that not every aspect of the transition to regional centres will run smoothly and HMRC must learn as it goes and respond proactively as issues arise. It should:

a Improve its control of the costs of the new regional centres. HMRC needs to be realistic in re-forecasting costs and guard against optimism bias. Given the inherent uncertainty in the property market, it should plan for the worst case rather than risk basing its plans on optimistic assumptions. It should put in place an adequate contingency for the programme of regional centres as a whole to make it resilient to emerging cost increases.

b Plan in detail how the infrastructure it is putting in place through regional centres will support the ways of working its business aspires to. HMRC has yet to demonstrate how in practice the regional centres will help its employees provide a better service to customers while increasing the efficiency and effectiveness of its compliance work. It should prioritise engagement with its business to identify what features of the new estate will be most important to support working practices that will deliver the outcomes it is seeking.

c Put in place a process to learn lessons by analysing the costs and benefits of occupying and operating regional centres. HMRC should be clear how it will establish whether it is achieving the benefits it expects from its regional centres once they become operational, and at what cost. It should identify and apply good practice from its occupation of the Croydon regional centre in 2017, and evaluate how its forecasts of the timetable, costs and benefits were affected by events. It should build a framework to compare the performance of the regional centres by identifying each centre's annual running costs, service levels and business outcomes.

d Build in flexibility to respond to future changes in technology and working practices. In negotiating property deals for the regional centres, it must therefore balance cost considerations against the benefits of retaining flexibility to make future changes to its estate.

Part One

HMRC's rationale for its estate strategy

1.1 As at November 2016, HMRC has over 200 properties spread across the United Kingdom. Of these, 170 are office buildings but it has 40 properties of other types, including garages, storage facilities, car parks and kennels. In 2015-16, it spent £269 million on accommodating its 58,600 full-time equivalent employees, amounting to 8% of its total running costs.

1.2 In 2001, HMRC sold its freehold properties, which formed two-thirds of its estate, to Mapeley STEPS Contractor Ltd (Mapeley) for £370 million. This was part of a 20-year private finance initiative contract known as STEPS (Strategic Transfer of Estate to the Private Sector). HMRC immediately leased back the properties from Mapeley, with Mapeley providing facilities management and maintenance services. The remaining third of HMRC's estate is managed under smaller private finance initiative deals, and smaller individual leases with landlords. HMRC also acts as the landlord for other government departments, by subletting vacant office space. Its total estate covers 994,000 m^2 in floor area, of which 842,000 m^2 is used by HMRC staff or operations.

1.3 In November 2015, HMRC set out its vision for a future estate. HMRC intends to establish 13 new regional centres across the United Kingdom, supplemented by four specialist sites. In the process, it will close 137 existing offices by 2021, keeping some offices temporarily as transitional sites. It intends to retain a small headquarters on Parliament Street in central London.

1.4 This part looks at how HMRC's estate strategy was formulated, including how it is designed to support HMRC's organisation-wide programme to transform its business and to align with wider plans to reconfigure the whole of the government estate.

HMRC's strategic case for reconfiguring its estate

1.5 HMRC developed its plan to move to regional centres as part of an integrated strategic programme of change, which is one the largest organisational change programmes in Europe. It has identified three main reasons why it is seeking to move from a widely dispersed estate to regional centres:

- it considers a different estate is necessary to support the wider transformation of its business;
- HMRC's programme will support the wider civil service agenda to move to a network of shared government hubs; and
- the end of the STEPS contract in 2021 provides an imperative for HMRC to act and an opportunity to reconfigure its estate on a large scale.

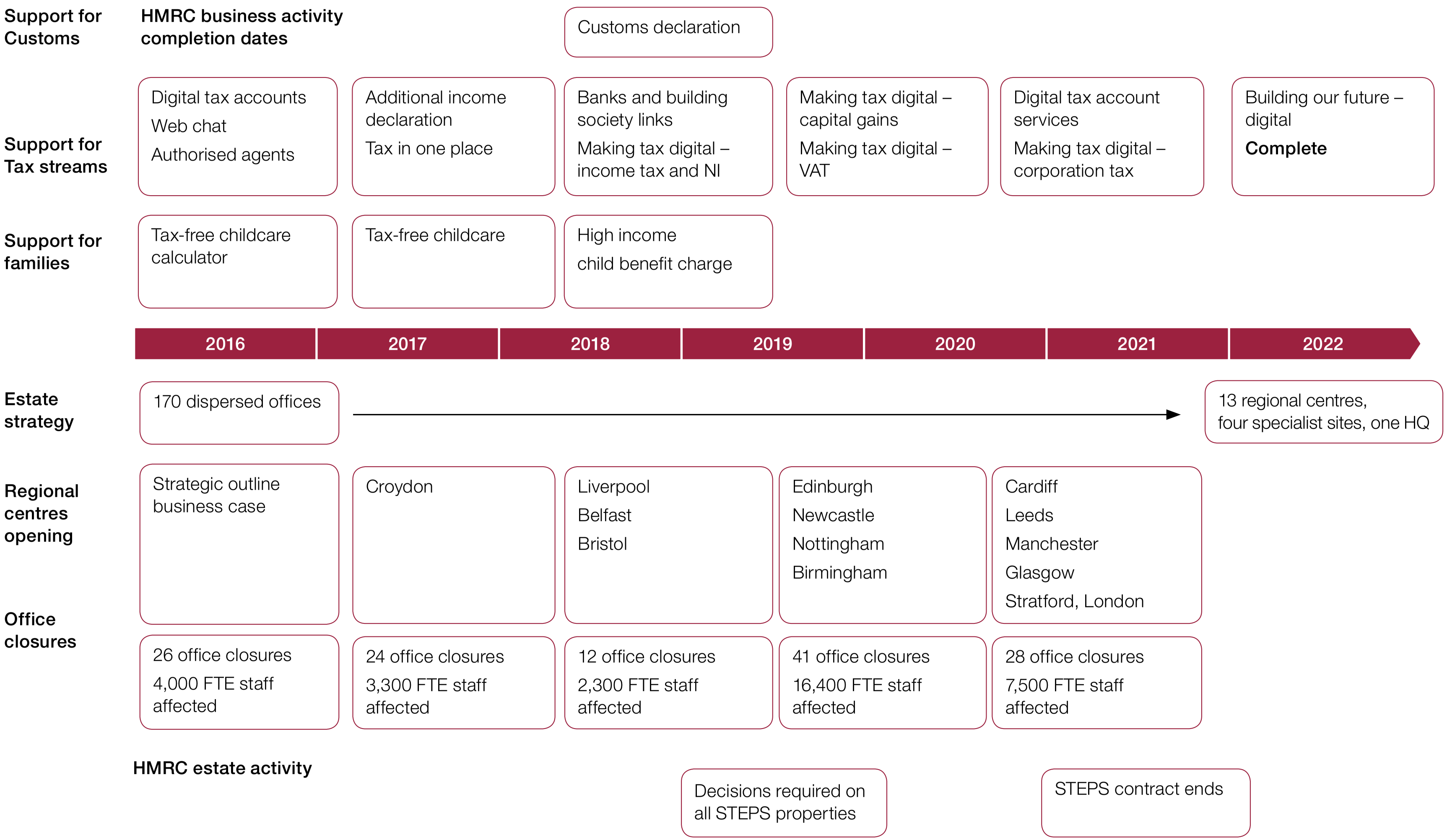
Supporting the wider transformation of HMRC

1.6 HMRC's programme to rationalise its estate is one of 15 major programmes it is implementing concurrently to transform how it operates and administers tax. It aims to become "one of the most digitally advanced tax administrations in the world". HMRC's transformation is large and complex, and many of the programmes within it are interdependent. For example, HMRC's programme to move to regional centres is closely aligned to its programme to create a more engaged and professional workforce with the capability to operate a tax system which relies on the digital services and the better use and analysis of data. Its plan for 13 regional centres aims to provide modern offices, suited to automated systems and digital working. **Figure 2** shows the activity that HMRC will undertake over the next few years as it moves to its new ways of working.

1.7 HMRC sees regional centres as offering the right infrastructure to enable new digital ways of working for its customers and staff, and a working environment that will attract and retain talent, increase the flexibility of its workforce and provide economies of scale. **Figure 3** on pages 16 and 17 shows the location of HMRC's offices before and after the moves and summarises how HMRC believes the new estate will improve its business. **Figure 4** on page 18 shows the main principles HMRC has set to guide the development of regional centres.

Figure 2

HMRC's business and estate activities 2016–2022



Notes

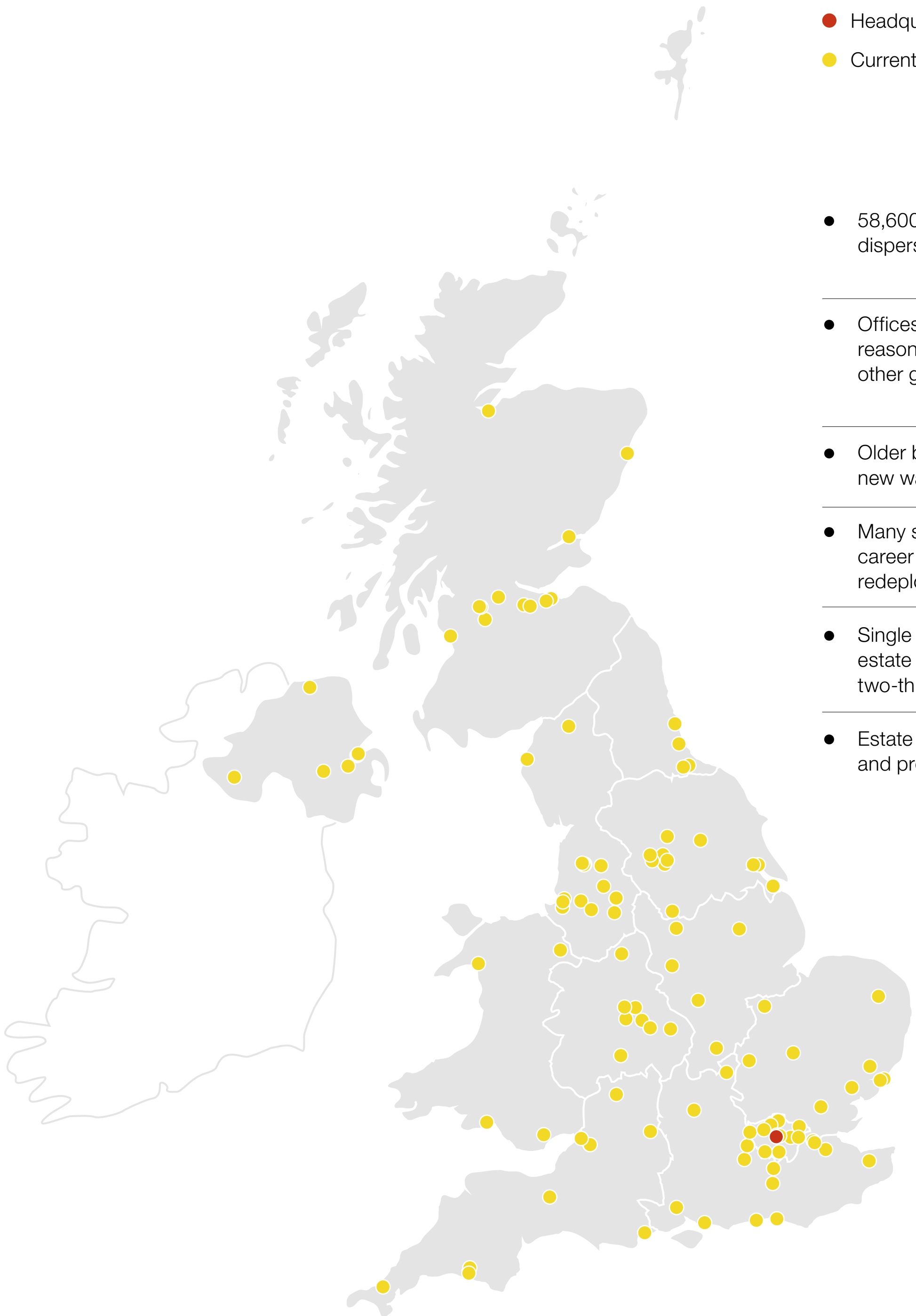
1 For business activities the date shown is the completion date for each programme, taken from HMRC's single departmental plan, 2015–2020.

2 For regional centres we show the opening date for each regional centre, taken from the strategic outline business case, revised September 2016.

3 Office closure dates taken from most recent public announcement of November 2015, combined with HMRC data on office FTEs.

Source: National Audit Office analysis of HM Revenue & Customs' transformation documentation

Figure 3
How HMRC is transforming its estate



Current position – 170 offices

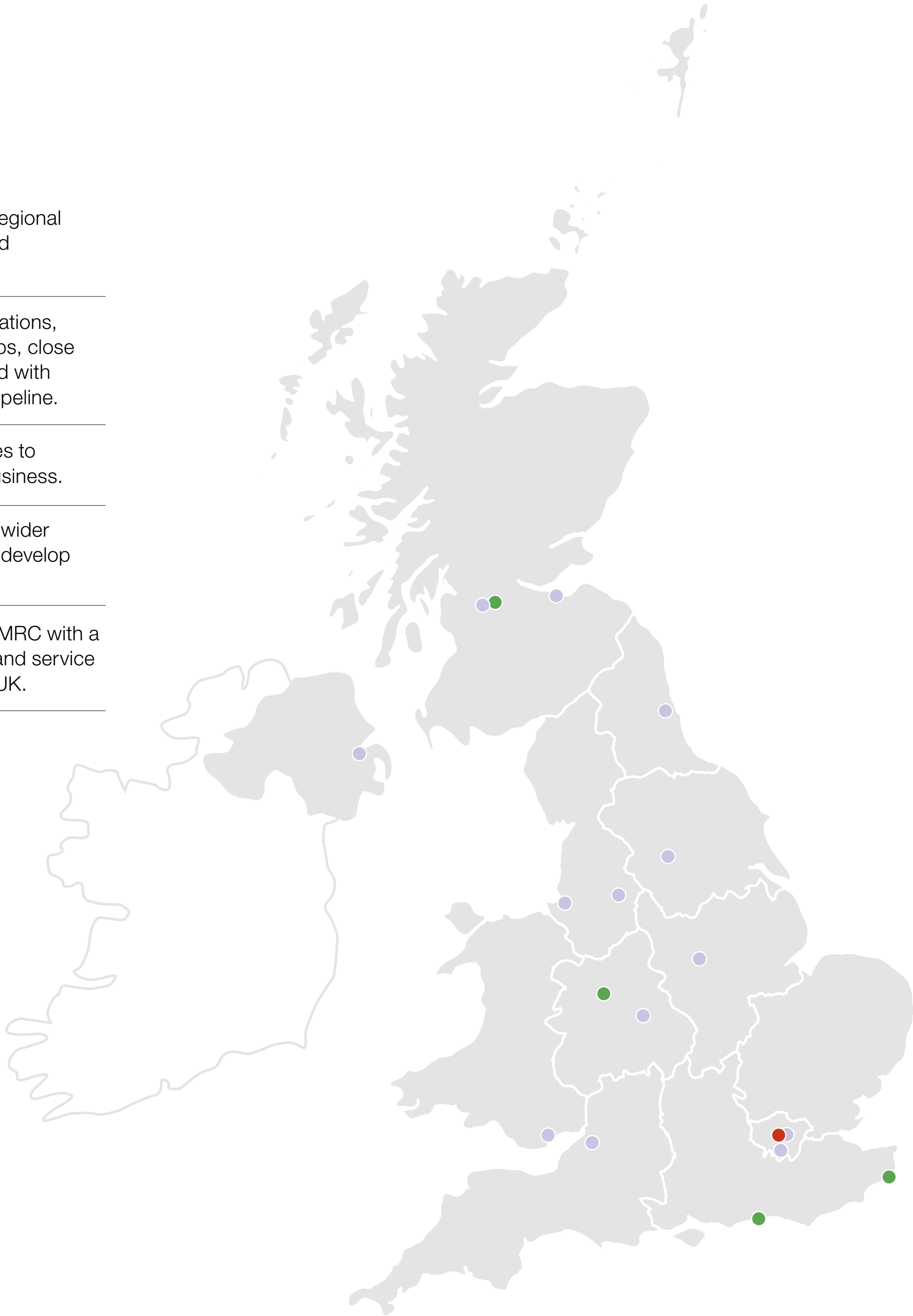
- Headquarters
- Current office

- 58,600 employees in 170 offices, dispersed across the UK.
- Offices in locations for historical reasons, sometimes isolated from other government departments.
- Older buildings, unable to adapt to new ways of working.
- Many small buildings with limited career opportunities or flexibility to redeploy staff.
- Single large PFI contract covering estate and facilities management in two-thirds of HMRC's properties.
- Estate reduces staff morale and productivity.

Source: National Audit Office analysis

Future position – regional centres and specialist sites

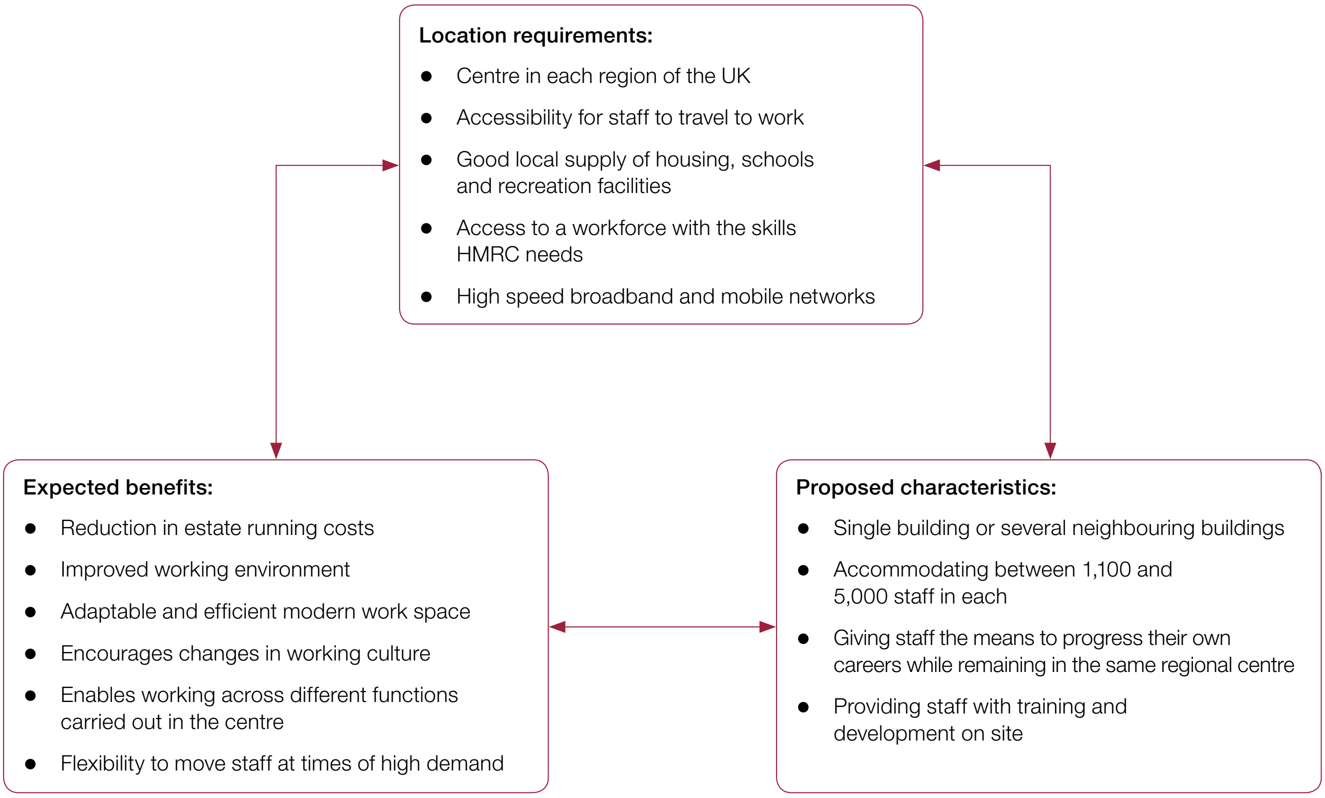
- Headquarters
- Regional centre
- Specialist site



- 50,000 employees in 13 large regional centres, four specialist sites and one headquarters.
- Offices based in city centre locations, forming part of government hubs, close to universities and colleges, and with stronger skill base and talent pipeline.
- Modern, flexible regional centres to support HMRC transformed business.
- Large regional centres offering wider opportunities for employees to develop their careers.
- Estate managed primarily by HMRC with a number of separate contracts and service providers in three areas of the UK.
- Estate supports a professional, efficient and engaged organisation.

Figure 4

HMRC's principles for its regional centres



Source: National Audit Office analysis of HM Revenue & Customs' strategic outline business case

1.8 An important feature of regional centres is that they should enable HMRC to work in ways which will serve customers better and increase the efficiency and effectiveness of its work to prevent and deter tax evasion and avoidance.

1.9 In moving to digital services, HMRC aims to serve its customers primarily online, supported by other channels which will offer taxpayers the additional help and advice they may need. These include its needs enhanced services, providing additional support for those that find using digital channels challenging. It closed its face-to-face enquiry centres in 2014 and is promoting the take-up of self-service, including by providing every taxpayer with a digital tax account, much of which HMRC aims to pre-populate with accurate, personalised data. It has assessed that a local presence in a high proportion of towns across the United Kingdom is not necessary to provide such a service, and that the co-location of customer service operations in large regional centres will help it to serve its customers more effectively.

1.10 The customer compliance group has assessed that basing its teams in regional centres will help the sharing of knowledge between employees with different areas of expertise and improve its understanding of how tax risks apply to different population groups. It also considers that bringing staff together in regional centres will present opportunities to improve team management, and enable staff to have a greater range of work, gain wider experience, and have greater opportunity for career development. It expects to more than offset the deterrence effect of a permanent physical presence in many localities by a more mobile and skilled workforce with better access to the intelligence needed to target its compliance activities in the right areas.

Supporting the creation of government hubs for the wider government estate

1.11 In 2014, the government set out its strategy to use government office space more efficiently and to dispose of surplus property. The Government Property Unit (GPU), which leads and coordinates the management of the government estate, aims to reduce the number of office buildings by 75% (80% in London) by 2025. It intends to establish large, flexible, cross-government hubs across the United Kingdom, in key locations with good transport links. It intends that in the long term these will have around 6m^2 of office space per full-time equivalent member of staff. The GPU has assessed that shared government hubs will enable departments, agencies and local bodies to work more collaboratively, and their staff to work flexibly. It also expects that these hubs will attract and retain skilled staff.

1.12 HMRC's strategy for a new estate of regional centres is closely aligned to the GPU's proposals for government hubs. The locations which HMRC selected for its regional centres match the GPU's proposed locations for hubs. In these hubs, HMRC aims to share space, services and facilities with other departments, agencies and local bodies. HMRC's strategy for regional centres also intends that this will give its staff opportunities to work across the government departments in these hubs, providing more job and career development opportunities. The GPU has yet to announce the detail of its plans and chosen locations, but it is likely to have a greater number of centres than HMRC's plan for 13 regional centres.

1.13 HMRC intends to have an estates service headquarters in Nottingham, plus a small service in each of its locations. It is not yet clear how HMRC is aligning its plans to manage the regional centres' estate itself with the GPU's intention to centralise the ownership and management of the public estate within the new property model.

1.14 HMRC's decisions and what it learns from the relocations are critical to the success of the government's plans to reconfigure its estate. The timing of HMRC's plans, created by its imperative to take decisive action before the end of the STEPS contract, place it in the vanguard of government's proposed move to shared government hubs. This means HMRC's decisions about the buildings it will occupy will affect the choices other departments will make. It is early days in implementing HMRC's move to regional centres, but important that HMRC takes stock of what it learns over the next few years, both to optimise its own decision-making and to inform the plans of the GPU and other government departments.

Opportunities to reconfigure its estate

1.15 HMRC has recognised and acted early on the opportunity to deliver a new estate to support the transformation of HMRC. It considers that a large, long-term outsourced contract such as STEPS is no longer the best way to provide the estate it needs, and no longer aligns with wider government objectives. It is committed to leaving the STEPS contract when it ends in 2021, but must give notice to its PFI provider by 31 March 2019 of its intentions for each building. This places additional pressure on HMRC to make decisions quickly. HMRC will have to negotiate new rental agreements for any properties it retains after expiry of the STEPS contract. It has assessed that if it were to sign new leases, it would see an increase in rental costs and service contracts.

1.16 HMRC also outlined that its estate is too large and it has a poor utilisation rate with staff working in the wrong place and with a demand for additional space in more strategic locations. Its strategic outline case stated it had a total of 15 m^2 of office space per full-time equivalent member of staff, compared with the government's target of 8 m^2 by 2018.[2] HMRC considers that much of its estate is in poor condition, and that this affects staff morale and productivity. HMRC also believes that its estate already creates operational issues and that it does not give it the flexibility it needs to transform the way it works.

2 This figure includes all HMRC property and is the figure HMRC quotes in its strategic outline cases of November 2015 and September 2016. Its Government Property Unit benchmark result is 9.8 m^2 per full-time equivalent having excluded non-office space and offices already set for vacation.

1.17 HMRC initially expected that regional centres would save £405 million over the period 2016-17 to 2024-25 and that the programme would see a payback period of, at most, 11 years when compared with what it currently pays under its current estate contracts. HMRC estimated that running costs in its new estate, covering leases, facilities management and utilities, would save between £80 million and £100 million each year after 2025.

1.18 The basis for HMRC's strategy was a financial model to forecast the cost of setting up and running a new estate, and the savings or benefits generated by closing its existing estate. HMRC designed the model to run scenarios around the future size of its estate, and dates and development options, to forecasts costs for each option. This included a 'do nothing' option, which estimated the estate costs that HMRC would incur, through to the expiry of the STEPS contract in 2021.

1.19 HMRC also used the forecast cost as a basis for considering whether its concept of regional centres was affordable. However, HMRC did not define 'affordability', and did not set a maximum amount that it was willing to spend on its new estate.

1.20 HMRC's financial model aimed to forecast the cost for each regional centre, based on costs that would be specific to each region (for example rental costs), and those costs which it thought would be constant across each option (for example, the costs per square metre of facilities management, cleaning and security). HMRC obtained estimates of the costs of these services from property experts. It analysed information on the commercial property market in each region, provided by external property analysts, and validated the information internally.

1.21 The model indicated significant differences in the cost forecasts between each region, with London the most expensive, and Northern Ireland the cheapest. HMRC acknowledges that in its initial planning, it could have done more to apply these differences in forecast costs per region to direct common work to the lowest cost regions. HMRC is now considering this option as part of its measures to control cost increases.

HMRC's strategic outline case for regional centres

1.22 The strategic outline case provided a broad statement of HMRC's intended business outcomes and benefits from regional centres, as outlined in Figure 4. It included a 'benefits logic map', which aimed to link outputs and benefits to its strategic objectives. The risk assessments in the strategic outline case were optimistic, both in terms of the severity of the risks and of their mitigation. HM Treasury's approval process for HMRC's estate programme highlighted affordability constraints in the strategic outline case. The strategic outline case was based on location specific advice from HMRC's property advisor but without direct consultation with developers. HMRC had not defined some of the benefits at that time, or how they related to different stakeholders. The strategic outline case did not set out expected performance outcomes or a plan for realising the benefits from regional centres. It also did not feature a critical path for moving to regional centres.

Part Two

HMRC's management of the STEPS contract

2.1 HMRC manages two-thirds of its estate through a single private finance initiative (PFI) known as STEPS (Strategic Transfer of Estate to the Private Sector). The remaining third of HMRC's current estate is managed under smaller PFI deals and individual leases with landlords.

2.2 STEPS is a 20-year deal set up in 2001 with Mapeley STEPS Contractor Ltd (Mapeley). Under the deal, HMRC sold its freehold properties, which comprised two-thirds of its estate, to Mapeley for £370 million. HMRC immediately leased back the properties from Mapeley, with Mapeley providing facilities management and maintenance services. As HMRC has reduced its workforce over this period, it has moved out of some of these buildings each year. This part looks at HMRC's management of its STEPS contract since our last report and how it is preparing for the end of the contract in 2021.

HMRC's response to previous recommendations by the NAO and Committee of Public Accounts

2.3 We reported on the STEPS contract in 2004 and 2009.[3] In our 2004 report, we identified significant risks with STEPS that HMRC needed to manage carefully. In 2009, we found that HMRC had not been managing those risks effectively, and it had not realised all the benefits available from the contract. In particular, HMRC had not made all the savings possible by moving out of as many buildings as the contract allowed. We also found that HMRC did not have full visibility under the contract of Mapeley's gains and losses, particularly on renegotiated leases that may ultimately affect its liabilities in the event of contractor default.

2.4 We recommended in our 2009 report that HMRC should strengthen its management of the contract and that senior managers should work directly with Mapeley's board to resolve issues, agree strategies and manage risks. Having taken evidence on our report from HMRC and Mapeley, the Committee of Public Accounts recommended that HMRC should insist on much greater transparency about the financial performance of the contract and its profitability to Mapeley.

3 Comptroller and Auditor General, *HM Revenue & Customs' estate private finance deal eight years on*, Session 2009-10, HC 30, National Audit Office, December 2009; and Comptroller and Auditor General, *PFI: the STEPS deal*, Session 2003-04, HC 530, National Audit Office, May 2004.

2.5 HMRC has responded positively to the recommendations of the NAO and the Committee of Public Accounts (Appendix Three). HMRC now employs a specialist team which oversees the contract and will do so for the remainder of its time. In 2011, HMRC and Mapeley signed a memorandum of understanding to recognise HMRC's need for financial transparency and Mapeley's need to know about HMRC's future plans. Both Mapeley and HMRC told us that they have since had a good working relationship and are open and honest with each other about performance, and future plans and requirements.

2.6 Since 2011, Mapeley has given HMRC access to a range of financial information relating to the STEPS contract and the financial health of the company. This includes management accounts, financial forecasts, loans and inter-company funding. This enhanced access has provided HMRC with much greater transparency about Mapeley's ability to meet its obligations to HMRC under the STEPS contract, helping HMRC to understand and manage risks to the delivery of services.

Evaluating Mapeley's performance

2.7 HMRC pays Mapeley approximately £12 million each month. In return, Mapeley provides HMRC with the right to occupy the fully-serviced office accommodation under the STEPS contract. Mapeley provides day-to-day facilities management and estate maintenance. HMRC monitors the whole life cost of the project as a measure of value for money. Its latest estimates suggest that the whole life cost of the contract will be £4.2 billion.[4] This is £213 million more than it originally forecast. The increase is due to higher inflation than forecast, payments for additional buildings which were not part of the original contract, and legacy settlement charges, which were not included in the original financial model. HMRC has improved its control of the costs of the contract since 2009, primarily by making use of the allowances within it for leaving buildings.

2.8 Each year, HMRC assesses the STEPS contract against 13 qualitative performance measures covering three areas: the contract's ability to support HMRC's transformation; the quality of the working environment; and Mapeley's management of the contract (**Figure 5**). Performance against most of these criteria has not fully met HMRC's requirements. HMRC assessed that the worst-performing area was the maintenance of required accommodation standards.

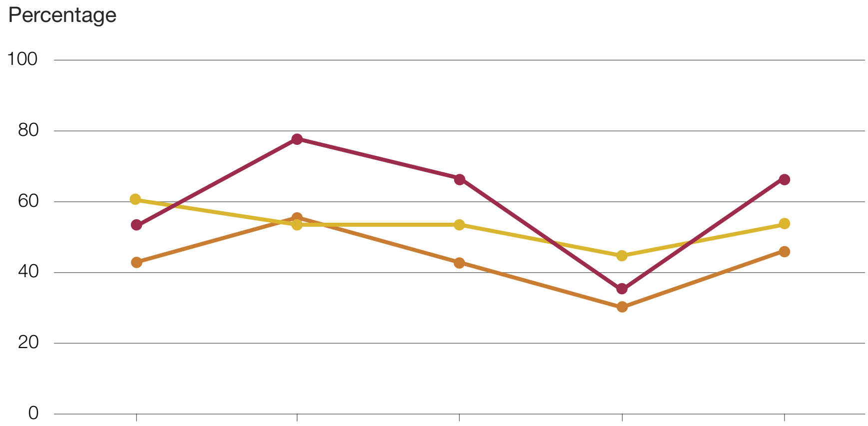
2.9 Performance deteriorated across a range of measures in 2013-14. HMRC was critical of Mapeley's failure to manage the performance of subcontractors, due to shortcomings in the way Mapeley sought to bring more of its facilities management services in-house. HMRC took action to address the areas of concern with Mapeley, such as by developing systems to monitor progress, setting improvement targets and using appropriate contract measures. In it's most recent report covering 2014-15, HMRC has assessed that Mapeley's performance under the contract has improved. However, Mapeley's performance in 2014-15 remained below the quality standards HMRC had set out in its invitation to tender.

4 Based on HMRC's most recently available value-for-money report, covering the reporting year 2014-15. The 2015-16 report was not available at the time of publication.

Figure 5

HMRC's assessment of the performance of the STEPS contract against qualitative performance measures

Mapeley's performance has not fully met HMRC's requirements



	2011	2012	2013	2014	2015
Mapeley's Management of the contract	53	78	67	35	67
Quality of the working environment	61	54	54	45	54
Ability to support departmental transformation	43	56	43	30	46

HMRC uses 13 qualitative measures to measure the performance of the STEPS contract. Each measure is scored from zero to three depending on how well performance meets HMRC's requirements. It is weighted on the measure's importance in reaching HMRC's strategic goals. The 13 measures are –

Ability to support departmental transformation:

- ability to support HMRC estate strategy;
- provision of new facilities; and
- management of change.

Quality of the working environment:

- maintenance of required accommodation standards;
- health and safety service;
- utilities and environmental service;
- securities services; and
- provision of cleaning and catering services.

Mapeley's management of the contract:

- management of services and properties portfolio;
- management information systems and communication with HMRC;
- availability, performance measurement system and incentives;
- designated contact point (helpdesk) and additional services; and
- performance-driven organisational and management structure.

Source: Analysis of HMRC's internal assessment of performance of the STEPS contract as outlined in HMRC's value-for-money reports

2.10 The contract allows for HMRC to deduct some payments from Mapeley if Mapeley does not meet contractual requirements. In 2014-15, HMRC's payments to Mapeley for facilities management were reduced by just under £700,000 for Mapeley's underperformance in that year. This equates to around 2% of what HMRC pays to Mapeley annually for this part of the contract and 0.5% of the total annual contract value.

Vacating unwanted space

2.11 The STEPS contract gave HMRC flexibility to move out of properties during the contract at no additional cost. The pace at which HMRC can do this is determined by the annual allowances agreed in the contract. In our 2009 report on the STEPS contract, we reported that HMRC had not taken full advantage of all the flexibility available to it.[5] We found that, by March 2009, HMRC had saved £52 million from moving out of STEPS properties, compared with the potential £151 million it could have saved had it used its allowance at the earliest opportunity. HMRC responded to recommendations and developed a building-by-building closure plan.

2.12 In 2011-12, HMRC used up the allowances it had accumulated from previous years. It has since used almost 100% of the available allowance on 'core' buildings, and 85% of the allowance it had built up to vacate 'flexible' buildings (**Figure 6**).[6]

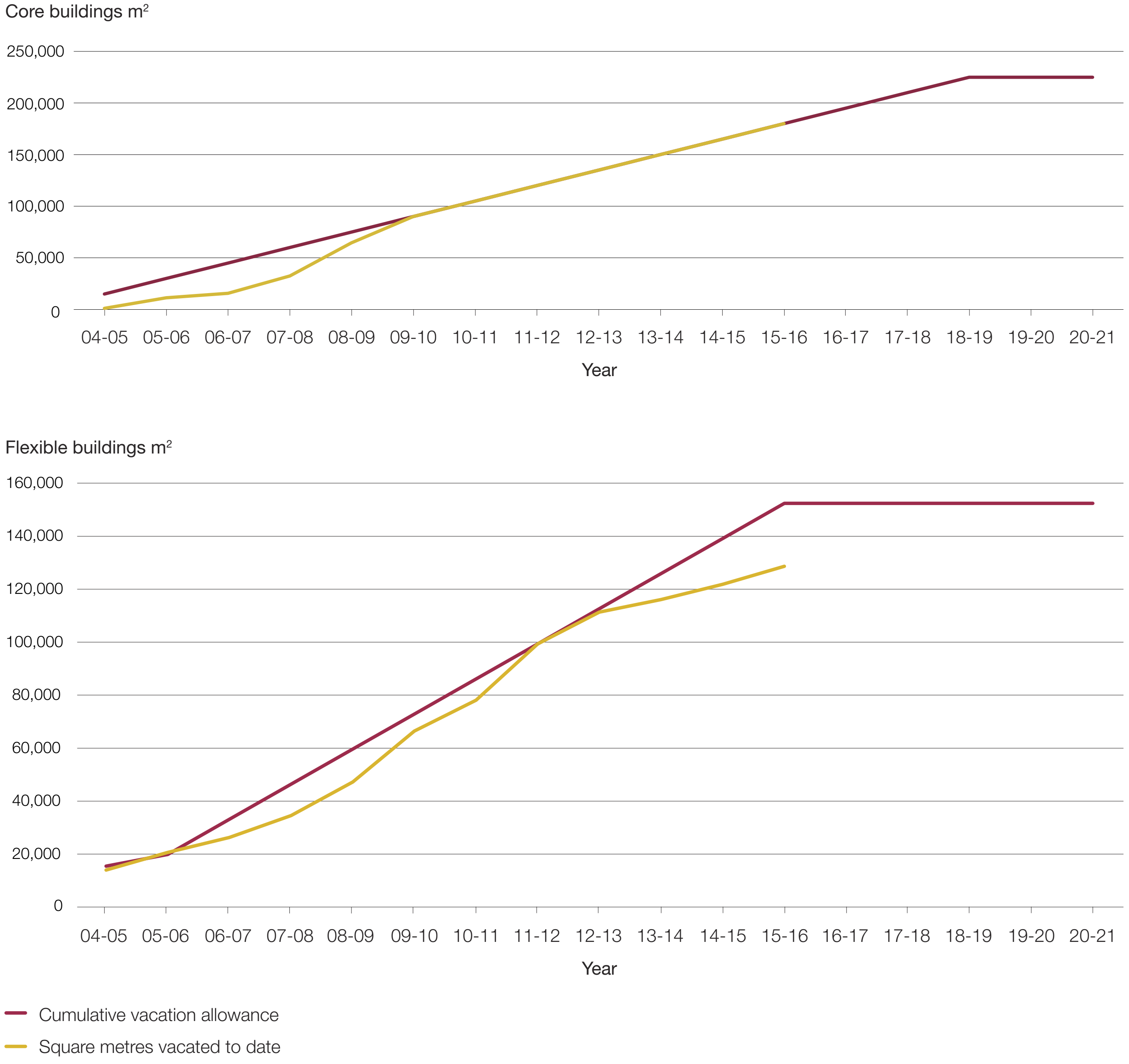
2.13 Since 2009, better use of the flexibility in the STEPS contract has enabled HMRC to vacate buildings and realise its estate savings targets. Between 2011 and 2016, HMRC vacated nearly 300 properties in total, of which 169 were managed by Mapeley under the STEPS contract. Of these 100 properties were enquiry centres. These were walk-in centres providing face-to-face help with tax queries, which HMRC closed in 2014 following a period of falling demand. HMRC achieved cumulative savings in the cost of its estate of £354 million in this period, reducing its annual running costs by 30% to £269 million. Its total floor area decreased by a similar proportion from 1.4 million to 994,000 m^2.

5 Comptroller and Auditor General, *HM Revenue & Customs' estate private finance deal eight years on*, Session 2009-10, HC 30, National Audit Office, December 2009.

6 Core buildings are those that HMRC expected to need for the full 20 years. Flexible buildings are buildings that HMRC expects to vacate at some point during the 20-year contract. Intermediate buildings are those that have specified dates that HMRC can vacate at the earliest at no additional cost.

Figure 6
Utilisation of vacation allowance within STEPS

HMRC has used up almost all the allowances available on its STEPS contract to vacate buildings



Source: National Audit Office analysis

Preparing for the end of the STEPS contract

2.14 HMRC recognises the challenges and risks involved in moving out of its current buildings. HMRC and Mapeley are jointly planning for the expiry of the STEPS contract and both parties recognise the importance of openness about their plans in the remaining few years of the contract. They have developed a joint strategy for buildings under the STEPS contract. This strategy aims to provide benefits for both organisations and to ensure that Mapeley has sufficient incentives to continue the partnership until 2021. HMRC and Mapeley both told us that they want the contract to run to full term in 2021.

2.15 The two organisations have held joint workshops to discuss each of the existing buildings in the estate. These workshops have considered the lease type and terms for each building and HMRC's expected occupancy needs. They have helped Mapeley to understand which buildings HMRC plans to vacate and when, and to consider the implications for its future management of each property.

Managing future risks and liabilities

2.16 HMRC is still developing its plans for its future estate and, where it can, it aims to occupy regional centres before the STEPS contract ends in March 2021. But HMRC recognises it may need to remain in some buildings managed under the STEPS contract beyond 2021. If it changes the timeline for regional centres, HMRC may need to remain in a larger number of buildings than its plans so far have implied. HMRC recognises that the terms of contracts for those sites will need to be renegotiated, and that in most cases it will require shorter-term leases with early break points.

2.17 HMRC's strategic case for regional centres estimated that if it stayed in STEPS properties beyond 2021, it would see an increase in its rental and service costs. Its aim to occupy regional centres before this happens has meant in some locations having to balance the need to achieve timely occupancy against cost and quality.

2.18 HMRC has identified a number of risks for the remaining years of the STEPS contract. These include: non-compliance with legislation or regulations; instability of the supply chain; lack of life cycle investment; failure to meet service delivery targets; and failure to meet avoidable waste targets.

2.19 We reported in 2009 that Mapeley's finances would continue to be finely balanced for the foreseeable future and profits would remain low for the lifetime of the contract.[7] HMRC has continued to monitor and manage these risks on the contract closely since then. Should the STEPS contract come to a premature end, buildings within the STEPS estate would revert to HMRC's ownership. In these circumstances, HMRC would be faced with the costs of maintaining and improving buildings it does not intend to stay in, and would need to manage the disposal of properties which might not have a ready market. HMRC has taken action to manage this risk, putting a specific team in place to oversee the period to the end of its PFI arrangements.

2.20 HMRC has engaged external experts to assess how large its financial commitments could be following any sudden loss of services under the STEPS contract. HMRC has developed business continuity plans to manage the risks of loss of services under the contract. Its plans aim to ensure that the estates services can continue to support HMRC overall. If any estates related service should be lost, HMRC has defined the procedures to follow to restore the service and communicated these to relevant staff. HMRC has assessed the likely scenarios that could affect estates services and day-to-day operations, as part of developing its responses.

7 Comptroller and Auditor General, *HM Revenue & Customs' estate private finance deal eight years on*, Session 2009-10, HC 30, National Audit Office, December 2009.

Part Three

Early indicators of the risks and challenges HMRC faces in implementing its strategy

3.1 This part examines HMRC's progress to date in implementing its strategy and the risks and challenges it faces. It is early days in implementing the strategy. We have therefore looked at what HMRC has learned from its experience of developing its plans and cost estimates over the last 18 months in the context of a programme that will take 10 years to complete.

HMRC's arrangements for overseeing the development and delivery of the programme

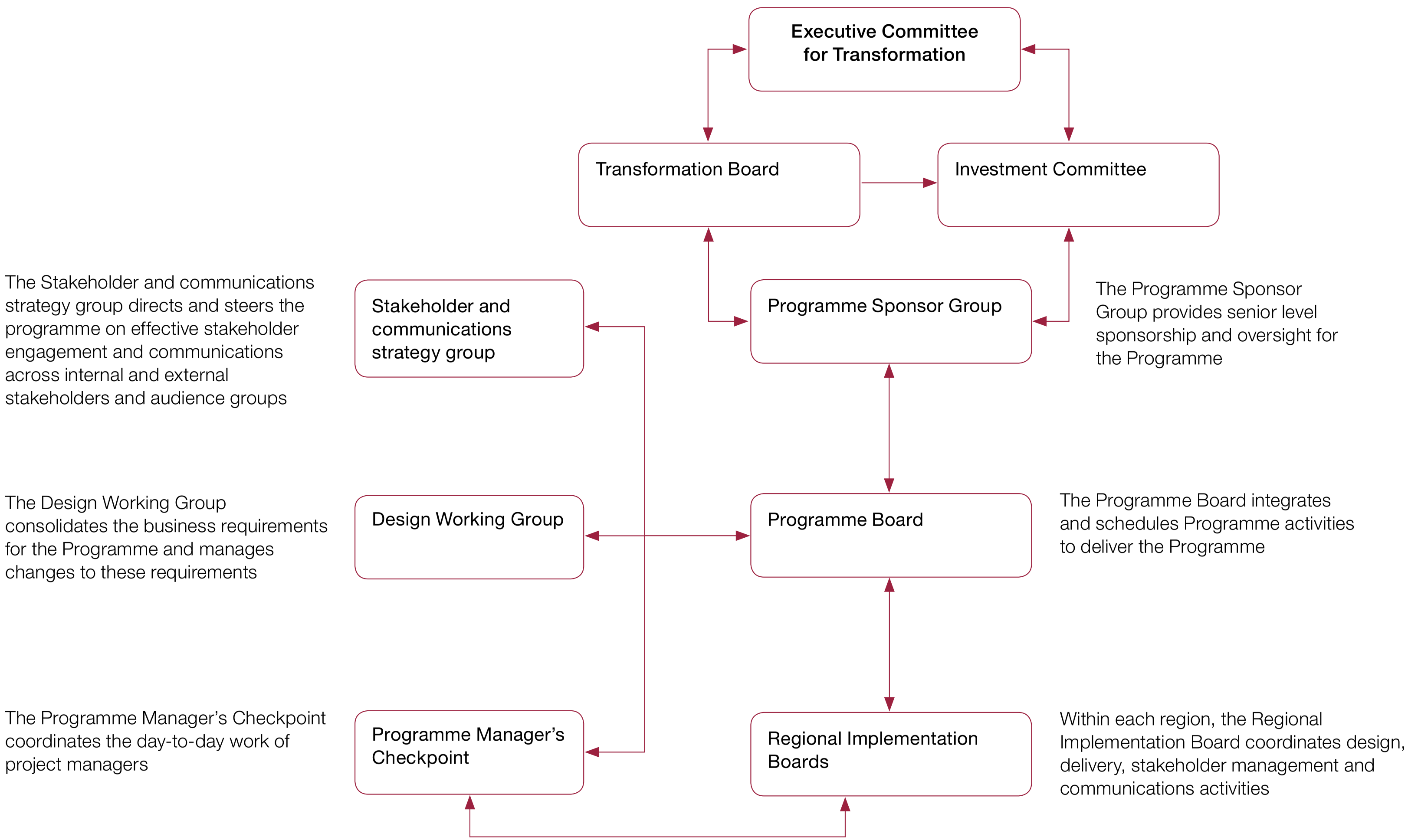
3.2 HMRC has put in place a clear governance structure to oversee the programme to transform its estate (**Figure 7**):

- The **executive committee** is made up of the most senior managers across the whole of HMRC's business and oversees delivery of HMRC's entire transformation programme, including its estate strategy.
- The **investment committee** makes investment decisions on behalf of the executive committee. It has scrutinised the initial and revised strategic outline case for the new estate and the outline business cases for individual regional centres.
- The **locations programme board** considered the strategic case for HMRC's new estate and continues to make recommendations about how the programme should develop. It considers emerging risks, affordability and timing, and proposed changes to the programme and its forecast costs and benefits. The board includes membership from HM Treasury, the Government Property Unit (GPU) and the Infrastructure and Projects Authority.

3.3 We have seen evidence that the programme board, investment committee and executive committee have provided robust challenge to the proposals put before them. Each group has recognised that the estates programme faces pressures on its budget, timetable and to business disruption and have asked for more analysis and the consideration of wider options where they have considered this necessary. As a result of such challenge, HMRC does not yet have an agreed programme business case.

Figure 7

HMRC's framework for governance and control of the estates programme



Source: National Audit Office analysis

Actions HMRC is considering to address emerging cost increases and delivery risks

3.4 HMRC does not yet have an agreed strategic outline case. It is developing its plans to reduce the risk of disruption to its business and reduce the costs over the next five years. HMRC's executive committee has said that the original strategic outline case, on the basis of which HM Treasury agreed funding in late 2015, was unrealistic. In September 2016, HMRC updated its strategic outline case with a revised forecast of the costs and timeline of the programme. The total cost of the new estate over 10 years (including investment and running costs) rose by almost £600 million (an increase of 22%). The revised business case forecast investment costs of £495 million between 2016-17 to 2020-21, with additional spending beyond 2021, bringing total investment costs to £588 million by 2025-26. HMRC had previously forecast no investment costs beyond 2020-21. It estimated that the average annual running cost of the new estate over these 10 years would be £160 million, a 27% increase in HMRC's original estimate. In the longer term, its forecast for annual running costs has increased from around £150 million to £180 million per year.

3.5 The increase in the forecast costs is largely due to: changes in programme scope, to include specialist and transitional sites; the requirement to bring pay costs into the programme; higher rental costs than anticipated; and increased allowances for exits and daily travel allowances. Having consulted the property market, HMRC concluded that suitable property would not be available in some of its chosen locations within the time frame set out in its 2015 spending review settlement. The revised business case also set out that the financial benefits HMRC had estimated from the new estate would be reduced by likely changes to the timetable for occupying regional centres, requiring HMRC to keep existing offices open for longer.

3.6 **Figure 8** shows how HMRC's forecast investment and running costs for its estate rose between November 2015 and September 2016. It also shows that HMRC now expects it will take 14 years to pay back its investment in the programme, against its original estimate of up to 11 years.

3.7 HMRC has also identified that changes to the timetable for regional centres meant that it had too much activity scheduled in the later years of the spending review period, in particular in 2019-20. It concluded that this would lead to an unacceptably high risk of disruption to its business, as it would be unable to serve its customers adequately while moving so many of its employees to new accommodation.

3.8 In September 2016, the Infrastructure and Projects Authority carried out an independent assurance review of HMRC's estate programme and reached similar assessments of the risks. At the time of the review, the programme received a low confidence rating, indicating that delivery of the programme is 'in doubt'. It said that HMRC had established the programme on a strong foundation of committed leadership, clear links to corporate plans and policies, and effective engagement with internal and external stakeholders. However, it also considered that HMRC had to move quickly, having encountered difficulties with schedules, costs and affordability.

Figure 8

HMRC's forecasts for the costs of its new estate have risen between November 2015 and September 2016

	Strategic outline case, November 2015 (SR15 bid)		Strategic outline case September 2016	
Area of expenditure	**5 year (£m)**	**10 year (£m)**	**5 year (£m)**	**10 year (£m)**
Investment costs	413	413	495	588
Of which:				
Estate investment	212	212	192	194
IT and digitisation	34	34	47	47
Daily travel allowance	17	17	19	54
Employee exits	149	149	165	203
Additional costs (eg pay bill and communications)	Not included	Not included	73	91
New accommodation running costs (total)	389	1,259	529	1,590
Legacy accommodation (total)	976	977	1,049	1,066
Total cost	**1,778**	**2,649**	**2,073**	**3,243**
Estate efficiencies (costs)	55	499	(127)	212
Payback period	At most 11 years		14 years	

Notes

1 Investment costs until 2021 have risen due to: changes in scope to include a new specialist site and a new transitional site (£22 million); the inclusion of the cost of the specialist team needed to run the programme (£27 million); an increase in the cumulative costs of digital and IT support, communications and business readiness activity (£14 million); and increases following property market consultation (£10 million).

2 In its November 2015 bid, HMRC did not expect or include investment costs beyond 2021.

Source: Analysis of HM Revenue & Customs' strategic outline business cases, November 2015 and September 2016

3.9 The review noted that HMRC was facing challenges in getting ready for the move to regional centres. This applies particularly to the Croydon regional centre, which HMRC is due to open in summer 2017. The review emphasised the need for good coordination across HMRC to ensure that everyone involved in the moves understood what was expected of them. It also asked HMRC to provide more clarity about what changes in working practices were required across its business and to coordinate its design of regional centres accordingly.

3.10 HMRC's executive committee has therefore been considering options to manage the risk of disruption to the business and to reduce the cost of the programme. These include:

- the timelines for opening and filling regional centres;
- reconsidering the functionality, location and size of individual units to determine the best mix of staff to undertake some work;
- the addition of an additional transitional site in East London to ease the disruption in the South East;
- where best to undertake new recruitment; and
- how best to deliver new flexible ways of working, including changes to working patterns for new recruits.

3.11 HMRC's executive committee has already agreed some proposals for reducing costs, but has sought further analysis of some of the options proposed in order to reduce further the risk of business disruption. The proposals which the executive committee has agreed so far would reduce the total spending on the estate by nearly £150 million up to 2020-21, but would defer some spending to a later date.[8]

3.12 If HMRC amends its timetable for opening regional centres, it will need to extend or renegotiate the leases on some of its current buildings, or move quickly to find new temporary accommodation. Such decisions would have cost implications and thereby defer the savings that the programme delivers. HMRC recognises that should it decide to change the size of some regional centres or move work to cheaper locations, potential savings may be offset if more employees leave HMRC, leading to potential loss of skills and capability. HMRC recognises that all of the measures it is considering carry a risk to the continuity of its business.

3.13 If regional centres open later than originally planned, it will be longer until HMRC starts to see savings from its new estate. In the long term, HMRC still expects its new estate to provide better value for money. In its updated strategic outline case of September 2016, HMRC estimated cumulative efficiency savings by 2025-26 of £212 million, reduced from £499 million when it produced its first outline case in November 2015. It expected to see a payback from its investment by 2029-30 and estimates a 25-year net present value of £430 million. HMRC expects its future estate to cost around £83 million less a year by 2025-26, compared to its current estates costs, and to be £86 million a year less from 2028-29.

8 The £150 million figure is an indicative estimate which should reduce total spending by 2020-21 from £2.073 billion to £1.925 billion.

Implications of the programme on HMRC's employees

3.14 As part of its initial planning for regional centres, HMRC carried out an assessment of the impact on its people. The assessments included the risks that it would lose experience and key skills in the move to regional centres, and that early departures could put pressure on remaining staff and disrupt HMRC's business. The assessments identified ways to manage these risks. Our analysis of relocations by other public sector bodies indicates that, in some cases more staff than anticipated chose to leave the organisation. The resultant loss of expertise can then have a negative impact on the organisations' capability.[9] The need to recruit and train new staff in the regional centres will increase the challenge to HMRC in managing the transition.

3.15 We estimate that around 38,000 staff currently work in offices scheduled to close. In its latest forecast, HMRC has increased its estimates of exit costs on the basis that around 5,000 of its employees may leave. To help as many staff as possible move to regional centres, it has also increased its estimate of the travel allowances it will pay. **Figure 9** overleaf shows the locations planned for the regional centres and the current offices linking to them.

3.16 The average distance between offices that HMRC is closing and its planned regional centres is 18 miles.[10] Most offices that HMRC is closing are within 50 miles by road of their respective regional centre, except for in the South West, the East and the South East, where HMRC's existing offices are more dispersed.[11] About 100 full-time equivalent staff are based in offices in the South West that are over 100 miles from Bristol regional centre. The longest distance between an HMRC office due to close and the nearest regional centre is 174 miles, from Redruth in Cornwall to Bristol regional centre. In Scotland, HMRC expects a high proportion of staff exits from its offices in Aberdeen, and to a lesser extent Dundee, as their work moves to Edinburgh regional centre.

3.17 By contrast, HMRC's offices in the East Midlands, North East, North West, Wales and Northern Ireland are more concentrated around the cities in which the future regional centres will be. In the North West, about two-thirds of existing staff are within five miles of either Liverpool or Manchester, the two regional centres in the region.

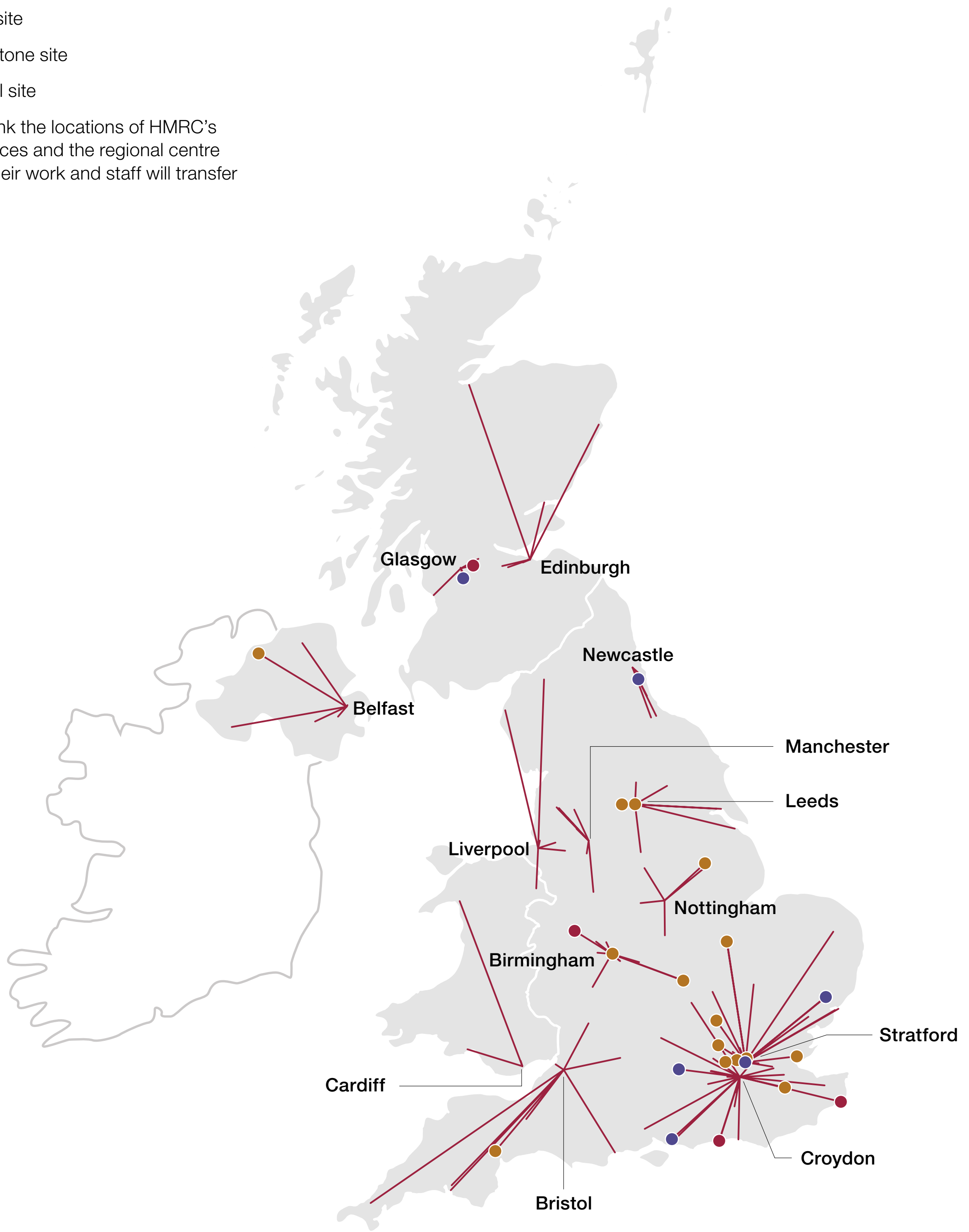
3.18 HMRC has sought to be open and transparent about its plans, consulting its employees at the outset and communicating from an early stage with all those affected about the potential implications. It gave details of the potential changes to their workplace and roles, future workplace(s), travel times and any compensation available to them (**Figure 10** on page 37).

9 Professor Sir Charles Bean, *Independent review of UK economic statistics*, March 2016.
10 This is calculated as the average driving distance from the current office to the city centre of the chosen locations, weighted by the number of full-time equivalent staff in each office.
11 We have used driving distance in our analysis, although HMRC expects staff to use public transport to get to work wherever possible.

Figure 9

HMRC regional centres and links to the current offices which will transfer work and staff to each regional centre

- Specialist site
- Stepping stone site
- Transitional site
- The lines link the locations of HMRC's current offices and the regional centre to which their work and staff will transfer



Source: National Audit Office analysis

Figure 10

Key features of HMRC's communications with staff on the regional estates strategy

Events and staff survey

HMRC began sharing plans for transforming its operations with staff in May 2014. In the first phase of communications, HMRC:

- held around 2,000 events, involving around 54,000 staff;
- carried out a survey, which produced 27,500 responses; and
- summarised the feedback received on its staff intranet.

One-to-one discussions with staff

HMRC has emphasised that it is not able to give staff certainty over the timings and nature of moves from their current workplace. HMRC managers are holding individual discussions with staff. These tell staff "what we know, when we know it", rather than make a commitment on future dates and locations, as it may change its plans and requirements. The one-to-one meetings between managers and staff may cover:

- whether they live within reasonable daily travel of a regional centre(s) and, if so, which regional centre is more suitable for them, based on their individual circumstances and convenience of travel;
- the intended year in which the regional centre(s) will open;
- the intended time at which the current offices will close;
- whether HMRC is considering redeploying the person into a new role as part of the moves and when this might happen;
- for staff who live outside of reasonable daily travel to a planned regional centre, the opportunity to say whether they would still like to travel to another office, or apply to leave under the voluntary exit scheme; and
- for staff who are not moving to a 'stepping stone' office or directly to a regional centre, where they will continue to be based and the office closure date.

Source: National Audit Office analysis

3.19 The changes HMRC is considering will inevitably increase uncertainty among some of its employees and have the potential to harm its relationship with them unless clear communications are maintained. In some cases, these changes could be significant, such as the possibility of moving in a different time frame. HMRC continues to work to minimise the potential of staff making more than one transitional move before moving to a regional centre. It is also now considering how it can bring forward its plans for flexible working, which might forego or defer some of the benefits it anticipates from bringing staff together in regional centres. HMRC is also reconsidering its requirements for its Croydon site, for which it may accelerate some moves. Some employees may therefore receive short notice of how the changes may affect them.

3.20 HMRC's move to regional centres will require good coordination across HMRC to ensure that everyone involved in the moves understands what is expected of them. It must therefore clarify what changes in working practices are necessary to support digital services and its future compliance model, and coordinate its design of regional centres to achieve these outcomes. In its strategic outline case of September 2016, HMRC stated that two of its key dependencies are that its lines of business deliver a clear set of requirements and have robust business readiness plans for the move. In some regions, the size of the regional centre is not aligned to the amount of work set out by the lines of business. It is not clear how this variation will be accommodated, or how it may affect operational performance in the process.

3.21 The review by the Infrastructure and Projects Authority also recommended that HMRC made changes to its working practices prior to the moves to regional centres. HMRC intends to move its first staff to its Croydon centre in Summer 2017, creating challenges in making these changes prior to the move. Both HMRC's lines of business and its estates team have significant work to do to achieve these changes.

3.22 The customer compliance group recognised that the move to regional centres involved risks in retaining its specialist and experienced staff, which may lead to disruption to its work and costs in replacing staff. Staff that will be recruited at the new regional centres may have lower initial performance and may take time to reach the productivity levels of more experienced staff.

Managing the regional centres' estate

3.23 HMRC has made progress in developing the leadership, management and commercial skills needed in the transition to regional centres. It has put together a team to focus on transforming its estate. The team includes external recruits, brought in to provide additional management capacity and capability on estates. HMRC will change the composition of this team to reflect the skills needed, as regional centres progress from planning to implementation and evaluation. The transformation team grew to around 40 people, reporting to HMRC's Director of Estates Transformation. HMRC also brought in additional external expertise, to provide information on local property markets, and to give advice on aspects such as commercial fit out of the new estate, to meet HMRC's operating needs.

3.24 HMRC has developed a future operating model for estates services to determine how it will run estates functions within regional centres. HMRC is using the model to develop its strategy for: facilities management; support services, such as security, health and safety and IT; and how it will manage contracts with suppliers. It is developing an understanding of the new skills the estates service will need to carry out these functions and the costs of the services.

3.25 In its new estate, HMRC expects to commission a mix of internal (to HMRC) and external facilities management providers for the regional centres, to achieve competitive prices. HMRC aims to use a range of providers and to include small companies. It will use the experience it gains in setting up and operating Croydon regional centre to commission and manage the others effectively and efficiently. It has estimated that the operating cost of Croydon regional centre for facilities management, rent, service charges, maintenance, rates, utilities, security, catering and insurance will be up to £14 million a year.

3.26 HMRC must also consider what its estate needs may be beyond its current transformation programme, and ensure it builds appropriate flexibility into its contracts to respond to future changes in service delivery or headcount. In general, longer-term leases with break options should be preferable to allow a degree of flexibility should HMRC make future changes to its business model.

3.27 So far, HMRC has agreed 25 year contracts for its regional centres in Croydon and Bristol without break clauses, which could tie the department to long term costs should its future operating model differ from its current plans. HMRC believes its property strategy addresses the need for flexibility by a balance of lease terms across the estate, the ability to sublet across government, and by working with the Government Hubs Programme to facilitate wider government flexibility. HMRC is also considering lease breaks where this is achievable while retaining value for money. In the case of its Bristol regional centre, HMRC believes a 25 year lease shows its long-te`rm commitment to stable jobs in the city and offers the best value for money. HMRC still needs to negotiate its remaining leases, and it must weigh the lower lease costs of making long-term commitments against the benefits of retaining the flexibility to allow for future changes to its business.

Appendix One

Our audit approach

1 In this report we examined whether HM Revenue & Customs (HMRC) is well placed to deliver its new estates model, which meets its changing operational needs. We reviewed:

- whether HMRC has a robust strategic case for moving to regional centres;
- how HMRC has managed the STEPS contract since 2009, including its response to the recommendations of the National Audit Office and Committee of Public Accounts, and its preparedness for the contract end in 2021; and
- whether HMRC is dealing effectively with the challenges in implementing its estate strategy and managing the risks.

2 We focused on HMRC's strategy and implementation plan for changes to its estate. We did not examine HMRC's overall transformation plans, or its approach to reducing employee numbers and updating staff skills sets.

3 We applied our analytical frameworks for strategic estates management and analysis of government business cases, to determine value for money.

4 We have summarised our audit approach in **Figure 11**. We describe our evidence base in Appendix Two.

Figure 11
Our audit approach

The objectives of HMRC

HMRC's key objectives are to: maximise revenues due and reduce avoidance and evasion; transform tax and payments for its customers; and design and deliver a professional, efficient and engaged organisation.

HMRC's objective is to have a future estate that will give staff an adaptable, efficient modern workspace, equipped with digital infrastructure and training facilities, to encourage greater staff openness and collaboration, and from which it can better serve its customers.

Its related objectives include reducing its estate costs and using its estate more efficiently, through reducing the overall size of its estate, the number of staff and the office space per full-time staff equivalent.

How this will be achieved

By 2021, HMRC will close 137 offices spread around the United Kingdom. It intends to accommodate around 95% of its staff in 13 new large regional centres. It will retain four specialist sites and its headquarters in Parliament Street, London. HMRC is communicating its estate strategy to its staff, holding one-to-one discussions with staff and offering to redeploy staff where necessary to different roles in the regional centres.

HMRC is also aiming to support the Government Property Unit's objective to establish cross-government hubs in England. It aims to achieve this by matching the cities for regional centres to government hubs.

Our study

We examined whether HMRC is well placed to deliver a new estate model that meets its changing operational needs.

Our evaluative criteria

HMRC has a robust strategic case for moving to regional centres.

HMRC has managed the STEPS contract well and is making effective preparations for the end of the STEPS contract in 2021.

HMRC is dealing effectively with the challenges in implementing its strategy and managing the risks.

Our evidence

(see Appendix Two for details)

- We used our analytical frameworks for strategic estates management, and analysis of business cases and commercial capability, to evaluate whether HMRC has a robust strategy to meet its future estate requirements.
- We interviewed officials at HMRC in the estates programme and in the Building our Future programme, across all parts of our examination.
- We interviewed officials in HMRC's customer compliance group on the wider impacts of the estate strategy.
- We interviewed representatives of Mapeley, which operates the STEPS contract for HMRC, to examine HMRC's planning, communications and transparency with Mapeley, for its exit from the STEPS contract.
- We analysed HMRC's estates data to determine the changes in the size and cost of its estate between 2010 and 2015, and whether it has achieved planned savings over this period.
- We analysed a wide range of documentary evidence, including: HMRC's annual STEPS value-for-money reports; Building our Future locations strategic outline business case (November 2015 and September 2016 versions); HMRC's financial model for its estate; and outline business cases for the first 10 of the 13 planned regional centres.
- We reviewed the Government Property Unit's proposals for cross-government hubs in England.

Our conclusions

It is important to see HMRC's estate strategy in two ways. First as a major programme in its own right, and second, as a component in HMRC's wider business transformation. From the standpoint of the estate strategy itself we can conclude that the handling of HMRC's STEPS contract has improved, and is more likely to deliver value for money though significant risks remain. As far as the new programme is concerned, HMRC has already recognised that its original plan was unrealistic and it is considering how it can adjust the scope and timing of the programme to reduce the cost and delivery risk. It is, of course, better management practice to recognise cost underestimates early and to consider options for recovery early as well. However, we think it important for HMRC to step back and consider the benefits afforded by the wider business transformation, and whether they might be reduced or placed at risk by cutting back on, or delaying, the estate plans, before going ahead.

Appendix Two

Our evidence base

1 Our independent conclusions on whether HM Revenue & Customs (HMRC) is well placed to deliver a new estate model, which meets its changing operational needs, were reached following our analysis of evidence collected between July and November 2016.

2 We examined whether HMRC had a robust strategic case for moving to regional centres. To do this, we examined:

- HMRC's strategic outline case for its future estate against our strategic estates management framework, covering:
  - vision and strategic planning;
  - collating and sharing information;
  - addressing financial barriers;
  - working together and aligning interests; and
  - skills and expertise.
- HMRC's financial model to generate estimates of the costs of options for regional centres, including the assumptions made, the external data sources and expert advice received, and its process for determining locations for regional centres.
- HMRC's November 2015 strategic outline case for the Building Our Future locations programme, against the structured review criteria as set out in HM Treasury's the *Green Book*:[12]
  - strategic case;
  - economic case;
  - commercial case;
  - financial case; and
  - management case.

12 HM Treasury, *The Green Book: Appraisal and evaluation in central government*, 2003.

- Whether HMRC's plans for regional centres align with the Government Property Unit's plans for government hubs, including the match between its selected locations for regional centres and the Government Property Unit's planned locations for government hubs.

3 **We examined whether HMRC has managed the STEPS contract well and is making effective preparations for the end of the STEPS contract in 2021.** To do this, we examined HMRC's responses to previous recommendations by the NAO and Committee of Public Accounts on its management of the STEPS contract and the changes it has put in place (Appendix Three).

4 We also examined how HMRC evaluates Mapeley's performance on the STEPS contract. This included the criteria against which it scores performance each year, and trends in Mapeley's performance against the requirements of the STEPS contract. We examined HMRC's actions in response to shortfalls in performance.

5 We reviewed HMRC's estates directorate's database on its estate and the data held on each property. We received and analysed data on the current estate from HMRC's estates directorate on:

- costs – total and types of estates costs;
- size – total, by lease type, by usage type, by location, by occupied/vacant, number of sites, variation in size across offices;
- estate profile and data on the characteristics of properties; and
- space utilisation and efficiency measures.

6 We also received and analysed time series data to examine HMRC's use of vacation allowances, estate-related targets and performance against targets:

- trends in key performance indicators (reductions in estate cost and size, reductions in number of offices, space per full-time equivalent (FTE) staff member, cost per FTE staff member, cost per m^2, reductions in staff and other activity metrics);
- reduction in estate size compared with reduction in HMRC FTE staff numbers over time; and
- the degree to which HMRC used opportunities in the STEPS contract to vacate properties without incurring penalties (percentage of allowances to vacate properties HMRC used).

7 We examined HMRC's preparedness for the expiry of its STEPS estate contract in 2021. We used our framework for commercial capability as a basis for our review. Within it, we examined:

- the actions HMRC has taken to implement recommendations from the Committee of Public Accounts in its 2009 report, covering HMRC's management of the STEPS contract with Mapeley;
- HMRC's planning for the exit from the STEPS contract;
- HMRC's timeline and arrangements for its office closures – this included how HMRC had identified options, gained an understanding of associated costs and how to manage these, developed processes to avoid and prevent delays and tested its readiness;
- the memorandum of understanding between HMRC and Mapeley, and their understanding, clarity and transparency on HMRC's early exit plans from property within its closure programme;
- how HMRC has developed the leadership, governance, management and commercial and contracting skills and capability necessary for its exit from the STEPS contract; and
- HMRC's approach to identifying, managing and mitigating end of contract financial and performance risks.

8 **We examined whether HMRC is dealing effectively with the challenges in implementing its strategy and managing the risks.** To do this, we examined:

- HMRC's framework for governance and control of the estates programme and the scrutiny and challenge provided;
- HMRC's management and commercial and contracting skills and capability for moving to a new estate model;
- updated forecasts of investment and revenue costs for the regional centres as estimated in the September 2016 strategic outline case and in the 10 outline business cases available to us, to understand the pressures on overall affordability of HMRC's estates programme;
- the updated forecasts of operational dates for the regional centres; and
- HMRC's approach to identifying, managing and mitigating the risks in moving to a new estate model.

9 We also examined the first 10 outline business cases for regional centres which HMRC had developed at the time of our fieldwork. We examined these against the structured review criteria:

- strategic case;
- economic case;
- commercial case;
- financial case; and
- management case.

10 We also examined the implications of the estates programme on HMRC employees. To do this, we examined HMRC's assessment of the impacts on its employees. We also reviewed its communications to staff over office closures, the moves to transitional sites and to new regional centres, and retraining and redeployment to new work areas. We examined the differing effect of office closures and moves to regional centres for HMRC staff across the United Kingdom, identifying the regional variations in distances between offices that will close and the regional centre to which work and staff will transfer.

11 We examined how HMRC's customer compliance group was managing the transition to regional centres. We interviewed customer compliance group managers to gain their views on the opportunities and risks associated with the transition to regional centres. This examined:

- maintaining performance and quality of service during the closure of offices and the relocation to regional centres;
- the changes to how customer compliance would operate based in regional centres, in 'Compliance for the future';
- the communications to customer compliance staff about the office closures and their scope to transfer to regional centres; and
- managing the risks of loss of staff expertise following the moves to regional centres.

12 We examined HMRC's plans for managing the new estate and controlling the revenue costs, including its proposals for a central estates directorate, plans for facilities management and support services, and approach to managing contracts with future suppliers.

13 We also examined the Infrastructure and Projects Authority's September 2016 independent assurance review of HMRC's estate programme.

Appendix Three

HMRC's response to recommendations by the Committee of Public Accounts (PAC), 2009

Figure 12

Recommendations by PAC and NAO and HMRC's actions

Value for money (VFM)

PAC recommendation	HMRC's actions
HRMC should develop cost and value-for-money targets for the remainder of the contract, measure its performance against these, and reflect the targets in its plan.	HMRC carries out annual VFM assessments of the STEPS contract, combining whole life costs and qualitative data.
NAO recommendations	**HMRC's actions**
HMRC should monitor the overall cost of the contract against initial models. HMRC should consider additional opportunities to achieve value for money.	HMRC updates the whole life cost of the contract annually and reconciles it with the original model. In 2011, HMRC successfully negotiated a reduction in overhead compensation payments of £12 million. HMRC monitors all gains on sales of vacated STEPS properties. HMRC appointed property experts to help it identify opportunities to increase the value of freehold buildings and therefore the share attributable to HMRC.

Understanding Mapeley's financial position

PAC recommendation	HMRC's actions
HMRC should understand and keep abreast of changes in Mapeley's financial position and the Department's potential liabilities in the event of Mapeley default. It should maintain an up-to-date business continuity plan. HMRC should understand and monitor [Mapeley] financial information, and use it to strengthen its management of the contract and negotiations. **NAO recommendations** HMRC should seek full access to Mapeley's financial information. HMRC should establish ongoing processes to assess Mapeley's financial position and profitability. HMRC should assess Mapeley's performance against qualitative measures. HMRC should seek independent assessment of Mapeley's viability. HMRC should assess potential liabilities and risks.	Mapeley discloses financial information to HMRC in accordance with HM Treasury guidance, through a memorandum of understanding, signed on 26 July 2011, which provides for the regular sharing of the estates strategy so far as it relates to STEPS properties. HMRC assesses the STEPS contract against 13 qualitative performance measures every quarter. HMRC uses a financial model to assess Mapeley's viability. HMRC discusses these results with Mapeley and agrees action plans to improve performance. HMRC has up-to-date business continuity plans and carries out work aimed at ensuring continuity in the event of service failure. In 2016, HMRC engaged external advisers to review the financial impact of service failure and assist HMRC in contingency planning. In 2013, HMRC developed models to calculate the likely costs to HMRC in the event of a STEPS failure.

HMRC's skills

PAC recommendation

HMRC should identify the commercial and legal skills it needs to achieve effective strategic and risk management, strong contract administration and good financial management. It should then appoint and deploy people with these skills over the remaining life of the contract.

HMRC's actions

HMRC engaged external advisers to assist in developing the financial model to assess Mapeley's viability.

HMRC carried out work to bring in the skills necessary for managing the contract.

Strategy and partnership with Mapeley

PAC recommendation

HMRC must establish an effective partnership with Mapeley, including: using joint board meetings for early and regular dialogue on strategy; sharing strategic aims, and establishing a shared property database.

NAO recommendations

HMRC should develop a joint annual estates strategy with Mapeley.

HMRC should develop a plan up to 2021 that details how it will make use of the allowances for vacating buildings.

HMRC's actions

HMRC's memorandum of understanding with Mapeley gave HMRC financial transparency and HMRC and Mapeley committed to work together, including developing a joint estate strategy.

In 2012, HMRC shared all actual and potential estate changes for Spending Review 2010 with Mapeley.

HMRC held joint workshops ('regional centre reviews') with Mapeley between June and August 2016 to review the impact of regional centres on the STEPS estate.

By 2011, HMRC had developed closure plans on a building-by-building basis up to 2014-15. It has used almost all the vacation allowances available to it under the contract since 2009.

In November 2015, HMRC announced the list of offices it plans to close up to 2027-28.

Mapeley's offshore status

PAC recommendation

HMRC should take whatever action it can to persuade Mapeley to bring the properties onshore. It should also reach agreement on including additional buildings in the contract.

HMRC should track the savings Mapeley actually obtains [from being based offshore] and Mapeley should provide full and timely information to enable the Department to do this. The Department should seek to recoup any additional benefits Mapeley obtains.

HMRC's actions

HMRC did not progress this recommendation.

HMRC and Mapeley did not agree terms for the inclusion of additional properties in the contract.

HMRC did not accept PAC's recommendation.

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