

PREM 19/718

PART 20 ends:-

28.9.82

PART 21 begins:-

1.10.82



cc Press Office
JV

Prime Minister (2)

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

29 September 1982

In an otherwise
rather empty Press
last week this
issue got quite a lot
of coverage.

David Clark, Esq.,
Private Secretary to the
Secretary of State for Social Services
Department of Health and Social Security

MUS 29/7

Dear David,

.....
Your Secretary of State yesterday saw a draft of the
Chancellor's reply to Mr. Peter Shore's letter of 24
September. I now attach the final version, which
reached Mr. Shore's office this morning, and will be
released to the press this afternoon.

Copies of this letter, and both halves of the exchange
with Mr. Shore, go to Michael Scholar at No.10,
David Heyhoe in the Lord President's Office, and Keith
Long in the office of the Chancellor of the Duchy.

Yours ever,

J.O. Kerr.

J.O. KERR



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

28 September 1982

The Rt. Hon. Peter Shore, MP
House of Commons

Dr Peter

MS

Thank you for your letter of 24 September. I am glad to answer the points you raise. There is of course no incompatibility between what Leon Brittan and Norman Fowler have said, as you quote them.

As Leon Brittan pointed out, there is an inexorable tendency for public expenditure to grow. We all want more spending on things like pensions, health and education. But there are limits to what it is reasonable to demand of the taxpayer; and borrowing - as the last Government found in 1976 - is no alternative. That is why that Government, of which you were a member, gave an undertaking to the IMF "to reduce the share of resources taken by public expenditure", and did indeed succeed in reducing the ratio of public expenditure to GDP from 46 to 41 per cent, a figure below the present level. Your own experience in 1976 proved indeed how painful and disruptive it is, not least from the point of view of the beneficiaries of these services, to have to make changes at short notice.

That is why we need to know - indeed why all responsible people, including yourself, should want to know - what the long-term costs of present policies are, so that if these look as though they are going beyond what we can afford we can consider what might be done while there is still time to take any necessary action in a sensible way. It is right and proper that a responsible Government should look ahead and consider where things are going, looking to the 90s, and beyond.

Meanwhile, as Norman Fowler has said, our primary purpose, in relation to health and personal social services, must be to develop - to the very best extent that resources allow - those services which attend to individuals in need, which help to prevent suffering or ill-health, and which care for those who are handicapped or ill. I confirm our view that

/where services



where services are best provided publicly they should be so provided, to a proper standard and as efficiently as possible.

It is because of this commitment, and entirely and necessarily consistent with it, that we are concerned about these long-term questions. How to secure the provision of adequate social and other services, at a time when, world wide, economic growth is slower, and what the right balance between public and private provision should be, are among the most difficult questions facing all of us, and not just in this country. These are questions which should concern all thinking people, and which deserve public debate at a rather more serious level than is represented by your letter. Your suggestion that we are contemplating "the destruction of the post-war welfare state" is frankly absurd. We have in fact increased expenditure on the Health Service, after allowing for inflation, by no less than 5 per cent.

Joel Barnett, writing of his experience as Chief Secretary in the last Government, has said "..... overall we failed to achieve the right balance between public and private expenditure because we stuck with levels of public expenditure decided on assumptions of growth in resources that were never achieved." It was that failure which brought about the crisis of 1976, and it is that sort of failure which we are determined to avoid for the future.

Like yours, this letter is being released to the press.

GEOFFREY HOWE



HOUSE OF COMMONS
LONDON SW1A 0AA

24 September 1982

Rt Hon Sir Geoffrey Howe MP
Chancellor of the Exchequer
Treasury
Gt. George Street
LONDON SW1

Dear Chancellor,

Now that you are back from Washington, it really is necessary that you answer some questions which have been widely discussed in your absence and which now appear to be the subject of open debate between your Cabinet colleagues.

When I first read the report in the Economist just over a week ago, describing in some detail the CPRS Report that apparently came before Cabinet on 9 September, I could scarcely credit it. But, as you will know, its account was both confirmed and elaborated by other newspapers, including The Observer last Sunday.

There seems therefore to be no doubt whatever that such a paper exists and that it came before you and your colleagues in Cabinet. The Economist account also alleges that the Think Tank paper was given broad backing by Treasury Ministers.

You will also know that your colleague the Chief Secretary spoke two days ago to Conservatives in West Derbyshire, confirming "that we did talk about the very disturbing long term trend in public expenditure..... it should come as no surprise that we are looking at various options. That does not mean that the decisions on these matters have been pre-judged. They have not been. But radical options have not been ruled out either. The whole area of Government expenditure has to be re-examined to see if we can identify ways in which we might reverse the past inexorable rise in public expenditure".

Since the "radical options" , according to press accounts, include the demolition of the National Health Service, the re-introduction of fee paying in both the nation's schools and higher education establishments, and the de-indexation of retirement pensions and other benefits, what you and your colleagues are talking about is the demolition of the post-War welfare state, an economic counter revolution in Britain.

You will also have seen the speech made by your other Cabinet colleague, Norman Fowler yesterday saying that there was no question of the Government changing its commitment to a public service which placed patients before politics and asserting:- "we need continued commitment and support for the National Health Service from the Government and those who work in it."

You yourself, as the Senior Economic Minister, have said nothing so far. I believe you have a duty to make plain whether your colleague Mr Brittan or your colleague Mr Fowler has given the correct interpretation of the Government's thinking.

You have done already, more than any other Chancellor in post-War Britain, to damage and divide this country. But I warn you now that if you are contemplating the pursuit of these wrecking and destructive policies, you will meet with a national protest, the character of which you have not even begun to understand.

Your name
Robin Cook

A.S. I am releasing this to the Press.



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PRIME MINISTER

Prime Minister

The Press know (Treasury briefing last weekend) that Cabinet will be considering this. It will be important, therefore, to decide at Cabinet what is to be said. At flags A and B are

Public Service Pay and Public Expenditure draft Press guidance
in 1983-84
(C(82) 35) notes which the Chancellor will have in his folder.

The Ministerial Committee on Economic Strategy agreed in July that there was a need for a further substantial reduction in pay settlements in the 1982-83 pay round compared with the round immediately past. There was to be no public numerical target; but the Government should privately aim at settlements of about 4 per cent on average to give overall earnings growth (after 'drift') of no more than 6 per cent. The question of the pay factor for public expenditure planning was left for later consideration (E(82) 17th Meeting, Item 1).

2. This memorandum by the Chief Secretary, Treasury, (C(82) 35) discusses that question. It proposes that there should be a pay factor for 1983-84 of 4 per cent (for public service groups apart from the National Health Service); and that this should not be formally announced until late November or early December as part of the announcement of the Government's public expenditure plans, although (paragraph 7) "if it leaked before then, as must be expected, this may be no bad thing". Ministers would, however, continue to take every opportunity to stress in general terms the need for pay settlements in the coming year to be much lower than in the past year.

MAIN ISSUES

- 3. The main issues before the Cabinet are:-
 - (i) Should there be an explicit pay factor for the purpose of planning public expenditure in 1983-84?
 - (ii) If so, what should it be?
 - (iii) If so, where and how should it be announced?

Should there be an explicit pay factor?

4. Present public expenditure plans for 1983-84 are based on an inflation factor of 6 per cent, not differentiated between pay and prices.

5. The disadvantages of an explicit pay factor are familiar: it may be seen as setting a floor from which public service unions seek to negotiate up, or a ceiling above which public service employers cannot go, or as effectively ruling out genuine pay negotiations.



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6. Those disadvantages could be avoided by a zero pay factor, leaving the whole amount of pay increases to come out of the contingency reserve; but that would weaken the discipline of cash planning.

7. Since inflation may well be running at around 6 per cent in 1983-84, not to declare a pay factor and leave the present figures as they stand would imply provision for the pay bill to rise by about 6 per cent. If that is to be avoided, and the aim of 4 per cent settlements is to be realised, an explicit pay factor, or at least a downward revision of the overall inflation factor, seems inevitable. It is preferable to have a separate pay factor, because the pay content of individual programmes varies very greatly. A figure will in any case need to be set for the preparation of the Estimates; there would probably also be advantage in having a figure which could be conveyed to the local authority employers on 25th October.

What should the pay factor be?

8. The pay factor for 1982-83 was 4 per cent. In that sense a pay factor of 4 per cent for 1983-84 would look like a "no change" signal, and inconsistent with the aim of a reduction in public service pay settlements. Hence the CBI's preference for no "signal" unless it is for less than 4 per cent.

9. But settlements this year were at around 6 per cent or more; so a pay factor of 4 per cent would still be consistent with a reduction in settlements if a major effort was made in public relations and in negotiations to ensure that the outcome, in terms of settlement rates, was nearer 4 per cent in 1983-84.

10. Cash planning demands a pay factor which can be seen as not too unrealistic. The risks of a 3 per cent pay factor are that it would appear to be unrealistic: that it would come in practice to be seen as neither a cash constraint nor as a prediction of the likely outcome but as an opening position in pay negotiations. This could undermine the cash planning approach.

11. There is thus a conflict between considerations of "signal" and considerations of "realism". Realism inclines the Chief Secretary to 4 per cent; the Cabinet will have to decide whether they agree.



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12. There are three other points which are relevant to the size of the factors:-

(a) The NHS Negotiations

The Press have inferred from the most recent offers to NHS workers that the Government is assuming a 4 per cent pay factor for 1983-84. To announce a 3 per cent factor would make those offers seem more generous and increase their chance of being accepted. On the other hand, it could be regarded by other public service groups, notably the Civil Service, as evidence that the Government intended to discriminate against them.

(b) Other current Negotiations

The offer to the mineworkers has been reported in the Press as being worth 8.2 per cent. This may make a figure of 3 per cent look implausible. On the other hand, it is no more out of line with a factor of 3 per cent than last year's settlement of 9.3 per cent on basic rates was with the public service pay factor of 4 per cent.

(c) Effect on Public Expenditure Programmes

The general inflation of 6 per cent for 1983-84 was widely regarded in Departments as providing for about an 8 per cent increase in prices and a 4 per cent increase in pay. The Chief Secretary says (paragraph 14) that he will take account of the "new assumption about public service pay" programme by programme, in his eventual proposals to Cabinet on public expenditure. Spending Ministers may question the implication that a pay factor of 4 per cent (which was implicit in the provision for existing programmes) provides some grounds for revising their figures. The Chief Secretary is likely to reply that 8 per cent is almost certain to be too high for movements in prices, but that he is not proposing a reduction in the public expenditure figures on that account. He therefore feels justified in proposing some adjustments in particular programmes in respect of pay. Some Ministers have reached agreement bilaterally with the Chief Secretary on their programmes and will be anxious for an assurance that the agreement is



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not now to be re-opened. We understand from Treasury officials that the Chief Secretary has struck his bargains in the expectation of a pay factor of 4 per cent and is unlikely to want to re-open them if that expectation is confirmed. If the Cabinet decides on a factor of 3 per cent, he will probably want to look again at the figures. It will not be possible to settle detailed points of this nature around the Cabinet table. If they are raised, no doubt you will wish to invite the Chief Secretary to discuss them bilaterally with the spending Ministers concerned.

Timing and Presentation of Announcement

13. The discussion about the timing and presentation of the announcement will be closely influenced by the decision on what the factor should be. If the decision is in favour of a 3 per cent factor, the Cabinet will have decided to give weight to the "signal" effect, and that would strengthen the case for an early announcement. If the decision is in favour of 4 per cent, there will be a good deal to be said in favour of the Chief Secretary's "low key" approach of deferring a formal announcement until late November/early December, while acknowledging that the decision might leak before then and that this might be no bad thing. That would be consistent with the offer to NHS workers, which has given the impression that the public service pay factor for next year may be 4 per cent. Against this it could be argued that deferring the announcement and allowing the Cabinet's decision to leak could lead to confusion about the status of the pay factor and that it would be preferable to get the Government's position across in a clear and controlled way by an announcement which could nevertheless be "low key".

14. The point is particularly relevant to discussions with the local authorities, whose negotiations have had a formative influence on the last two pay rounds. Ministers are due to meet the local authority employers on 25th October to discuss the coming pay round. The local authorities may be assuming that the Rate Support Grant settlement will allow pay increases of 6 per cent. Even if there has been no formal announcement of the pay factor, the local authorities

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will need and expect to be given clear quantitative guidance. It will be important to have a clear line, agreed between Ministers, before the meeting of 25th October. This can be left to be settled in detail, in the light of the conclusions at this meeting, between the Chancellor of the Exchequer, the Secretary of State for the Environment and the other Ministers with local authority responsibilities.

HANDLING

15. You will wish to ask the Chief Secretary, Treasury to introduce his memorandum. The Chancellor of the Exchequer might then be asked to speak about the economic outlook in general and the pay scene in particular. The Home Secretary and the Secretaries of State for Education and Science, Defence, Environment, Scotland and Social Services will have views on the likely implications for public service pay negotiations in the current pay round; and the Secretary of State for Employment is also likely to have general comments on this aspect. The Lord Privy Seal may wish to comment on the implications for Civil Service management. The Secretary of State for Industry should be able to offer advice about the likely attitude of the private sector. Finally, the Lord President of the Council and the Chancellor of the Duchy of Lancaster may have views on presentation.

CONCLUSIONS

16. The Cabinet will need to reach conclusions on the following:-

- (i) Should there be an explicit public service pay factor for 1983-84?
- (ii) If so, what should it be? and how should it be taken into account in the remainder of the Public Expenditure Survey?
- (iii) When and how should it be made known?
- (iv) What guidance should be given to the Ministers concerned in deciding the line to be taken when the Government sees the local authorities on 25th October to discuss the current pay round?

Robert Armstrong

28th September 1982

CONFIDENTIAL

Public Expenditure Planning and Pay

As usual at this time of year, the Government is now reviewing and finalising the plans for public expenditure in the coming year. Their decisions will be announced at the end of November or early December. As part of the process of reaching final decisions on the cash total for each programme, it is necessary to make a planning assumption about the increase in earnings in 1983-84 for those groups for which the government is directly responsible.

2. The Government had decided to use a single assumption of 4 per cent for this purpose, to be applied from due settlement dates. They have decided to announce it now to avoid possible misunderstanding.

3. This assumption does not apply to the NHS. A decision about the planning assumption to be used for health service expenditure has been deferred.

4. Nor does it apply to the local authorities nor the nationalised industries, which are not within the Government's direct control and in respect of whom the same operational requirement for a planning assumption does not arise in the same way.

5. The assumption determines the provision to be made for the pay of the groups concerned in the public expenditure plans. It is not a pay norm. Nor does it represent a forecast of, or a decision about, the settlements which the government expects to reach. Some settlements may be more, some may be less. Each will be considered on its merits.

6. The Government is, however, convinced of the need to achieve a lower level of settlements than last year in both the private and public sectors if the progress which has already been made in reducing inflation is to be sustained and if the proper foundations are to be laid for more jobs.

Notes for Editors

7. A similar announcement about the planning assumption used for pay in 1982-83 was made last year on 15 September. The assumption for 1982-83 was also 4 per cent.

8. Circumstances this year are different in that the Government is, for the first time, reviewing plans already expressed at the time of the previous White Paper in cash. Consequently there is no need this year, as there was last in the transition to cash planning, to specify a general assumption about prices as well as pay. In general,

However, inflation is coming down more quickly than expected and there is no evidence of programmes coming under greater pressure from the general level of prices than had been anticipated when they were first expressed in cash.

9. The Government's decisions about public expenditure, of which this announcement is part of the background, are expected to be announced in late November/early December.

10. As in previous years, the assumption applies to the increase in earnings (basic pay plus overtime etc), not basic rates and applies from settlement dates. If a reduction in manpower numbers is planned (as in the civil service) that will be taken into account in the calculation of the provision for the relevant programmes.

B

PAY AND PUBLIC EXPENDITURE: GUIDANCE TO TREASURY PRESS OFFICE IN THE ABSENCE OF AN ANNOUNCEMENT

(1) POINTS TO MAKE

1. Of course, Ministers have been discussing the pay assumptions they should use in finalising the public expenditure plans for next year. It is an essential part of cash planning that they should do so. It is necessary to have assumptions about pay for the groups for which the Government is responsible both for the plans themselves and for the detailed Supply Estimates derived from them. A similar requirement arose last year.
2. When the plans are announced in November/December, whatever assumptions have been made about pay will no doubt be made clear as part of the background. But final decisions about public expenditure plans have not yet been taken.
3. It would be wrong therefore to confirm or deny particular figures. But it is no secret that the Government is looking for lower pay settlements this round, which has obvious implications for the assumptions likely to be used.
4. It is important to be clear what we are talking about. There is an operational need to have a planning assumption about the pay of central government groups as part of the process of finalising the provision to be made in particular programmes. The assumption, or assumptions used will not represent a norm, still less an incomes policy. Nor will they represent a decision on the offer to be made in any individual case. Settlements higher, or lower, than the assumptions used will not be ruled out. Each case will be considered on its merits.
5. Ministers have not yet determined any assumption about NHS pay for public expenditure plans. That would obviously be premature.
6. Nor is there the same operational needs for planning assumptions at this stage for local authority or nationalised industry pay.
7. The Government has already announced the amount of cash it is prepared to make available to local authorities next year through the rate support grants. It is consistent with a range of pay outcomes - the lower the settlements the more available for services. But obviously the Government are looking to the local authority employers to play their part in reducing the level of pay settlements.

Any planning assumptions for central government pay will not apply directly to nationalised industries (whose EFLs are not precisely equivalent to cash limits on central government expenditure). But in setting EFLs Ministers will be looking carefully at individual industries' assumptions, including their pay assumptions, in the light of their view of the appropriate level of settlements in the economy generally. Once EFLs have been fixed, it will be for the management of each industry to choose between expenditure on pay and expenditure on other things, including investment.

9. The Government is absolutely committed to getting inflation down further. This is essential if we are to regain our ability to compete and lay the foundation for more jobs. Considerable progress has been made. The Chancellor has already said that he now expects the rate of increase in the RPI to have fallen to around $6\frac{1}{2}$ per cent by the end of this year. The indications are that the improvement will be sustained into next year. It is essential that this is not jeopardised by relaxation on pay. Hence the Government's insistence that the level of pay settlements in the coming year should be lower than over the last 12 months.

PRIME MINISTER

CABINET: PUBLIC SERVICE PAY FACTOR

FLAG A The Chief Secretary's paper C(82)35 proposes a pay factor for the public services for the forthcoming pay round of 4 per cent; and that this decision should not be formally announced until late November or early December. You will know from our briefing for your dinner with the Chancellor on 3 August that we favour a lower pay factor. We also believe that it should be announced earlier, but that is a secondary issue.

The case for a 3 per cent pay factor

The main argument for a pay factor lower than 4 per cent is that 4 per cent or more would result in a rise in average earnings (after negotiation and wage drift) of at least 6 per cent, which would not be consistent with the fall in real wages that Ministers are agreed must be achieved if employment is to recover. The prospect for inflation has significantly improved since Cabinet provisionally agreed a 4 per cent target last summer, and that improvement ought to be reflected in our aspirations for the forthcoming pay round. A further, and strong, argument for less than 4 per cent is that it will become public knowledge sooner or later - probably sooner - and when it does it will be clear to all that the Government is not seeking further deceleration in public sector pay, because 4 per cent is the figure we chose last year.

In the summer we were inclined towards a 2 per cent pay factor, reflecting a serious determination on the part of the Government to bring down real wages. But we accept that, since then, the public sector unions have more effectively got their act together, and that the choice of such a low figure might enable them to rally considerable public support for common cause against the Government. We therefore believe that 3 per cent is the right figure; Alan Walters in particular endorses that.

/ The case

The case for announcement the figure soon

The Chief Secretary's case against an early announcement (ie. before the end of November) rests on the danger of provoking the unions, and particularly the Civil Service unions. But I do not believe that we have most to fear from that quarter. Our current pay difficulties are with the NHS; with the miners; with the water workers; and with the local authority manuals, who will set the tone for the public services who settle later in the round.

Holding back our announcement until the end of November would mean losing the opportunity to influence all of those negotiations.

The NHS in particular, who have been offered a deal which assumes 4 - 4½ per cent for next year, would realise what they stood to lose if they did not settle. The position of the unions representing both the miners and the water workers would surely be significantly weakened if they had to pursue their present claims against the background of a 3 per cent pay factor. And in the absence of an announcement to the contrary, the likelihood is that the local authority employers will base their negotiations on the assumption of 5 per cent, since that was the assumption for this year in last year's figures.

I do not pretend that this decision is absolutely clear-cut. An early announcement of a 3 per cent pay factor would carry some risk of a successful effort by the public service unions to discredit the Government's approach to pay, and could therefore result in a higher pay round than if we had chosen 4 per cent and been able to stick to it. But with the present rate of unemployment, the prospect of Royal Assent to the 1982 Employment Bill, and the preparations we have made for dealing with industrial action in the public sector, we think that on balance it would be right to go for 3 per cent and an early announcement.



24 September 1982



Econ Pol 39

10 DOWNING STREET

From the Principal Private Secretary

SIR ROBERT ARMSTRONG

PUBLIC EXPENDITURE SURVEY: 1982

The Prime Minister has seen your minute of 10 September (A09434) and is content with the proposals in it for a small Ministerial group, consisting of the Home Secretary, the Chief Secretary, Treasury, the Lord President of the Council and the Chancellor of the Duchy of Lancaster, to be established to consider certain public expenditure programmes before the Chief Secretary reports to Cabinet. She also agrees that you should approach the Home Secretary if, after consultation with the Chief Secretary, you wish to propose the establishment of such a group, prior to sending round the minute saying that the group was being set up with the Prime Minister's authority.

E. E. R. BUTLER

13 September 1982

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Prime Minister

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Mus 13/9

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

10 September 1982

The Rt. Hon. David Howell MP
Secretary of State for Transport

NORTH SEA OIL TAX CLIMATE

Thank you very much for your letter of 27 August, and for letting me know Chevron's views about current UK oil taxation.

I do of course accept the point that tax is bound to have some influence on oil companies' future development plans. But there are other factors outside our control which are also important in North Sea decisions - and which the oil companies tend to play down in discussion with government. Oil price uncertainties and technical difficulties, for example, have featured significantly in recent project deferments.

But that is not to suggest that we do not take what the industry tells us seriously. We have told them that we share their concern that taxation should not slow down the overall development of our North Sea reserves. The next generation of fields are likely to be smaller and less profitable than those we have seen hitherto, and special account of the needs of such fields was taken in framing this year's oil tax changes. This point has been made to the industry, and indeed the changes were settled only after full discussions, and a thorough assessment of their likely impact on development prospects. We carried out our usual extensive tests on field profitability under a wide range of economic scenarios, including, especially, falls in the price of oil as steep and steeper than those that occurred just before the Budget. Our conclusion is that the general level of return in the North Sea remains sufficiently attractive over a range of field sizes to encourage an acceptable rate of future development.

The signs are that development is indeed beginning to move again: firm proposals have recently been submitted for the Clyde field, and I know that Nigel's officials are currently discussing other development programmes with the industry as well. Chevron themselves are, I understand, currently carrying out further appraisal drilling work on the Columba field, and as far as I am aware their exploration work elsewhere in the North Sea is continuing.

I was, incidentally, encouraged by the results of a recent comparative study of several different oil tax regimes by Alex Kemp and David Rose of Aberdeen University. They concluded that our current regime is markedly more progressive taking into account field profitability, and variations in costs and oil prices, than those of many of our competitors, and that overall the UK scores remarkably well in terms of its attractiveness to investors.



I think, therefore, that the outlook for the North Sea is by no means as bleak as has been suggested in some quarters. We believe that the tax regime as it now stands leaves the industry with a fair range of attractive prospects for development, and that further major changes are neither necessary nor desirable. But I should not give the impression that we have closed our minds to the possibility of improvement to the details of the regime and we are continuing to hold regular discussions with the industry.

I am copying this to the Prime Minister and Nigel Lawson.

GEOFFREY HOWE

A handwritten signature in dark ink, appearing to be "G. Howe", written in a cursive style.

Ref: A09434



CONFIDENTIAL

Prime Minister

cle J.V.

PRIME MINISTER

Yes not

Mentioned to you by Sir R. Armstrong this morning. You will see that the Secretary of State for Scotland is unavailable. Agree that Sir R. Armstrong should proceed as he suggests, if necessary?

FERB 10.9.

Public Expenditure Survey: 1982

The Cabinet agreed in July that the aim in the next stages of the 1982 Public Expenditure Survey should be to hold to the existing planning totals for 1983-84 and 1984-85, and invited the Chief Secretary, Treasury to hold bilateral discussions with spending Ministers accordingly (CC(82) 38th Conclusions, Minute 5). The outcome of the Chief Secretary's discussions is due to be taken in Cabinet on 21st October.

2. I understand from the Treasury that, although the Chief Secretary still has some way to go before he has completed his bilateral discussions, he thinks it unlikely that he will be able to report to Cabinet, on the basis of those discussions, that the prospective public expenditure figures are within striking distance of the existing planning totals. There are likely to be some programmes - defence and housing, for example - which can be settled only by your intervention or at Cabinet. But there are others which the Chief Secretary may not be able to settle bilaterally but might be susceptible to resolution in a small group of Ministers outside Cabinet.

3. It would be possible simply to let this situation develop and to take whatever action seemed appropriate in the light of the Cabinet discussion on 21st October. But that may not be the best way of proceeding. The Cabinet has already set the underlying policy: it could do no more than reaffirm (or weaken) it on 21st October. And because the Government has announced its intention, in response to the recommendations of the Treasury and Civil Service Committee, of publishing its expenditure and other plans in more detail this autumn than in past years, time will be short if spending Ministers wait until after 21st October before getting down to serious negotiations. It seems worth making every effort to settle as much as possible outside Cabinet before 21st October.



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4. This points to the setting up of a small Ministerial Group to do the work that was done last year by the Ministerial Group on Public Expenditure (MISC 62). The group would operate within the framework of the Cabinet's decision in July; and its recommendations would be reported to Cabinet in time for the discussion on 21st October. Because of the Party Conference and other timing constraints, such a group would have to do most of its work in the latter part of September.

5. I suggest that the Home Secretary might be asked to act as Chairman, with the Chief Secretary, Treasury, the Lord President of the Council and the Chancellor of the Duchy of Lancaster as members. I understand that these Ministers are expected to be in this country during the latter part of September.

6. This membership differs from that of MISC 62 (and the group would therefore have a different serial number, though the same title) in leaving out the Secretaries of State for Industry and Scotland and including the Lord President of the Council and the Chancellor of the Duchy of Lancaster. The two non-departmental Ministers have no expenditure programmes to protect. I am afraid that the Secretary of State for Scotland will be in North America until 29th September, and will not be available. We could try the Secretary of State for Industry, but he is one of those whose programmes the group is likely to need to consider. The Secretary of State for Wales will be out of the country. The Lord Privy Seal is a possibility; but she will be out of the country from 20th to 24th September.

7. Because the Chief Secretary's series of bilateral meetings is still in progress it is not yet possible to be sure that a group on these lines will be needed. The Chief Secretary does not expect to be able to make a firm assessment of the need for about 10 days; by then, of course, you will be in the Far East. I therefore propose, if you are content with the approach suggested in this minute, that you should authorise me to approach the Home Secretary, if after consultation with the Chief Secretary it seems clear that such a group needs to be set up. I should then send round a minute, making clear the purpose for which the group was, with your authority, being set up.

Yes
ms

RA

Robert Armstrong

10th September 1982

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CONFIDENTIAL

Ref A09400

PRIME MINISTERThe Longer Term: C(82) 30, 31, 32 and 33

BACKGROUND

Early this year, after the Chancellor of the Exchequer had expressed concern about the prospects for public expenditure in the longer term, you agreed that officials should set in hand an examination of the likely pattern of public expenditure over the next decade on the basis of a range of possible assumptions about growth and other factors. The resulting study by officials was circulated to the Cabinet (and has been re-circulated with C(82) 32) with the Chancellor's minute of 28 July, which suggested that the prospects revealed in the study were disturbing and that the Cabinet should have a broad-ranging discussion about the Government's long-term objectives for the size and shape of the public sector. He suggested, and you agreed, that the CPRS should be asked to prepare a paper outlining possible ways of making significant changes in the scale and pattern of public expenditure.

2. This line of thought is developed further in the Chancellor's memorandum (C(82) 30), and the accompanying note by Treasury officials containing projections of tax revenue and borrowing.

3. The memorandum by the CPRS (circulated with C(82) 31) discusses a number of radical options for achieving substantial reductions in the longer-term. The memorandum by the Secretary of State for Defence (C(82) 33) argues against one of these options, a levelling-off of defence expenditure after 1985-86 rather than a continuance of 3 per cent annual growth in volume.

4. The Treasury notes on expenditure and taxation explore two economic scenarios -

Scenario A: GDP grows at an average rate of $2\frac{1}{2}$ per cent a year; unemployment falls to 2 million by 1990-91; and inflation runs at 5 per cent a year in the middle and late 1980s.

Scenario B: GDP grows at an average of $\frac{3}{4}$ per cent a year to late 1985-86, then at $\frac{1}{2}$ per cent a year to 1990-91; unemployment is 3 million in 1990-91; and inflation runs at 10 per cent a year in the middle and late 1980s.

Under both scenarios real wages in the market sector are assumed to increase at $1\frac{1}{2}$ per cent a year; but under Scenario A, productivity in the market sector is assumed to increase at 3 per cent a year, implying a significant increase in profits.

5. The expenditure, taxation and borrowing projections under the two scenarios are set out in the table annexed to this brief, which also sets out comparative figures for 1982-83. The Chancellor argues that the outlook under Scenario B is unacceptable: in order to contain the borrowing requirement at a tolerable level taxes would have to be raised to levels which would wreck the Government's whole economic and political approach (and would probably lead to serious evasion, involving still higher nominal rates of tax).

6. The Chancellor also argues that even the outlook under Scenario A is not really acceptable, on the grounds that the expenditure figures are probably understated; that in order to improve incentives and profitability reduction in taxation will be needed; and that it will not be possible to do this, consistently with a tolerable borrowing requirement, unless expenditure is lower than projected. In any event, it would be imprudent to plan on the assumption that the economy will develop as favourably as Scenario A implies.

7. He therefore concludes that it is essential to study ways of creating room for manoeuvre in public expenditure. He does not seek specific cuts at this stage, but suggests that the options identified in the CPRS memorandum should be studied and the results reported to Cabinet in the Spring of 1983. He also proposes -

- i. that Ministers should make no further public commitments which would add significantly to expenditure beyond 1985-86, and should avoid repeating former pledges which would otherwise expire;
- ii. that in this year's Public Expenditure Survey particular regard should be paid to the longer-term indications of decisions; and
- iii. that Ministers should consider further how the issues should be presented publicly.

MAIN ISSUES

8. The importance of this meeting lies in the opportunity it provides for the Cabinet to lift their eyes from current and short-term preoccupations and to focus on what they would like the shape of things in this country to be at the end of the decade. The discussion should be not just on the size of public expenditure in relation to the gross domestic product but about the role of the Government and the public sector, particularly in the fields of education, health and the social services. If broad political judgments and conclusions on chosen matters can be established, they will give a basis for and a sense of direction to the discussion of specific options. It would be better to use the time in that way than in detailed discussion and criticism of the Chancellor's projections and scenarios.

THE PROJECTIONS

9. The projections are stylized and in no sense forecasts; but, on their own terms, it is hard to see much wrong with them. The projections for individual expenditure programmes have been discussed between departments at official level. The Ministry of Defence have complained that it is unfair to draw attention in paras 15 and 16 to the increase in the share of GDP devoted to defence and the fact that in cost terms the projected percentage increase in the defence programme is greater than that for other programmes, without reminding the reader that the social security programme is about twice the size of the defence programme. This is what Mr Nott is referring to in the first sentence of paragraph 4 of C(82) 33. However although some Ministers may complain about presentation there is so far as we know, no disagreement about the figures.

THE PROSPECTS

10. There may be criticism of the Chancellor's argument that the projections reveal an unacceptable prospect. Possible lines of arguments are as follows -

a. 'Scenario B is not realistic.' It may be said that if, for a decade, growth remained at little more than $\frac{1}{2}$ per cent a year and inflation at 10 per cent, and unemployment was permanently over 3 million (the 3 million given in the note by officials is the narrow definition - the 'headline figure' would be significantly larger), there would be profound social and political upheavals. To plan for Scenario B is therefore to plan for disaster. Moreover, Scenario A may be optimistic by comparison with our own performance for much of the 1970s; it is less so by comparison with the 1950s and 1960s in the United Kingdom, or even later in other countries.

b. 'The prospects under Scenario A are less serious than the Chancellor suggests.' His argument that the expenditure figures are understated may be challenged (the health figures, for example, allow for significant real growth; it may be possible, with faster economic growth, to cut back substantially on expenditure on industrial support and employment and training measures); and there may be room, as real incomes grow, to improve incentives by a further switch from direct to indirect taxation. It may

also be suggested that his arguments about the need to reduce the size of the public sector are overstated since the Government's privatisation programme will achieve a much larger transfer of economic activity to the private sector than appears in the public expenditure figures. (The public expenditure figures include only the external financing requirements of the nationalised industries; a much better measure of the importance of their economic activity is their turnover.) The Government certainly regards defence and law and order as essential public sector activities and has made clear its intention to increase expenditure on them.

c. 'The prospects, if realistic, cast doubt on current economic policies.' Some of your colleagues may wish to broaden the discussion out to include short-term economic prospects and policies. However, the purpose of the meeting is to discuss the longer-term. Moreover it is a misunderstanding of the Chancellor's argument to suggest that the modest economic performance implied by the two scenarios calls the Government's basic economic policy into question. The scenarios are not forecasts; and the Chancellor is arguing that a reduction in the relative size of the public sector is a necessary condition of being able to improve on them (and perhaps even to achieve an outcome as favourable as Scenario A).

WHAT IS TO BE DONE?

11. Your colleagues will naturally see a link between the question whether the prospects sketched in the papers are unacceptable and the question of what should be done to change them. At the extreme, some may argue that to adopt any of the radical proposals discussed by the CPRS would be even

more unacceptable than the prospects on unchanged policies. But the meeting will have failed in its purpose if Ministers collectively are not willing at least to contemplate the possibility of radical action. If they are willing to contemplate that, then it would probably be best to say that all options should be remitted for further study, unless there are any that you and your colleagues think so unrealistic that it would be a waste of time to study them. If many areas are exempted from study, it will be more difficult to persuade those whose responsibilities are not exempted to give full co-operation.

OPTIONS DISCUSSED BY THE CPRS

12. For the most part, the considerations relating to the proposals discussed in Annexes A to K of the CPRS paper (C(82) 31) are very clearly set out, and the paper serves as its own brief. But in a few cases there are additional points that you may wish to bear in mind, or which seem worth emphasising further.

i. SMALLER PROGRAMMES (ANNEX A)

There may be more to be looked at in the field of housing than the note suggests. Increasing rents - and relating rents more closely to standards of accommodation - should reduce the demand for housing and so save money indirectly as well as directly. If such possibilities are to be looked at, it will be for question whether it is necessary also to look again at mortgage interest relief.

ii. PUBLIC SERVICE MANPOWER (ANNEX B)

The Cabinet is not being asked to take immediate decisions on Civil Service manpower. Treasury Ministers intend to bring forward a paper on this subject to Cabinet before the end of this year.

It will be important to ensure that any study of reduction in expenditure outside central government includes a study of methods of enforcement. There is, for instance, little point in constructing public expenditure programmes on the assumption that local authorities will reduce manpower simply in response to Government exhortation.

iii. ACCOUNTING CHANGES (ANNEX C)

As the CPRS point out, these changes would be purely cosmetic, and would have no effect on the balance of the economy.

iv. PRIVATE HEALTH INSURANCE (ANNEX E)

As the Annex implies, it will be important to be clear whether the aim is to reduce taxation and the size of the public sector or 'national overheads' - the burden on productive industry and commerce. If it is the latter, private health insurance could even be counter-productive, for the reasons given in paragraph 6 iii. of the Annex.

v. CUTTING SOCIAL SECURITY BENEFITS (ANNEX J)

If Ministers are willing to 'think the unthinkable', they may wish to consider more radical changes in the structure as well as the value of social security benefits. Is it, for example, necessary to provide indefinitely a comprehensive system of widows' pensions if women are expected to become economically more self-sufficient?

13. There are also some more general questions (including those discussed in paragraph 15 of the CPRS memorandum) which Ministers may wish to have considered, either as points to be taken into account in whatever specific studies may be commissioned or as subjects in their own right, for example -

i. As is pointed out several times in the paper, public expenditure has a strong tendency to increase, almost irrespective of circumstances. (It is, for example, striking that the levels of expenditure projected under Scenarios A and B are virtually the same.) What are the reasons

for this? Is it largely as the Chancellor implies, a matter of changing public expectations which can be achieved by the necessary degree of political will and a major effort of public education? Or are there other causes which need to be identified and remedies found for them?

ii. There is little pressure in much of the public sector to find ways of doing the same thing at lower cost. It appears, for example, to be taken for granted in Annex 2.11 to the officials' note on the expenditure projections that improvements in medical care will mean more expenses. But industry would probably think it as important to find ways of doing the same thing at less cost as to find ways of doing new things. Can more of this approach be imported into public service?

iii. As paragraph 15b. of the CPRS memorandum points out, some of the options, involving new charges with reliefs for the less well-off, would have important effects on incentives. Should there be a study of the structure of taxation, benefits and public sector charges in the longer term?

iv. A related question is the extent to which the problem discussed in the papers is a problem of the prospective total tax burden or a problem of high nominal rates of direct taxation. If it is solely the former, reductions in prospective expenditure are the only solution. But if it is partly the latter, it strengthens the case for examining the structure of the tax system, including tax relief.

ORGANISATION OF STUDIES

14. If there is to be a programme of far-reaching studies by officials, it will need to be carefully organised. At the meeting, I suggest that you should say that you yourself will consider how it should be set up. I will then offer you further advice when it is clearer what the exact scope of the studies is to be.

PUBLIC PRESENTATION

15. It is implicit in much of the discussion that public opinion has come to expect an ever-increasing provision of public services. If this expectation is to be reversed, a major campaign of public education will be needed. You may wish to ask the Chancellor of the Exchequer to bring forward specific proposals in the light of the discussion.

HANDLING

16. I suggest that it will be convenient to break the discussion into two parts. (This will fit in well with the suggestions in the Chancellor's minute of 27 August to you - not copied to other Ministers), ie -

i. A general discussion, relating mainly to the two Treasury papers, (C(82) 30 and 32), on the prospects for public expenditure, taxation and borrowing over the period to 1990-91, and what the Government's broad aims and strategy ought to be.

ii. A discussion, relating mainly to the CPRS paper (C(82) 31), of the options which might be studied for bringing public expenditure in the longer-term more in line with the Government's preferred strategy.

17. Depending on how the discussion goes, the first part might be taken before lunch and the second in the afternoon.

18. You will wish to invite the Chancellor of the Exchequer to introduce the first part of the discussion. All your colleagues will wish to contribute; but I suggest that it will be desirable to try to avoid discussion of purely departmental points (unless they have a significant bearing on the prospects for expenditure or taxation) and concentrate on the broad political aspects.

19. For the second part of the discussion, you will wish to ask Mr Sparrow to introduce the CPRS memorandum. You might then go through each of the Annexes to that paper in turn, inviting comments from the responsible Minister or Ministers (there are, in particular, important Scottish and Welsh dimensions to education, health and local authority matters).

The Secretary of State for Defence will presumably wish to speak on his paper (C(82) 33). The Chief Secretary, Treasury may also wish to offer comments on individual programmes. You might then ask for additional suggestions, whether general or particular; or advance any which seem to you to merit further study.

CONCLUSIONS

20. You will wish the Cabinet to reach conclusions on the following -

a. whether, as the Chancellor of the Exchquer recommends in C(82) 30, there is a need for a new and fundamental look at levels of public spending; which calls for a programme of studies by officials reporting back in (say) six months;

b. whether, as part of the new and fundamental look at public spending, there should be studies relating to -

i. Health (increased and extended health charges - Annex D and private health insurance - Annex E);

ii. Education (cutting spending - Annex F, charging - Annex G, and charging for higher education - Annex H);

iii. Social Security (breaking the link between benefits and prices - Annex J);

iv. Defence (Annex K);

v. Smaller programmes (Annex A);

vi. Public service manpower (Annex B);

vii. Accounting changes (Annex C);

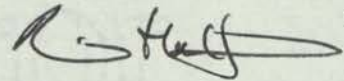
viii. Any other subjects proposed in discussion.

c. whether it is agreed, as recommended in C(82) 30 -

i. that no further public commitment should be made adding significantly to expenditure in the longer-term, and that pledges which would otherwise expire should not be extended;

ii. that in the 1982 Public Expenditure Survey particular regard should be paid to longer-term implications;

iii. that further consideration should be given to the public presentation of the issues.



Approved by
ROBERT ARMSTRONG
and signed in his absence.

8 September 1982

	<u>1990-91</u>				<u>1982-83</u>	
	<u>Scenario A</u>		<u>Scenario B</u>		<u>£m*</u>	<u>% gdp</u>
	<u>£m*</u>	<u>% gdp</u>	<u>£m*</u>	<u>% gdp</u>		
Programme totals	109.0	36.9	107.5	<u>43.8</u>	95.5	40.7
Debt interest	7.0	2.4	7.5	3.0	7.5	3.3
	—	—	—	—	—	—
Total public expenditure	116.0	39.3	115.0	46.8	103.0	44.0
<u>less</u> taxation	109.9	37.2	97.4	39.7	92.1	39.4
	—	—	—	—	—	—
Borrowing requirement	6.1	2.1	17.6	7.1	10.9	4.6
	—	—	—	—	—	—

* At 1980-81 cost terms or prices.

PRIME MINISTERPUBLIC EXPENDITURE IN THE LONGER TERM1. The task of explaining

The Treasury's projections have wonderfully concentrated the minds of Ministers and officials upon the growing burden of existing commitments and lines of policy. We recognise that this burden, if unaltered, will within the next decade call for taxation at intolerable levels which can only seriously damage our economy.

Yet we have still to convince the public of this. In particular, we have to educate the public in the uniquely large size of Britain's nationalised sector. No other Western nation has both a 95% nationalised education service and a 95% nationalised health service, as well as a high degree of nationalisation in the fuel, transport, and basic heavy industries and the utilities. While, say, Sweden may have a comprehensive welfare state, her industry has a remarkably low degree of nationalisation. State control in France covers a wide variety of industry and services, yet there is room for the private sector to breathe in the provision of welfare. It is vital to get across that Britain is still conspicuously over-nationalised by Western standards.

2. The options

The CPRS performs a valuable task in confronting starkly some of the options for the four major sectors where increased spending is certain on existing policies.

However, I doubt whether these options exhaust the possibilities. And in some cases, they tend to propose solutions that are so politically difficult that we may be tempted to shy away from the whole idea of radical reform and ignore less unpopular alternatives.

We do not have either to do nothing or to cut or abolish state services which have been with us for a century or more.

Instead of crude cutting, a better alternative strategy would often be to freeze the public service and boost the private element. What has gone wrong, after all, is not so much the existence of a public

service in the first place as the progressive throttling of private contributions and alternatives.

3. Private health insurance

The growth of voluntary private health cover, from 2½ to 4 million persons under this Government, is phenomenal. To extend the existing corporate tax reliefs to individuals might well unleash a further spurt. This would require only a modest amendment in a Finance Bill. It would avoid the huge complications of fitting a compulsory national private health insurance scheme in with an inescapable public safety-net scheme. It also avoids the bureaucracy and hard cases inherent in a means-tested extension of charges.

If we combine:

- (a) fiscal encouragement of the natural growth of private health insurance;
- (b) equally natural extension of the de facto tendency towards privatisation in the optical, dental, etc services;
- (c) increases in those charges which are cost-effective;
- (d) proper control of costs in the NHS hospitals and in the GP services,

we would be resuming the natural growth of the alliance between the communal and individual provision of health care which is the British tradition that has been interrupted by the progressive squeezing out of the private sector in the post-War years.

4. A revived alliance between private and public in education

Again, on education the CPRS's options seem incomplete; they omit any serious consideration of vouchers or, as W E Forster put it in 1870, education "tickets".

The prime purpose of vouchers is to confer power on less well-off parents.

But a subsidiary effect is to provide scope for increased private expenditure on education. If we set the state voucher at a basic, or "no-frills" level, then we would expect both l.e.a. schools and independent schools to have their income supplemented in order to satisfy parental expectations - either by parents themselves, or by grants from the rates, or by contributions from churches, charities and businesses. This is the kind of partnership which is taken for granted all over the Continent and in Northern Ireland.

To take a simple example, if we froze the ticket or capitation grant at roughly the present level of £900 per pupil, a contribution of £3 per week from non-state sources (the equivalent of 10 cigarettes a day) would produce a 16% increase in expenditure per pupil.

5. Social security

We must distinguish between:

- (a) the problem of retirement pensions, where we have consistently promised to maintain purchasing power; and
- (b) the problem of unemployment benefit where any commitment to maintain purchasing power runs into the poverty trap and the "why-work" syndrome.

With retirement pensions, the only economy that is realistically to be expected is that they should be frozen at their present real value. Considerable savings can, however, be made by making sure that miscalculations about the future rate of inflation do not allow real benefit levels to creep upwards. The expectation of a real annual 1% increase in Scenario A ought not to be tolerated.

The levels of unemployment benefit must be fitted into Government strategy for reducing unemployment, and cannot be discussed solely in the light of economising on Government expenditure.

But any effective strategy for reducing unemployment must have the beneficial side-effect of reducing Government expenditure as well.

6. Defence

The Secretary of State for Defence rightly points that the peculiarly adverse impact of the Relative Price Effect on defence spending is sometimes acknowledged by the Treasury, and sometimes not.

He claims that an "adequate" defence and deterrent capability can be manned only by continuing to aim for a 3% real increase in expenditure each year into the foreseeable future. He envisages that defence spending should rise from just over 10% of general Government expenditure to nearer the average of the 1960s, at about 15%.

But of course there is no reason to assume that the increase would stop there. Since the increase in the growth of the economy is unlikely to come anywhere near 3% per annum, and since the adverse

RPE is unlikely to vanish in 1990, the progressive militarisation of Government spending - and of the British economy as a whole - would be open-ended. Historically, it is reckoned that an over-militarised nation is in the end likely to be as unstable economically and politically as an under-militarised nation. There are two things we can do:

- (a) Insist on the most rigorous and continuous independent appraisal of defence spending in all its aspects. The Treasury does not at present seem equipped for this massive task.
- (b) Re-examine what we mean by "adequate".

fm

FERDINAND MOUNT



Prime Minister

(1)

CF/
Pl pm
MS 6/9

SECRET

Agree circulation of this modified version?
MS 3/9

Qa 06051

2 September 1982

To: PRIME MINISTER

From: JOHN SPARROW

11- in not the annexes that should be withheld - but the short summary of them in the condensation - to the main paper - which I see have been deleted. I have not seen though for other sections which I consider could justify the wrong impression.

Long Term Options and Public Spending

1. Michael Scholar has told me of your reactions to our draft paper on radical options for public spending in the longer term. I fully understand your concern about the possibility of leaks, but I believe that there is a risk whatever the form of our paper. It seems to me that the most damaging leaks would come from reproduction of any of the major options reviewed in Annexes A - G of the original draft and that modifying the document therefore necessarily precludes a circulation of those annexes.

2. We have changed the covering paper to take account of your worries and to make it possible to omit Annexes A - G. I have to say that the document loses a large part of its punch and immediate relevance as a result, making it more difficult for Ministers collectively to decide what full-scale reviews they want to commission (as proposed in the Chancellor's paper). But you may feel that it is preferable to have the revised draft circulated and keep the deleted Annexes simply as briefing for yourself and the Chancellor.

3. In view of the sensitivities, I have not circulated the revised paper in accordance with the 7 day rule but have withheld it until I can hear from you whether you still prefer the modified form and if so, whether it is now acceptable. I enclose copies of both the original draft and the revised version and would welcome a message, preferably before 10.00 a.m. on Monday morning.

JS.

May I have a word with Michael on Monday morning. Short of going through both papers and for word it is not easy to make changes. not

SECRET

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[Revised Version]

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C(82)

COPY NO

September 1982

CABINET

LONGER-TERM OPTIONS

Memorandum by the Central Policy Review Staff

The Chancellor's paper (C(82)) considers the prospects for public expenditure in the longer term and proposes a new and fundamental look at public spending programmes. The CPRS has been asked to examine some of the long-term options open to the Government, especially as regards the possibilities for major structural changes affecting the larger expenditure programmes.

2. This presents an unusual opportunity for the Government to review prospects over the rest of the decade and beyond, and to consider any major changes of direction. We have therefore considered what changes of approach Ministers might wish to examine in each of the four main programmes. Such changes would involve a major shift of policy, so that Ministers may well not wish to reach decisions now, but instead to arrange for a full review to report within say six months for collective consideration then.

3. Although these four programmes together cover nearly two-thirds of total public expenditure, there may well be room for radical changes of direction in other areas also. Some of these are mentioned briefly in Annex A, so that Ministers can consider whether they want more work done on them (beyond the reviews already taking place in some areas).

4. There is one area, public service manpower, where we believe collective consideration might be valuable, and this is discussed in Annex B. A related objective might be to reduce public spending by holding the relative costs (including wage costs) of public services below the rest of the economy. But the projections by officials already assume public service wages falling relative to "market sector" wages by 10% or more in the decade to 1990, and it seems unrealistic to suppose that a further large permanent shift could be achieved. In any case this turns on future wage negotiations, and we see no distinct "policy option" which could usefully be reviewed at this stage.

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11 send a copy

This paper + annexes to Secretary Muntz.

MUS 6/9

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5. In considering major options, we suggest that Ministers will wish to measure them against several objectives:-

- agreed*
- (i) to improve incentives by reducing the burden of taxation;
 - (ii) to increase freedom of choice;
 - (iii) to ensure that those who demand public services appreciate their cost by requiring them to pay;
 - (iv) to allow increasing demands to be met by market sources rather than constrained by public expenditure limits;
 - (v) to maintain or increase efficiency;
 - (vi) (as a minimum) to reduce the nominal total of public expenditure, even without any of these consequences. (This might well be dismissed as "cosmetic", but two possibilities are discussed in Annex C.)

If Ministers decide that any options should be fully reviewed, we suggest that part of the purpose of the review should be to examine how they measure up to these broad objectives. The following paragraphs outline a broad approach to each of the four main programmes, and suggest options (which we have examined in rather more detail) for review.

Health

6. As living standards rise, individuals are likely to demand more and better health care. There is some social gain from improved health care, but mainly it is a matter of individual wants and choices (income-elastic demand). Hence it is arguably not appropriate for public finance, and puts a strain on the Exchequer by distorting choices and shifting the burden from consumer to taxpayer. Public health services also tend to be led by producers rather than consumers.

7. It is therefore worth considering whether over a period the provision of health care for the bulk of the population could be shifted from the State to privately owned and run medical facilities. Those who could not afford to pay would then have their charges met by the State, via some form of rebating or reimbursement. As an exception to the general rule, it might be judged more efficient for the State to continue to provide institutional care for long-stay patients (mentally handicapped, elderly) who clearly could not afford to contribute.

8. This would mean leaving to individuals how far they insured against facing high costs of health care, and it would be important to monitor the growth of private health insurance over the intervening period. Given that the State would in the last resort meet the costs of necessary health care, there could be a danger of under-insurance by a large part of the working population, and thought might therefore have to be given to a scheme for compulsory private insurance.

9. If Ministers accept the broad concept as a longer-term objective, they will want to judge more immediate health options as steps along the road. In particular they will want an examination of how far the switch from public to private provision of health care could be promoted, and whether they are any institutional changes, within the NHS, which could make this switch easier.

10. There has been a departmental review of health service financing options earlier this year. But in this broader context there might be a case for a fuller review of two options, as stages towards the longer-term objective:-

(i) Increased and extended health charges

(ii) Private health insurance

Education

11. The demand for education, as for health, is likely to be "income-elastic" - as living standards rise, people will want to spend a higher proportion of their income on more and better education for their children, and will be increasingly frustrated by the lack of any way of making this choice effective within the State primary and secondary system. In addition, however, there is a social interest, arguably greater than in health, in the quality and quantity of education, because these will determine the capacity and versatility of the next generation of working people. Hence in our judgement it is probably not realistic to envisage, even as a long-term option, the wholesale privatisation of provision for education in schools. However, it may well be desirable to make higher education more market-oriented, giving more choice to consumers and making the system more responsive to the needs of both students and employers.

12. We therefore assume that the State will continue to provide universal facilities for children of primary and secondary school age, and to be concerned about quality. But the parallel system of private-sector schooling will remain, and may expand with increasing prosperity.

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More parents could be encouraged to choose the private sector, at the margin, by schemes for vouchers or tax relief; but if such schemes simply relieve parents of part of the cost of education, they are bound to be expensive for the taxpayer. Hence as radical options for schools education, Ministers may wish to consider a substantial reduction in the resources going to the public sector, or compulsory charges for schooling (which could be combined with vouchers). For higher education (where most of the provision is already private-sector though publicly financed) an option might be to charge the full cost of tuition.

Social Security

13. The present system indexes most benefits to prices, and a very large number of beneficiaries (9m pensioners, 3m unemployed etc) have the real value of their benefits preserved, even at times when the working population has to suffer a cut in living standards. The Government probably cannot avoid recognising preservation of real value as a benchmark (as for tax thresholds). But it could avoid any commitment to prolong the link between benefits and prices, and take the first legislative opportunity to break the link. With inflation down to a much lower level, the assurance of full protection is arguably less necessary. Given discretion to hold benefits below inflation, it could make a once-for-all cut as a contribution to reducing the tax burden. It would also, of course, have discretion to allow beneficiaries a share in increased prosperity when economic conditions improve, by increasing benefits ahead of prices.

Defence

14. The United Kingdom has been struggling to maintain its NATO commitment, when many other NATO members have not done so. The share of defence spending in GDP in the UK is among the highest, and this arguably reflects some failure in the UK to adjust to poor economic performance and a reduced role in the world. There are serious and complex issues here which Ministers may wish to consider:-

- could there be greater emphasis on mutual defence with fairer sharing arrangements?
- should there be a link between European defence (BAOR) and EC budget negotiations?
- if a reduced role has to be accepted, does this have implications for FCO and aid spending as well as defence?

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Some of these issues go outside the defence area and are mentioned in Annex A. Within the defence field, the main option would be to halt the real growth of defence spending after 1985/86.

General

15. On the major options there are some general points to make:-
- (a) Some options may lead to an increase in the amount of real resources (including labour) devoted to these services. Charges for education and health, for example, might have the effect of increasing the resources consumed by those services, if people chose to buy more of them. So long as the services are provided within the public sector, we think that Ministers will wish to see the claim which they make on resources reduced. But where people choose to pay more for private sector services, they should be free to do so.
 - (b) Some of the options would involve higher charges for services, and these raise difficult questions about incentives. Assuming no change in the existing tax and social security systems, charging for the full cost of services would cause a massive redistribution of income, in general away from families to people without children. This would exacerbate poverty to a level which we assume Ministers would judge unacceptable. To the extent that it is desired to adjust for these effects, changes in the charging, benefit or tax systems would be needed. If charges were rebated or reimbursed to those below some income threshold, the inevitable result would be high marginal "tax" rates at the bottom of the scale. This adverse effect on the incentive to find a job or earn more would offset the gain from lower direct tax rates made possible by the expenditure saving. A form of graduated income support, probably requiring a fully integrated system for combined tax and benefits, would be preferable; but even then there might be little or no overall gain in incentives, though the effect would be distributed more smoothly up the income scale. If minimal charges for schooling or health insurance were compulsory, they would only reduce the aggregate burden of taxation in a nominal sense; but they could allow more people to make their own decisions at the margin (analogous to a shift from direct to indirect taxation).

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- (c) Some of the options would make some people worse off. But it is very difficult - in many cases impossible - to effect changes in the role of Government without making some people worse off, particularly where public expenditure and hence taxation are involved. It is therefore necessary to accept that possibility, whilst always recognising that it is the proper function and duty of Government to ensure that no-one is made so much worse off that he or she is subjected to undue hardship. If poverty is thought of as a relative condition, adverse redistributive effects become hard to accept. If, however, it is recognised that there is such a thing as an absolute level of poverty from which people should be protected, and that poor people should share in the increasing wealth of the country, but perhaps not in full proportion, then some redistributive effects can be accepted - as they must be if the amount of wealth available for distribution is to increase.

Conclusion

16. Ministers are invited to decide -
- (i) whether they wish to commission full strategic reviews of any of the main options discussed in paragraphs 9, 11, 12 and 13 above;
 - (ii) whether they want to include additionally any of the possibilities listed in Annexes A, B (manpower), and C (accounting changes).

Cabinet Office

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SMALLER PROGRAMMES

Some other programmes, outside the four major programmes discussed in the main paper, could offer scope for very significant reductions in public expenditure, either by a generalised squeeze or by identifying policy changes. Following is a list of smaller areas where there may be scope for review, with figures for present annual spending (in 1980-81 cost terms, from the LTPE report) -

i. Export credits - the LTPE figure of £0.3 bn does not reflect extent of commitments, and there may be scope for review.

ii. Employment - £2.2 bn - much of this reflects policy reactions to the state of the labour market and will continue to do so; but there might be some scope for review:

- the Youth Training Scheme might take the place of the last year of compulsory schooling, instead of following it;

- on the training side, a remissible training tax on employers would reduce public expenditure;

- on employment services, privatisation of job centres might be examined.

iii. Regional - counting together expenditure by the Departments of Industry and Environment, this is of the order of £1 nb a year, and is already being reviewed.

iv. Housing - £2.9 bn - has been falling, but the future trend depends mainly on the real level of rents (as well as rate of sales, new building and improvements); a review of rent policy, and of relating subsidy to current rather than historic values, might be worthwhile (though most of the savings would not count as public expenditure).

3. Some other significant areas are -

i. Payments to European Communities - £1.8 bn - depends on future negotiations (in which it may be necessary to bring in the possibility of alternative defence savings, eg in BAOR).

ii. Other local authority services - £10 bn - there may be more scope for increased contracting out and/or charging, analogous to charging for education.

iii. Nationalised industries - £2.3 bn: - privatisation will generate once-for-all gains, but where industries sold are self-financing will have a nil or negative effect on total EFLs thereafter; - continuing deficits might be removed or reduced in the longer term, but this is bound to be a difficult and piecemeal process.

iv. Scotland, Wales, Northern Ireland - £10 bn - extra spending in Scotland in relation to needs has been investigated in the past, and is probably not worth a further full-scale review.

PUBLIC SERVICE MANPOWER

Proposal

1. Ministers would decide on a target for further reduction of civil service manpower, by say 10 per cent during the next Parliament. This would entail giving a high priority to -

- reducing functions, contracting out etc;
- simplifying policies and procedures (tax, social security etc);
- legislation where necessary to achieve these changes;
- expenditure on information technology.

The overall reduction would be allocated among departments and services according to the scope for such changes.

2. Similar targets would also be set for reductions in NHS and local authority manpower. These could be linked with increasing contracting out and privatisation of services.

Background

3. The pay bill for the civil service (industrial and non-industrial) is about £5 bn this year. Numbers will already have been reduced by about 14 per cent since 1979, so that the scope for further reduction merely by a continuing squeeze on numbers is likely to be small. Hence the need for more radical changes in functions and policies.

4. In principle there should be room for at least equal savings in other public services. The NHS employs approximately 1 million people, and numbers increased by 5 per cent between 1979 and 1981. The Government has set targets for reductions in management costs as a proportion of NHS resources over the next three years (in England, a cut of 10 per cent). Local authorities employ about 2 million people, and have reduced numbers by about 3 per cent since March 1979 - mostly in the education service, which employs nearly half the total.

Arguments in Favour

5.

- i. Over the rest of this decade, information technology will yield further economies in data processing, storage etc. It is already being applied to Government administrative operations, but the pace could be accelerated.
- ii. To achieve anything like a further 10 per cent reduction in civil service numbers would mean a radical review of present functions to achieve contracting out or privatisation of those services where economic costs might be charged (eg ^{eg} PSA, ^{or} ADAS). This would be in line with Ministers' objective of "rolling back the frontiers of the public sector".
- iii. Very worthwhile savings might be achieved by subjecting NHS and local authority manpower to the sort of squeeze which has proved successful in the civil service. Pressure on numbers should lead to the contracting out of functions to the private sector, with gains in efficiency.

Problems

6.

- i. A good deal of effort has already gone into the reduction in Civil Service numbers to 630,000 by April 1984. Further substantial cuts will be hard to achieve unless Ministers are prepared to give up significant aspects of their present functions.
- ii. A separate manpower target can lead to inefficiencies, where it might be more cost-effective to employ staff (eg on social security fraud cases); and if the reduction of unemployment remains a prime objective, any such inefficiencies conflict with that objection.
- iii. In the NHS, given the decentralised system of control and the high proportion of staff closely involved in patient care, it will be alleged that any sizeable cut will mean a reduction in the quality of service.
- iv. In the local authorities, if the target is to go beyond exhortation some mechanism will be needed for enforcement, with familiar difficulties.

ACCOUNTING CHANGES

a. Local Authority Expenditure. Local authorities at present have a large degree of autonomy, including the right to spend more than the Government's current spending target if they raise the money locally (by rates) to pay for it. Ministers have been considering this in MISC 79. If they decide not to impose direct central control over current spending, there is a case for counting as "public expenditure" only that part of local authorities' spending which is not financed from local revenues - as for nationalised industries and water authorities now, and local authorities in many other countries. This would be easier to justify if there were a limit on Exchequer grant, and non-domestic rates, so that expenditure beyond those limits was entirely a "charge" on local ratepayers/electors for extra services provided; both these changes are under consideration in MISC 79.

b. National Insurance Fund. More than half (£19 bn) of social security payments are met from contributions to the Fund. This will increase with the new State pension scheme, where public expenditure will vary according to the number "contracted out". In other countries contributory benefits are often treated "off-budget" rather than as part of public expenditure. The case for such a change would be stronger to the extent that contributions are regarded as different from ordinary direct taxation, and as buying an "entitlement" to benefits.

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C(82)

September 1982

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CABINET

LONGER TERM OPTIONS

Memorandum by the Central Policy Review Staff

1. The Chancellor's paper (C(82)) examines the prospects for public expenditure in the longer term and proposes a new and fundamental look at public spending programmes. The CPRS has been asked to point up some of the long term options open to the Government, especially as regards the possibilities for major structural changes affecting the larger expenditure programmes.
2. This presents an unusual opportunity for the Government to review prospects over the rest of the decade and beyond, and to consider any major changes of direction. We have therefore examined each of the four main programmes and suggested what changes of approach Ministers might wish to consider. Each of these involves a major shift of policy, so that Ministers may well not wish to decide the issue now, but instead to arrange for a full review to report within say six months for collective consideration and decision then.
3. Although these four programmes together cover nearly two-thirds of total public expenditure, there may well be room for radical changes of direction in other areas also. Some of these are mentioned briefly in Annex H, so that Ministers can consider whether they want more work done on them (beyond the reviews already taking place in some areas).
4. There is one area, public service manpower, where we believe collective consideration might be valuable, and this is discussed in Annex J. A related objective might be to reduce public spending by holding the relative costs (including wage costs) of public services below the rest of the economy. But the projections by officials already assume public service wages falling relative to 'market sector' wages, by 10 per cent or more in the decade to 1990, and it seems

unrealistic to suppose that a further large permanent shift could be achieved. In any case this turns on future wage negotiations, and we see no distinct 'policy option' which could usefully be reviewed at this stage.

5. In considering the main options, we suggest that Ministers will wish to measure them against several objectives:

- i. to improve incentives by reducing the burden of taxation;
- ii. to increase freedom of choice;
- iii. to ensure that those who demand public services appreciate their cost by requiring them to pay;
- iv. to allow increasing demands to be met by market sources rather than constrained by public expenditure limits;
- v. to maintain or increase efficiency;
- vi. (as a minimum) to reduce the nominal total of public expenditure, even without any of these consequences. (This might well be dismissed as 'cosmetic', but two possibilities are discussed in Annex K.)

If Ministers decide that any of the options should be fully reviewed, we suggest that part of the purpose of the review should be to examine how they measure up to these broad objectives. The main points are briefly mentioned in each of the Annexes, but it may be useful to describe here our broad approach to the four main programmes.

Health

5. As living standards rise, individuals are likely to demand more and better health care. There is some social gain from improved health care, but mainly it is a matter of individual wants and choices (income-elastic demand). Hence it is arguably not appropriate for public finance, and puts a strain on the Exchequer by distorting choices and shifting the burden from consumer to taxpayer. Public health services also tend to be led by producers rather than consumers.

6. It is therefore worth considering aiming over a period to end the State provision of health care for the bulk of the population, so that medical facilities would be privately owned and run, and those seeking health care would be required to pay for it. Those who could not afford

to pay would then have their charges met by the State, via some form of rebating or reimbursement. As an exception to the general rule of private provision, it might be judged more efficient for the State to continue to provide institutional care for long-stay patients (mentally handicapped, elderly) who clearly could not afford to contribute, rather than contracting this out wholly to private institutions with full reimbursement.

7. This would of course mean the end of the National Health Service. It would also mean leaving to individuals how far they insured against facing high costs of health care, and it would be important to monitor the growth of private health insurance over the intervening period. Given that the State would in the last resort meet the costs of necessary health care, there could be a danger of under-insurance by a large part of the working population, and thought might therefore have to be given to a scheme for compulsory private insurance.

8. If Ministers accept the broad concept as a longer-term objective, they will want to judge more immediate health options as steps along the road. In particular they will want an examination of how far the switch from public to private provision of health care could be promoted, and whether there are any institutional changes, within the NHS, which could make this switch easier.

9. There has been a departmental review of health service financing options earlier this year. But in this broader context we consider there is a case for a fuller review of two options, as stages towards the longer-term objective:

- (i) Increased and extended health charges (Annex A)
- (ii) Private health insurance (Annex B)

Education

10. The demand for education, as for health, is likely to be 'income-elastic' - as living standards rise, people will want to spend a higher proportion of their income on more and better education for their children, and will be increasingly frustrated by the lack of any way of making this choice effective within the State primary and secondary system. In addition, however, there is a social interest, arguably greater than in health, in the quality and quantity of education, because these will determine the capacity and versatility of the next

generation of working people. Hence in our judgement it is probably not realistic to envisage, even as a long-term option, the wholesale privatisation of provision for education in schools. However, it may well be desirable to make higher education more market-oriented, giving more choice to consumers and making the system more responsive to the needs of both students and employers.

11. We therefore assume that the State will continue to provide universal education facilities for children of primary and secondary school age, and to be concerned about quality. But the parallel system of private-sector schooling will remain, and may expand with increasing prosperity. More parents could be encouraged to choose the private sector, at the margin, by schemes for vouchers or tax relief; but if such schemes simply relieve parents of part of the cost of education, they are bound to be expensive for the tax payer. Hence as radical options for schools education, we have examined a drastic reduction in the resources going to the public sector (Annex C), and compulsory charges for schooling (which could be combined with vouchers - Annex D). For higher education (where most of the provision is already private-sector though publicly financed) we have examined charging the full cost of tuition (Annex E).

Social Security

12. The present system indexes most benefits to prices, and a very large number of beneficiaries (9m pensioners, 3m unemployed etc) have the real value of their benefits preserved, even at times when the working population has to suffer a cut in living standards. The Government probably cannot avoid recognising preservation of real value as a benchmark (as for tax thresholds). But it could avoid any commitment to prolong the link between benefits and prices, and take the first legislative opportunity to break the link. With inflation down to a much lower level, the assurance of full protection is arguably less necessary. Given discretion to hold benefits below inflation, it could make a once-for-all cut as a contribution to reducing the tax burden. It would also, of course, have discretion to allow beneficiaries a share in increased prosperity when economic conditions improve, by increasing benefits ahead of prices. This option is examined in Annex F.

Defence

13. The United Kingdom has been struggling to maintain its NATO commitment, when many other NATO members have not done so. The share of defence spending in GDP in the UK is among the highest, and this

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arguably reflects some failure in the UK to adjust to poor economic performance and a reduced role in the world. There are serious and complex issues here which Ministers may wish to consider:

- could there be greater emphasis on mutual defence with fairer sharing arrangements?
- should there be a link between European defence (BAOR) and EC budget negotiations?
- if a reduced role has to be accepted, does this have implications for FCO and aid spending as well as defence?

Some of these issues go outside the defence area and are mentioned elsewhere (Annex H). Annex G concentrates on the option of halting the real growth of defence spending after 1985/86.

General

14. On the main options as described in Annexes A-G, there are some general points to make:

(a) Some options may lead to an increase in the amount of real resources (including labour) devoted to these services. Charges for education and health, for example, might have the effect of increasing the resources consumed by those services, if people chose to buy more of them. So long as the services are provided within the public sector, we think that Ministers will wish to see the claim which they make on resources reduced. But where people choose to pay more for private sector services, they should be free to do so.

(b) Some of the options involve higher charges for services, and these raise difficult questions about incentives. Assuming no change in the existing tax and social security systems, charging for the full cost of services would cause a massive redistribution of income, in general away from families to people without children. This would exacerbate poverty to a level which we assume Ministers would judge unacceptable. To the extent that it is desired to adjust for these effects, changes in the charging, benefit or tax systems would be needed. If charges were rebated or reimbursed to those below some income threshold, the inevitable result would be high marginal 'tax' rates at the bottom of the scale. This adverse effect on the incentive to find a job or earn more would offset the gain from lower direct tax rates made possible by the expenditure saving.

A form of graduated income support, probably requiring a fully integrated system for combined tax and benefits, would be preferable; but even then there might be little or no overall gain in incentives, though the effect would be distributed more smoothly up the income scale. If minimal charges for schooling or health insurance were compulsory, they would only reduce the aggregate burden of taxation in a nominal sense; but they could allow more people to make their own decisions at the margin (analogous to a shift from direct to indirect taxation).

(c) Some of the options would make some people worse off. But it is very difficult - in many cases impossible - to effect changes in the role of Government without making some people worse off, particularly where public expenditure and hence taxation are involved. It is therefore necessary to accept that possibility, whilst always recognising that it is the proper function and duty of Government to ensure that no one is made so much worse off that he or she is subjected to undue hardship. If poverty is thought of as a relative condition, adverse redistributive effects become hard to accept. If, however, it is recognised that there is such a thing as an absolute condition of poverty from which people should be protected and that poor people should share in the increasing wealth of the country, but perhaps not in full proportion, then some redistributive effects can be accepted - as they must be if the amount of wealth available for distribution is to increase.

Conclusion

15. Ministers are invited to decide -

(i) whether they wish to commission full strategic reviews of any of the main options discussed in Annexes A - G (which give order-of-magnitude estimates of savings):

- A increased health charges
- B private health insurance
- C reduced education spending
- D charges for schooling
- E charges for higher education
- F de-indexation of social security benefits
- G a halt to growth in defence spending after 1985/86;

(ii) whether they want to include additionally any of the possibilities listed in Annexes H, J (manpower), and K (accounting changes).

CHARGING FOR HIGHER EDUCATION

Proposal

1. A significant saving could be achieved by charging degree students at universities etc for their degree courses. The size of this saving would depend on the amount of State assistance it was decided to make available to higher education students; but £1 bn a year could be saved by charging the full cost of degree courses, while still providing assistance in the form of scholarships and/or State-guaranteed loans to, say, 300,000 students (the exact number of students who could be assisted for the same cost would depend on the way this assistance was distributed as between scholarships and loans).

Background

2. On present projections, there will be about 450,000 students in higher education in 1985-86 of whom 35,000 will be from overseas. The cost of providing courses to these students varies considerably as between the arts and sciences but the average cost (at 1980-81 prices) of a university course is about £4,000 per year and that of a polytechnic is £3,000. At present, all State-assisted institutions of higher education charge all United Kingdom resident students the same fees, (£480); these are met by a grant of £480 from the local authority. The rest of the cost is met by central government grants to universities (£1,263 million in 1982-83) and to other advanced further education institutions (£538 m); although some of this expenditure is for research.

3. Under this proposal, universities and other higher education institutions would receive no funds direct from government (except for research) but would be funded entirely through student fees, plus any outside endowment funds they could raise.

4. This proposal is distinct from the scheme for replacing present maintenance grants, for students' living expenses, with State guaranteed loans, which would only save some £200 m a year. But the two schemes could be combined, by offering loans to cover both tuition costs and maintenance.

Arguments in Favour

5.

i. Charging full cost fees would increase the pressure on institutions of higher education to recruit students and add the dimension of "value for money" to decisions about higher education. This would make them more responsive to the demands of potential consumers, as well as more conscious of the need to control costs and to improve the quality of their "products" (eg it might encourage the development of two-year courses).

ii. More competition between students, for a smaller amount of Government aid, should lead them to appreciate the full value of their courses and to take them more seriously. It would encourage students to seek financial support from non-governmental sources (eg industry) or to find ways of supporting themselves eg by working part-time, during vacations, before going to university, during years-off between academic years etc.

iii. It would encourage closer links between institutions of higher education and industry and commerce. The universities would have to make greater efforts to seek financial support from industry while firms would want to safeguard their share of the supply of trained manpower. They could do this by providing scholarships to able students who would be required to work for their "supporting" firms for a limited period after having received their degrees.

iv. To the extent that universities etc did not meet demands and raise finance for themselves, they would need to cut back on teaching resources, and student numbers would fall.

Problems

6.

i. This proposal would attract fierce opposition from the academic community, as giving rise to fluctuating demands and making planning impossible.

ii. If the effect of this proposal were to be a significant reduction in total student numbers, this could mean a less qualified work force. But charging for degree courses could lead to more students choosing "industrially-relevant" courses or more mid-career study and this should have beneficial effects on economic performance.

iii. Those who did not qualify for any form of State assistance and did not manage to secure support from industry or other private sources could face a bill of at least £12,000 (or more if maintenance costs were included) for a 3-year degree course. The burden of servicing and paying off a loan of this scale would be a considerable disincentive to higher education.

iv. Because higher education is effectively a life-long investment, those who borrow to finance it would wish to be able to repay their loan over long periods. There could be difficulty in developing a private sector market for such long-term student loans.

v. This proposal might encourage many students to seek higher education in those EEC countries in which fees are subsidised, with some resulting permanent loss of highly skilled manpower.

vi. As science and technology courses are likely to be very much more expensive than arts ones (unless the universities decide to subsidise the former from fees earned from the latter), students might consider the arts courses better "value for money" in terms of potential career advancement, and it might be difficult to attract enough students to the most expensive courses such as medicine.

INCREASED CHARGES FOR HEALTH SERVICES

Proposal

1. The National Health Service (NHS) would remain broadly as now but a higher proportion of costs would be met from charges to patients. Existing charges for drugs, dental treatment and spectacles would be raised, and extended to cover everyone (including children and old people), except those close to supplementary benefit level. A modest charge would be introduced for consulting the general practitioner, and for hospital outpatient visits. Hospital inpatients would also pay a modest charge (say £5 a day). Total savings would ~~savings would~~ depend on the scheme of charges adopted, but would be unlikely to exceed £1 bn a year, even with a drastic reduction in exemptions.

Background

2. Expenditure on the family practitioner services this year is expected to be £2.4 bn, one-eighth of which (£300 m) will be recovered in charges. There are no charges for NHS hospital treatment, which will cost £8.8 bn this year. Demand for all services is expected to increase steadily, partly because the number of the very elderly will increase up to 1990; and the cost of the NHS rises in real terms because it is labour intensive and because scientific advance leads to better but usually more expensive forms of treatment. The number of people covered by private insurance is growing but still represents less than 10 per cent of the population.

3. Increasing the proportion of costs recovered through NHS charges clearly lessens the distinction between NHS and private treatment; and the logical conclusion of the process would be the abolition of NHS entitlement for certain groups of patient. Under a variant of the proposal above, therefore, drugs, spectacles and dental treatment would no longer be provided under the NHS except to limited exempt groups. The rest of the population would have to make private arrangements with the pharmacist, optician or dentist.

Arguments in favour

4.

- i. The proposal leaves the basic structure of the NHS intact.
- ii. Patients and others would be more aware of the high costs of medical treatment; unnecessary use of the service would be discouraged; and public opinion might act more powerfully to hold down NHS costs (including wage rates).
- iii. Heavier NHS charges would, at least modestly, stimulate the growth of private medical insurance and thus relieve pressure on the NHS. Hence it could be seen as a preparatory move before full privatisation (Option D).

Problems

5.

- i. To save substantial sums involves raising existing charges and breaking unpopular ground in three areas - imposing charges (eg for drugs) on patients who are now exempt (eg children); charging for seeing the general practitioner; and for hospital treatment.
- ii. It would cost money and staff to collect new categories of charges, and to carry out means tests (a taper would be necessary above supplementary benefit level). Some of the staff involved (eg general practitioners) would object strongly.
- iii. People who genuinely needed treatment might be discouraged from seeking it.
- iv. As long as the poorest are exempted from charges, increasing the charges would automatically increase the poverty trap - ie makes it less attractive for people to increase their earnings at the margin.

CHARGING FOR SCHOOLING

Proposal

1. Parents able to afford it would be required to pay the cost of their children's education, whether in the State system (where schools would be required to charge fees which covered their costs) or in competing private schools. It would still be compulsory to have children educated, normally at a school which met statutory minimum educational standards. Those with incomes too low to afford to pay would either have fees rebated or (preferably) would be subsidised via some form of income support.

Background

2. Schools expenditure this year is £7.4 bn, or 6½ per cent of total public expenditure. Nearly all of this is spent by local authorities at their own discretion, and it is about a third of their total current spending. The average cost per pupil is about £950 a year. Numbers of pupils will decline to 1990, and hence spending is projected to fall (but less than proportionately). Education in maintained schools will remain one of the largest social services, with private-sector education for compulsory school-age pupils (at present 5 per cent of all such pupils) remaining small.

3. A scheme for issuing vouchers to parents is sometimes suggested, as a less radical alternative to charging. It could help to promote wider choice, and would make it cheaper to send children to private schools if vouchers had a reimbursable "face value". But it would do nothing to reduce public expenditure, unless as an adjunct to charging with vouchers covering less than the full costs. Indeed there would be increased expenditure to meet any reimbursement for private education. Hence it is not put forward as an option here.

Arguments in Favour

4.

i. The saving could be as large as £3-4 bn, depending on the scale or rebating and whether it counted as public expenditure.

ii. Parents who wanted to secure a higher-quality education for their children, and were prepared to spend more, could do so by shopping around within the State sector or by going to private schools (and they would no longer be contributing to the cost of State schooling via central and local taxation). As real incomes rise, it is right to allow more resources to go into education to the extent that parents wish to purchase more and better schooling for their children.

iii. State schools would need to become more competitive and cost-conscious, and to pay more attention to parents' concerns (examination results, vocationally relevant courses, etc).

Problems

5.

i. There would be formidable political and administrative problems. Some mechanism would be needed for compelling local education authorities to charge "adequate" fees, which would entail new powers of central control and if necessary take-over.

ii. Cost differences do not only reflect differences in quality, and in particular schools in inner city areas tend to have higher costs. Some form of central government equalisation grant would probably still be needed to offset this.

iii. Students taking A-level courses in further education colleges would also be required to pay fees (to match the treatment of sixth-formers in schools). This would increase the discrimination between those in further education colleges undergoing training (on training allowances) and those on "school equivalent" courses (paying fees).

iv. There would be a wholesale redistribution of disposable income from paying parents to tax-paying non-parents. One way to offset this would be to raise child benefit to cover (standard) school fees, but this would

defeat the main object of reducing public expenditure and taxation. An alternative would be to re-introduce child tax allowance, but this would be sharply regressive, helping only parents with taxable incomes.

v. Given that fees would need to be rebated for parents with low family incomes, this would inevitably mean high marginal "tax" rates at the bottom of the scale, with bad effects on poverty trap and in-work/out-of-work incentives. Hence a form of graduated income support, on "negative income tax" lines, would be preferable - but previous tax credit schemes have been extremely costly, and the basic disincentive effect would remain, however distributed up the income scale.

vi. Since children could not be refused schooling, the business of collecting fees would be difficult and administratively expensive.

PRIVATE HEALTH INSURANCE

Proposal

1. The working population would be obliged by law to obtain insurance to cover the costs of health care for themselves and their dependants. Premiums would relate to the family's risks, not their means, and so the poor would need help with meeting the costs. Either initially or later the scheme could be extended to cover the non-working population, who would obviously need much more subsidy.

Background

2. Expenditure on the NHS this year is some £11.7 bn. The main components are some £2.1 bn (net of charges) for the family practitioner services (the services provided by family doctors, dentists, opticians and chemists); and £8.8 bn for hospital and community health services. Demand for all services is expected to increase steadily, partly because the number of the very elderly is increasing; and the cost of the NHS rises in real terms because it is labour intensive and because scientific advance leads to better but usually more expensive forms of treatment.

3. It would be prohibitively expensive to insure against the costs of long-term medical care and so, as in all countries, the state would have to continue to provide for certain types of patient (eg the mentally handicapped). Even so, it is estimated that the cost of basic medical cover for an average family of four would be about £600 a year. Those below average earnings (and possibly others) would need help with these costs and to the extent that this had to be channelled through payments rather than tax reliefs (since the poorest do not pay income tax), the public expenditure savings would be lessened. It is difficult to envisage a scheme which would reduce public expenditure on the NHS by more than say a third (£4 bn).

4. Within an insurance-based system, providers of health care (eg doctors) could be encouraged to set up companies to offer health care to clients in return for an annual subscription. Limited American experience with such Health Maintenance Organisations suggests that they may help to restrain costs.

Arguments in favour

5.

i. This proposal offers the prospect of a very large cut in the costs of health care to the taxpayer.

ii. The public would have its horizon of choice and of responsibility greatly widened.

iii. Patients could (within the limits imposed by their insurers) shop around for health care, so that doctors and hospitals would have to be more responsive to patients' wishes if they wished to stay in business.

iv. Although initially at least NHS hospitals could remain in state ownership, trading like nationalised industries, they could be progressively privatised. This would give much more scope for experiment and for variety in such matters as rates of pay reflecting local market conditions.

Problems

6.

i. Even though a free state service would be retained for the uninsured and possibly for the non-working population, for the majority the change would represent the abolition of the NHS. This would be immensely controversial.

ii. There would be transitional problems in persuading insurance companies to take on the risks before cash reserves had been built up to meet them.

iii. While this proposal would reduce the amount of public money spent on health, it would not reduce the community's spending on health care; on the contrary it would probably increase sharply. Some of this would be consumers' preference for higher quality, shorter delays etc. But judging by overseas experience, the providers of health care would also take advantage of the ever buoyant demand and of the inability of patients or of insurance companies to control costs, or in most cases to make informal judgments about the medical treatments on offer. Competition between doctors and hospitals would be on quality more than price.

iv. Providing help for those unable to afford the insurance premiums would raise vast difficulties. All claimants (perhaps over half the adult population) would have to be means-tested and even if the help were graduated, on negative income tax lines, there would be a sharp disincentive effect; increasing one's earnings, or moving into work from unemployment, would become less attractive.

v. Patients would face extra complications (form-filling etc). Patients or their insurers would need to be invoiced for treatment, and subsidies of some kind would need to be provided to a large part of the population. It would also be necessary to police the compulsory insurance system.

CUTTING THE REAL VALUE OF SOCIAL SECURITY BENEFITS

Proposal

1. The present laws which require most benefits to be increased annually by at least as much as prices would be repealed. New legislation would bring these benefits into line with the present arrangements for child benefit: upratings would become a matter of discretion for the Secretary of State who would attempt to preserve their real purchasing power but only as far as economic circumstances permit. If desired the Government could take the opportunity during the first year of operation of the new legislation to uprate some or all benefits by amounts which would effect substantial, once-for-all cuts in the real value of benefits. The bolder these initial cuts were the less need there would be in future years to hold down upratings below the level of inflation.

Background

2. Social Security expenditure in the current year is estimated at £32 bn, (28 per cent of total expenditure). In the three years to 1981-82 social security expenditure rose by 74 per cent, whilst public expenditure in total rose by 61 per cent; but the disproportionate increase was in large part due to the rise in the number of unemployed receiving benefit. At present most benefits must by law be increased annually at least in line with prices. Since 1972 the basic retirement pension has risen by 28 per cent in real terms while real national disposable income has risen by some 10 per cent. (Nearly all this very large improvement in the value of the pension occurred before 1979).

3. For the purpose of illustration, this option would yield some £3 bn a year by 1990-91 if a 10 per cent reduction in the LTPE projections is assumed. The effect on the real value of benefits depends on future economic performance. On the poor performance case - where the LTPE projections assumed that benefits would be maintained in real terms - benefits in 1990-91 would be 10 per cent below their current level in real terms. On the improved

economic performance case - where the LTPE projections assumed a 1 per cent per annum real improvement in social security expenditure ie increased real value of benefits and coverage - benefits in 1990-91 would perhaps be only a little below their existing real value.

Arguments in Favour

4.

i. The real increases in benefit rates during the 1970s have imposed a very large extra burden on the tax payer and those in work. Implementing the proposal could produce very large savings in public expenditure and lighten the burden on employers and the working population. In relation to the 1982 uprating each 1 per cent point reduction would have saved about £0.3 bn in public expenditure, a third of this being reflected in a reduction in the employer's contribution to the National Insurance Fund.

ii. The reduction in the real value of benefits for those of working age would increase incentives to work and increase the attraction of low-paid jobs.

iii. There would be a consequential saving on public service occupational pensions (eg those for civil servants, local government employees, NHS staff, the armed forces). This is because increases in these occupational pensions are statutorily linked to increases in the state retirement pension. A 10 per cent reduction in the value of these public sector pensions would yield about £300 m a year.

Problems

5.

i. Cutting the real value of benefits would be unpopular, particular in relation to the benefits for pensioners where the largest savings can be made. Pensioners would receive a lower share of the nation's wealth than

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ANNEX E (cont 2)

they do now , at least until the benefits of the new pension scheme become significant (after 1990); this would contrast starkly with what Labour once provided (upratings based on higher prices or earnings).

ii. There would be an increase in real poverty and current problems of social deprivation would be worsened (crime, poor care of children, illness from cold homes and poor nutrition etc).

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CUTTING EDUCATION SPENDING

Proposal

1. Spending on compulsory education for 5-16 year olds would be cut by about £1 bn a year while every effort would be made to maintain essential standards.

Background

2. Economies should be possible across the range of school provision by concentrating on the essentials and cutting out the peripheral. The process would need to start from an analysis of what schooling is intended to achieve and how the important outputs could be maintained at lower cost. Since 70 per cent of expenditure represents teachers' salaries (£4 bn a year at current prices), it would be impossible to achieve a £1 bn reduction without reducing teacher numbers substantially. But the pupil/teacher ratio in both primary and secondary schools has fallen dramatically since the end of World War II, for example in England between 1950-81 when it fell from 31 to 23 in the primary sector and from 22 to 17 in secondary schools. Although it is often claimed that the pupil/teacher ratio is a measure of the "quality" of education, the relationship between this ratio and academic student performance is far from straight-forward. At present the number of teachers is around 520,000, and the LTPE projections imply a fall to around 440,000 by the end of the decade, roughly in line with the fall in pupil numbers.

Arguments in Favour

3.

i. It would provide an opportunity to weed out the lower qualified and less satisfactory teachers, and achieve a more efficient teaching force, supported by modern information technology to supplement class-room teaching (eg cassette teaching, audio-visual aids, modular courses etc).

ii. The closure of wasteful poorly attended schools with small classes would be speeded up.

iii. Schools would be required to concentrate, particularly at secondary level, on a "core" of academic and vocational subjects, cutting down resources on other non-academic activities (unless on repayment).

Problems

4.

i. Some mechanism would be required for compelling local education authorities to make the planned cuts, eg in teacher numbers. This would entail new powers of central control, with a fall-back power to take over the functions of LEAs.

ii. There would be other formidable problems in implementing this proposal. In particular -

a. Unless the curriculum were severely pruned - see 3 iii above - schools could be left with a core of teachers each of whom would be required to teach a wide range of subjects.

b. There would be major resistance from the teaching profession.

c. There would be considerable redundancy costs.

iii. There might be a significant fall in the overall quality of education provided by the State system, even if this fall were not immediately reflected in public examination results.

iv. Pupils would have to work more on their own and this could have deleterious effects on classroom discipline and on the morale and achievement of the less able. On the other hand, it might help those who go on to higher education.

v. This approach is distinct from, and probably not compatible with the charging approach discussed in Annex C.

DEFENCE

Proposal

1. LTPE projections assumed that defence spending would increase in volume terms by 3 per cent a year from 1982-83 until 1988-89, with 1 per cent a year thereafter. The United Kingdom commitment to the 3 per cent growth target currently runs only to 1985-86. The proposal is to maintain the 1985-86 level in real terms, which would save about £1½ bn a year by 1990-91 as against LTPE. Internal forward planning in the Ministry of Defence currently assumes no growth in the defence budget after 1985-86. Hence this option could be achieved either by providing for no additions to spending at present planned, or by reductions to make room for some inescapable additions, eg by cancelling Trident. But the present planning assumption is deliberately cautious, to allow for some flexibility, so it does not follow that the option could be achieved without affecting military capabilities.

2. The political and diplomatic difficulties of this option would be reduced if NATO could be persuaded to reduce the 3 per cent target to a level which all or most member countries could realistically be expected to achieve.

Background

3. The present defence base-line is uncertain, in relation both to the level of spending in 1982-83 and to any revisions of plans in the immediate aftermath of the Falkland conflict. But defence spending cannot be ignored in this exercise. It now accounts for about 12 per cent of total public expenditure programmes, and on the basis of the LTPE assumptions (including the assumption that defence prices rise 2 per cent faster than prices generally) it will account for 15 per cent in 1990-91. On these projections, defence is responsible for more than a third of the total expenditure increase (in cost terms) from 1982-83 to 1990-91 - a much larger share than any other programme - though a different base year, or a different assumption about relative prices, would give different results.

Arguments in Favour

4.

i. If defence spending is not slowed down, it will continue to rise in relation to GDP, to around 6 per cent on the projection we have taken. Sooner or later, depending on the performance of the economy, this rise is very likely to be found unsustainable, so that drastic cuts will have to be made. It would be more sensible to plan from the outset for a sustainable rate of defence spending, as in the proposal.

ii. In the past a number of other countries have failed to meet the NATO target (even among those with GDP growth rates higher than the United Kingdom), and after 1980 (the last year for which comparative figures are available) their performance is likely to continue to fall short.

iii. The lower expenditure path would be feasible. It would be broadly in line with the forward planning now being undertaken in the MOD (though this deliberately leaves room for flexibility - para 1). Spending with British industry could still be higher than it is today (£6-7 bn per annum).

iv. A lower rate of spend on defence R & D would free scarce resources (high-quality scientists and engineers) for employment in civil R & D.

Problems

5.

i. There would be political problems, international and domestic, in changing course after 1985-86. Last year the United Kingdom supported the NATO Ministerial Guidance extending the commitment to 1988. Present political pressures are for more defence spending, not less.

ii. The absence of real growth in the defence budget, as against the increase in complexity and cost of major equipment, would entail a reduction in United Kingdom military capabilities.

OTHER PROGRAMMES

1. There is a number of other programmes which have not be included in the list of major options - either because there is no policy issue worth a full-scale review, or because the programme is too small to offer cuts approaching the £1 bn a year threshold, or both.

2. These programmes could nevertheless offer scope for very significant reductions in public expenditure, either by a generalised squeeze or by identifying policy changes. Following is a list of smaller possible areas where there may be scope for review, with figures for present annual spending (in 1980-81 cost terms, from the LTPE report) -

i. Export credits - the LTPE figure of £0.3 bn does not reflect the full extent of commitments, and there may be scope for review.

ii. Employment - £2.2 bn - much of this reflects policy reactions to the state of the labour market and will continue to do so; but there might be some scope for review:

- the Youth Training Scheme might take the place of the last year of compulsory schooling, instead of following it;

- on the training side, a remissible training tax on employers would reduce public expenditure;

- on employment services, privatisation of job centres might be examined.

iii. Regional - counting together expenditure by the Departments of Industry and Environment, this is of the order of £1 bn a year, and is already being reviewed.

iv. Housing - £2.9 bn - has been falling, but the future trend depends mainly on the real level of rents (as well as rate of sales, new building and improvements); a review of rent policy, and of relating subsidy to current rather than historic values, might be worthwhile (though most of the savings would not count as public expenditure).

3. Some other significant areas are -

i. Payments to European Communities - £1.8 bn - depends on future negotiations (in which it maybe necessary to bring in the possibility of alternative defence savings, eg in BAOR).

ii. Other local authority services - £10 bn - there may be more scope for increased contracting out and/or charging, analogous to charging for education (Annex C).

iii. Nationalised industries - £2.3 bn: - privatisation will generate once-for-all gains, but where industries sold are self-financing will have a nil or negative effect on total EFLs thereafter; - continuing deficits might be removed or reduced in the longer term, but this is bound to be a difficult and piecemeal process.

iv. Scotland, Wales, Northern Ireland - £10 bn - extra spending in Scotland in relation to needs has been investigated in the past, and is probably not worth a further full-scale review.

PUBLIC SERVICE MANPOWER

Proposal

1. Ministers would decide on a target for further reduction of civil service manpower, by say 10 per cent during the next Parliament. This would entail giving a high priority to -

- reducing functions, contracting out etc;
- simplifying policies and procedures (tax, social security etc);
- legislation where necessary to achieve these changes;
- expenditure on information technology.

The overall reduction would be allocated among departments and services according to the scope for such changes.

2. Similar targets would also be set for reductions in NHS and local authority manpower. These could be linked with increasing contracting out and privatisation of services.

Background

3. The pay bill for the civil service (industrial and non-industrial) is about £5 bn this year. Numbers will already have been reduced by about 14 per cent since 1979, so that the scope for further reduction merely by a continuing squeeze on numbers is likely to be small. Hence the need for more radical changes in functions and policies.

4. In principle there should be room for at least equal savings in other public services. The NHS employs approximately 1 million people, and numbers increased by 5 per cent between 1979 and 1981. The Government has set targets for reductions in management costs as a proportion of NHS resources over the next three years (in England, a cut of 10 per cent). Local authorities employ about 2 million people, and have reduced numbers by about 3 per cent since March 1979 - mostly in the education service, which employs nearly half the total (hence there is an overlap with Annex F).

Arguments in Favour

5.

- i. Over the rest of this decade, information technology will yield further economies in data processing, storage etc. It is already being applied to Government administrative operations, but the pace could be accelerated.
- ii. To achieve anything like a further 10 per cent reduction in civil service numbers would mean a radical review of present functions to achieve contracting out or privatisation of those services where economic costs might be charged (eg ^{say} PSA, ^{or} ADAS). This would be in line with Ministers' objective of "rolling back the frontiers of the public sector".
- iii. Very worthwhile savings might be achieved by subjecting NHS and local authority manpower to the sort of squeeze which has proved successful in the civil service. Pressure on numbers should lead to the contracting out of functions to the private sector, with gains in efficiency.

Problems

6.

- i. A good deal of effort has already gone into the reduction in Civil Service numbers to 630,000 by April 1984. Further substantial cuts will be hard to achieve unless Ministers are prepared to give up significant aspects of their present functions.
- ii. A separate manpower target can lead to inefficiencies, where it might be more cost-effective to employ staff (eg on social security fraud cases); and if the reduction of unemployment remains a prime objective, any such inefficiencies conflict with that objection.
- iii. In the NHS, given the decentralised system of control and the high proportion of staff closely involved in patient care, it will be alleged that any sizeable cut will mean a reduction in the quality of service.
- iv. In the local authorities, if the target is to go beyond exhortation some mechanism will be needed for enforcement, with familiar difficulties (cf Annex F).

ACCOUNTING CHANGES

a. Local Authority Expenditure. Local authorities at present have a large degree of autonomy, including the right to spend more than the Government's current spending target if they raise the money locally (by rates) to pay for it. Ministers have been considering this in MISC 79. If they decide not to impose direct central control over current spending, there is a case for counting as "public expenditure" only that part of local authorities' spending which is not financed from local revenues - as for nationalised industries and water authorities now, and local authorities in many other countries. This would be easier to justify if there were a limit on Exchequer grant, and non-domestic rates, so that expenditure beyond those limits was entirely a "charge" on local ratepayers/electors for extra services provided; both these changes are under consideration in MISC 79.

b. National Insurance Fund. More than half (£19 bn) of social security payments are met from contributions to the Fund. This will increase with the new State pension scheme, where public expenditure will vary according to the number "contracted out". In other countries contributory benefits are often treated "off-budget" rather than as part of public expenditure. The case for such a change would be stronger to the extent that contributions are regarded as different from ordinary direct taxation, and as buying an "entitlement" to benefits.



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From: John Sparrow

Qa 06045

Covering CONFIDENTIAL

31 August 1982

The Rt Hon Sir Geoffrey Howe QC MP
HM TREASURY
S W 1

Dear Geoffrey,

Longer Term Options

In the light of your comments at the meeting last Friday, we have re-cast our draft paper for 9 September, to make it more of a fundamental review of options for the main programmes, and less a list of possible cuts.

I enclose the revised draft. If you are content with it as a basis for collective discussion, I will arrange for it to be circulated. Otherwise I would of course be very glad to have another word with you about it.

You told me that you would be discussing the handling of the meeting with the Prime Minister, and I am accordingly sending a copy of this draft to her. I am also sending a copy to Sir Robert Armstrong.

Yours sincerely,

John.

John Sparrow

Enc



with compliments

Mr Scholas

We spoke.

Jansz Boonay

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7/ix

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C(82)

September 1982

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CABINET

LONGER TERM OPTIONS

Memorandum by the Central Policy Review Staff

1. The Chancellor's paper (C(82)) examines the prospects for public expenditure in the longer term and proposes a new and fundamental look at public spending programmes. The CPRS has been asked to point up some of the long term options open to the Government, especially as regards the possibilities for major structural changes affecting the larger expenditure programmes.
2. This presents an unusual opportunity for the Government to review prospects over the rest of the decade and beyond, and to consider any major changes of direction. We have therefore examined each of the four main programmes and suggested what changes of approach Ministers might wish to consider. Each of these involves a major shift of policy, so that Ministers may well not wish to decide the issue now, but instead to arrange for a full review to report within say six months for collective consideration and decision then.
3. Although these four programmes together cover nearly two-thirds of total public expenditure, there may well be room for radical changes of direction in other areas also. Some of these are mentioned briefly in Annex H, so that Ministers can consider whether they want more work done on them (beyond the reviews already taking place in some areas).
4. There is one area, public service manpower, where we believe collective consideration might be valuable, and this is discussed in Annex J. A related objective might be to reduce public spending by holding the relative costs (including wage costs) of public services below the rest of the economy. But the projections by officials already assume public service wages falling relative to 'market sector' wages, by 10 per cent or more in the decade to 1990, and it seems

unrealistic to suppose that a further large permanent shift could be achieved. In any case this turns on future wage negotiations, and we see no distinct 'policy option' which could usefully be reviewed at this stage.

5. In considering the main options, we suggest that Ministers will wish to measure them against several objectives:

- i. to improve incentives by reducing the burden of taxation;
- ii. to increase freedom of choice;
- iii. to ensure that those who demand public services appreciate their cost by requiring them to pay;
- iv. to allow increasing demands to be met by market sources rather than constrained by public expenditure limits;
- v. to maintain or increase efficiency;
- vi. (as a minimum) to reduce the nominal total of public expenditure, even without any of these consequences. (This might well be dismissed as 'cosmetic', but two possibilities are discussed in Annex K.)

If Ministers decide that any of the options should be fully reviewed, we suggest that part of the purpose of the review should be to examine how they measure up to these broad objectives. The main points are briefly mentioned in each of the Annexes, but it may be useful to describe here our broad approach to the four main programmes.

Health

5. As living standards rise, individuals are likely to demand more and better health care. There is some social gain from improved health care, but mainly it is a matter of individual wants and choices (income-elastic demand). Hence it is arguably not appropriate for public finance, and puts a strain on the Exchequer by distorting choices and shifting the burden from consumer to taxpayer. Public health services also tend to be led by producers rather than consumers.

6. It is therefore worth considering aiming over a period to end the State provision of health care for the bulk of the population, so that medical facilities would be privately owned and run, and those seeking health care would be required to pay for it. Those who could not afford

to pay would then have their charges met by the State, via some form of rebating or reimbursement. As an exception to the general rule of private provision, it might be judged more efficient for the State to continue to provide institutional care for long-stay patients (mentally handicapped, elderly) who clearly could not afford to contribute, rather than contracting this out wholly to private institutions with full reimbursement.

7. This would of course mean the end of the National Health Service. It would also mean leaving to individuals how far they insured against facing high costs of health care, and it would be important to monitor the growth of private health insurance over the intervening period. Given that the State would in the last resort meet the costs of necessary health care, there could be a danger of under-insurance by a large part of the working population, and thought might therefore have to be given to a scheme for compulsory private insurance.

8. If Ministers accept the broad concept as a longer-term objective, they will want to judge more immediate health options as steps along the road. In particular they will want an examination of how far the switch from public to private provision of health care could be promoted, and whether there are any institutional changes, within the NHS, which could make this switch easier.

9. There has been a departmental review of health service financing options earlier this year. But in this broader context we consider there is a case for a fuller review of two options, as stages towards the longer-term objective:

(i) Increased and extended health charges (Annex A)

(ii) Private health insurance (Annex B)

Education

10. The demand for education, as for health, is likely to be 'income-elastic' - as living standards rise, people will want to spend a higher proportion of their income on more and better education for their children, and will be increasingly frustrated by the lack of any way of making this choice effective within the State primary and secondary system. In addition, however, there is a social interest, arguably greater than in health, in the quality and quantity of education, because these will determine the capacity and versatility of the next

generation of working people. Hence in our judgement it is probably not realistic to envisage, even as a long-term option, the wholesale privatisation of provision for education in schools. However, it may well be desirable to make higher education more market-oriented, giving more choice to consumers and making the system more responsive to the needs of both students and employers.

11. We therefore assume that the State will continue to provide universal education facilities for children of primary and secondary school age, and to be concerned about quality. But the parallel system of private-sector schooling will remain, and may expand with increasing prosperity. More parents could be encouraged to choose the private sector, at the margin, by schemes for vouchers or tax relief; but if such schemes simply relieve parents of part of the cost of education, they are bound to be expensive for the tax payer. Hence as radical options for schools education, we have examined a drastic reduction in the resources going to the public sector (Annex C), and compulsory charges for schooling (which could be combined with vouchers - Annex D). For higher education (where most of the provision is already private-sector though publicly financed) we have examined charging the full cost of tuition (Annex E).

Social Security

12. The present system indexes most benefits to prices, and a very large number of beneficiaries (9m pensioners, 3m unemployed etc) have the real value of their benefits preserved, even at times when the working population has to suffer a cut in living standards. The Government probably cannot avoid recognising preservation of real value as a benchmark (as for tax thresholds). But it could avoid any commitment to prolong the link between benefits and prices, and take the first legislative opportunity to break the link. With inflation down to a much lower level, the assurance of full protection is arguably less necessary. Given discretion to hold benefits below inflation, it could make a once-for-all cut as a contribution to reducing the tax burden. It would also, of course, have discretion to allow beneficiaries a share in increased prosperity when economic conditions improve, by increasing benefits ahead of prices. This option is examined in Annex F.

Defence

13. The United Kingdom has been struggling to maintain its NATO commitment, when many other NATO members have not done so. The share of defence spending in GDP in the UK is among the highest, and this

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arguably reflects some failure in the UK to adjust to poor economic performance and a reduced role in the world. There are serious and complex issues here which Ministers may wish to consider:

- could there be greater emphasis on mutual defence with fairer sharing arrangements?
- should there be a link between European defence (BAOR) and EC budget negotiations?
- if a reduced role has to be accepted, does this have implications for FCO and aid spending as well as defence?

Some of these issues go outside the defence area and are mentioned elsewhere (Annex H). Annex G concentrates on the option of halting the real growth of defence spending after 1985/86.

General

14. On the main options as described in Annexes A-G, there are some general points to make:

(a) Some options may lead to an increase in the amount of real resources (including labour) devoted to these services. Charges for education and health, for example, might have the effect of increasing the resources consumed by those services, if people chose to buy more of them. So long as the services are provided within the public sector, we think that Ministers will wish to see the claim which they make on resources reduced. But where people choose to pay more for private sector services, they should be free to do so.

(b) Some of the options involve higher charges for services, and these raise difficult questions about incentives. Assuming no change in the existing tax and social security systems, charging for the full cost of services would cause a massive redistribution of income, in general away from families to people without children. This would exacerbate poverty to a level which we assume Ministers would judge unacceptable. To the extent that it is desired to adjust for these effects, changes in the charging, benefit or tax systems would be needed. If charges were rebated or reimbursed to those below some income threshold, the inevitable result would be high marginal 'tax' rates at the bottom of the scale. This adverse effect on the incentive to find a job or earn more would offset the gain from lower direct tax rates made possible by the expenditure saving.

A form of graduated income support, probably requiring a fully integrated system for combined tax and benefits, would be preferable; but even then there might be little or no overall gain in incentives, though the effect would be distributed more smoothly up the income scale. If minimal charges for schooling or health insurance were compulsory, they would only reduce the aggregate burden of taxation in a nominal sense; but they could allow more people to make their own decisions at the margin (analogous to a shift from direct to indirect taxation).

(c) Some of the options would make some people worse off. But it is very difficult - in many cases impossible - to effect changes in the role of Government without making some people worse off, particularly where public expenditure and hence taxation are involved. It is therefore necessary to accept that possibility, whilst always recognising that it is the proper function and duty of Government to ensure that no one is made so much worse off that he or she is subjected to undue hardship. If poverty is thought of as a relative condition, adverse redistributive effects become hard to accept. If, however, it is recognised that there is such a thing as an absolute condition of poverty from which people should be protected and that poor people should share in the increasing wealth of the country, but perhaps not in full proportion, then some redistributive effects can be accepted - as they must be if the amount of wealth available for distribution is to increase.

Conclusion

15. Ministers are invited to decide -

(i) whether they wish to commission full strategic reviews of any of the main options discussed in Annexes A - G (which give order-of-magnitude estimates of savings):

- A increased health charges
- B private health insurance
- C reduced education spending
- D charges for schooling
- E charges for higher education
- F de-indexation of social security benefits
- G a halt to growth in defence spending after 1985/86;

(ii) whether they want to include additionally any of the possibilities listed in Annexes H, J (manpower), and K (accounting changes).

CHARGING FOR HIGHER EDUCATION

Proposal

1. A significant saving could be achieved by charging degree students at universities etc for their degree courses. The size of this saving would depend on the amount of State assistance it was decided to make available to higher education students; but £1 bn a year could be saved by charging the full cost of degree courses, while still providing assistance in the form of scholarships and/or State-guaranteed loans to, say, 300,000 students (the exact number of students who could be assisted for the same cost would depend on the way this assistance was distributed as between scholarships and loans).

Background

2. On present projections, there will be about 450,000 students in higher education in 1985-86 of whom 35,000 will be from overseas. The cost of providing courses to these students varies considerably as between the arts and sciences but the average cost (at 1980-81 prices) of a university course is about £4,000 per year and that of a polytechnic is £3,000. At present, all State-assisted institutions of higher education charge all United Kingdom resident students the same fees, (£480); these are met by a grant of £480 from the local authority. The rest of the cost is met by central government grants to universities (£1,263 million in 1982-83) and to other advanced further education institutions (£538 m); although some of this expenditure is for research.

3. Under this proposal, universities and other higher education institutions would receive no funds direct from government (except for research) but would be funded entirely through student fees, plus any outside endowment funds they could raise.

4. This proposal is distinct from the scheme for replacing present maintenance grants, for students' living expenses, with State guaranteed loans, which would only save some £200 m a year. But the two schemes could be combined, by offering loans to cover both tuition costs and maintenance.

Arguments in Favour

5.

i. Charging full cost fees would increase the pressure on institutions of higher education to recruit students and add the dimension of "value for money" to decisions about higher education. This would make them more responsive to the demands of potential consumers, as well as more conscious of the need to control costs and to improve the quality of their "products" (eg it might encourage the development of two-year courses).

ii. More competition between students, for a smaller amount of Government aid, should lead them to appreciate the full value of their courses and to take them more seriously. It would encourage students to seek financial support from non-governmental sources (eg industry) or to find ways of supporting themselves eg by working part-time, during vacations, before going to university, during years-off between academic years etc.

iii. It would encourage closer links between institutions of higher education and industry and commerce. The universities would have to make greater efforts to seek financial support from industry while firms would want to safeguard their share of the supply of trained manpower. They could do this by providing scholarships to able students who would be required to work for their "supporting" firms for a limited period after having received their degrees.

iv. To the extent that universities etc did not meet demands and raise finance for themselves, they would need to cut back on teaching resources, and student numbers would fall.

Problems

6.

- i. This proposal would attract fierce opposition from the academic community, as giving rise to fluctuating demands and making planning impossible.
- ii. If the effect of this proposal were to be a significant reduction in total student numbers, this could mean a less qualified work force. But charging for degree courses could lead to more students choosing "industrially-relevant" courses or more mid-career study and this should have beneficial effects on economic performance.
- iii. Those who did not qualify for any form of State assistance and did not manage to secure support from industry or other private sources could face a bill of at least £12,000 (or more if maintenance costs were included) for a 3-year degree course. The burden of servicing and paying off a loan of this scale would be a considerable disincentive to higher education.
- iv. Because higher education is effectively a life-long investment, those who borrow to finance it would wish to be able to repay their loan over long periods. There could be difficulty in developing a private sector market for such long-term student loans.
- v. This proposal might encourage many students to seek higher education in those EEC countries in which fees are subsidised, with some resulting permanent loss of highly skilled manpower.
- vi. As science and technology courses are likely to be very much more expensive than arts ones (unless the universities decide to subsidise the former from fees earned from the latter), students might consider the arts courses better "value for money" in terms of potential career advancement, and it might be difficult to attract enough students to the most expensive courses such as medicine.

INCREASED CHARGES FOR HEALTH SERVICES

Proposal

1. The National Health Service (NHS) would remain broadly as now but a higher proportion of costs would be met from charges to patients. Existing charges for drugs, dental treatment and spectacles would be raised, and extended to cover everyone (including children and old people), except those close to supplementary benefit level. A modest charge would be introduced for consulting the general practitioner, and for hospital outpatient visits. Hospital inpatients would also pay a modest charge (say £5 a day). Total savings would ~~savings would~~ depend on the scheme of charges adopted, but would be unlikely to exceed £1 bn a year, even with a drastic reduction in exemptions.

Background

2. Expenditure on the family practitioner services this year is expected to be £2.4 bn, one-eighth of which (£300 m) will be recovered in charges. There are no charges for NHS hospital treatment, which will cost £8.8 bn this year. Demand for all services is expected to increase steadily, partly because the number of the very elderly will increase up to 1990; and the cost of the NHS rises in real terms because it is labour intensive and because scientific advance leads to better but usually more expensive forms of treatment. The number of people covered by private insurance is growing but still represents less than 10 per cent of the population.

3. Increasing the proportion of costs recovered through NHS charges clearly lessens the distinction between NHS and private treatment; and the logical conclusion of the process would be the abolition of NHS entitlement for certain groups of patient. Under a variant of the proposal above, therefore, drugs, spectacles and dental treatment would no longer be provided under the NHS except to limited exempt groups. The rest of the population would have to make private arrangements with the pharmacist, optician or dentist.

Arguments in favour

4.

- i. The proposal leaves the basic structure of the NHS intact.
- ii. Patients and others would be more aware of the high costs of medical treatment; unnecessary use of the service would be discouraged; and public opinion might act more powerfully to hold down NHS costs (including wage rates).
- iii. Heavier NHS charges would, at least modestly, stimulate the growth of private medical insurance and thus relieve pressure on the NHS. Hence it could be seen as a preparatory move before full privatisation (Option D).

Problems

5.

- i. To save substantial sums involves raising existing charges and breaking unpopular ground in three areas - imposing charges (eg for drugs) on patients who are now exempt (eg children); charging for seeing the general practitioner; and for hospital treatment.
- ii. It would cost money and staff to collect new categories of charges, and to carry out means tests (a taper would be necessary above supplementary benefit level). Some of the staff involved (eg general practitioners) would object strongly.
- iii. People who genuinely needed treatment might be discouraged from seeking it.
- iv. As long as the poorest are exempted from charges, increasing the charges would automatically increase the poverty trap - ie makes it less attractive for people to increase their earnings at the margin.

CHARGING FOR SCHOOLING

Proposal

1. Parents able to afford it would be required to pay the cost of their children's education, whether in the State system (where schools would be required to charge fees which covered their costs) or in competing private schools. It would still be compulsory to have children educated, normally at a school which met statutory minimum educational standards. Those with incomes too low to afford to pay would either have fees rebated or (preferably) would be subsidised via some form of income support.

Background

2. Schools expenditure this year is £7.4 bn, or 6½ per cent of total public expenditure. Nearly all of this is spent by local authorities at their own discretion, and it is about a third of their total current spending. The average cost per pupil is about £950 a year. Numbers of pupils will decline to 1990, and hence spending is projected to fall (but less than proportionately). Education in maintained schools will remain one of the largest social services, with private-sector education for compulsory school-age pupils (at present 5 per cent of all such pupils) remaining small.

3. A scheme for issuing vouchers to parents is sometimes suggested, as a less radical alternative to charging. It could help to promote wider choice, and would make it cheaper to send children to private schools if vouchers had a reimbursable "face value". But it would do nothing to reduce public expenditure, unless as an adjunct to charging with vouchers covering less than the full costs. Indeed there would be increased expenditure to meet any reimbursement for private education. Hence it is not put forward as an option here.

Arguments in Favour

4.

i. The saving could be as large as £3-4 bn, depending on the scale or rebating and whether it counted as public expenditure.

ii. Parents who wanted to secure a higher-quality education for their children, and were prepared to spend more, could do so by shopping around within the State sector or by going to private schools (and they would no longer be contributing to the cost of State schooling via central and local taxation). As real incomes rise, it is right to allow more resources to go into education to the extent that parents wish to purchase more and better schooling for their children.

iii. State schools would need to become more competitive and cost-conscious, and to pay more attention to parents' concerns (examination results, vocationally relevant courses, etc).

Problems

5.

i. There would be formidable political and administrative problems. Some mechanism would be needed for compelling local education authorities to charge "adequate" fees, which would entail new powers of central control and if necessary take-over.

ii. Cost differences do not only reflect differences in quality, and in particular schools in inner city areas tend to have higher costs. Some form of central government equalisation grant would probably still be needed to offset this.

iii. Students taking A-level courses in further education colleges would also be required to pay fees (to match the treatment of sixth-formers in schools). This would increase the discrimination between those in further education colleges undergoing training (on training allowances) and those on "school equivalent" courses (paying fees).

iv. There would be a wholesale redistribution of disposable income from paying parents to tax-paying non-parents. One way to offset this would be to raise child benefit to cover (standard) school fees, but this would

defeat the main object of reducing public expenditure and taxation. An alternative would be to re-introduce child tax allowance, but this would be sharply regressive, helping only parents with taxable incomes.

v. Given that fees would need to be rebated for parents with low family incomes, this would inevitably mean high marginal "tax" rates at the bottom of the scale, with bad effects on poverty trap and in-work/out-of-work incentives. Hence a form of graduated income support, on "negative income tax" lines, would be preferable - but previous tax credit schemes have been extremely costly, and the basic disincentive effect would remain, however distributed up the income scale.

vi. Since children could not be refused schooling, the business of collecting fees would be difficult and administratively expensive.

PRIVATE HEALTH INSURANCE

Proposal

1. The working population would be obliged by law to obtain insurance to cover the costs of health care for themselves and their dependants. Premiums would relate to the family's risks, not their means, and so the poor would need help with meeting the costs. Either initially or later the scheme could be extended to cover the non-working population, who would obviously need much more subsidy.

Background

2. Expenditure on the NHS this year is some £11.7 bn. The main components are some £2.1 bn (net of charges) for the family practitioner services (the services provided by family doctors, dentists, opticians and chemists); and £8.8 bn for hospital and community health services. Demand for all services is expected to increase steadily, partly because the number of the very elderly is increasing; and the cost of the NHS rises in real terms because it is labour intensive and because scientific advance leads to better but usually more expensive forms of treatment.

3. It would be prohibitively expensive to insure against the costs of long-term medical care and so, as in all countries, the state would have to continue to provide for certain types of patient (eg the mentally handicapped). Even so, it is estimated that the cost of basic medical cover for an average family of four would be about £600 a year. Those below average earnings (and possibly others) would need help with these costs and to the extent that this had to be channelled through payments rather than tax reliefs (since the poorest do not pay income tax), the public expenditure savings would be lessened. It is difficult to envisage a scheme which would reduce public expenditure on the NHS by more than say a third (£4 bn).

4. Within an insurance-based system, providers of health care (eg doctors) could be encouraged to set up companies to offer health care to clients in return for an annual subscription. Limited American experience with such Health Maintenance Organisations suggests that they may help to restrain costs.

Arguments in favour

5.

i. This proposal offers the prospect of a very large cut in the costs of health care to the taxpayer.

ii. The public would have its horizon of choice and of responsibility greatly widened.

iii. Patients could (within the limits imposed by their insurers) shop around for health care, so that doctors and hospitals would have to be more responsive to patients' wishes if they wished to stay in business.

iv. Although initially at least NHS hospitals could remain in state ownership, trading like nationalised industries, they could be progressively privatised. This would give much more scope for experiment and for variety in such matters as rates of pay reflecting local market conditions.

Problems

6.

i. Even though a free state service would be retained for the uninsured and possibly for the non-working population, for the majority the change would represent the abolition of the NHS. This would be immensely controversial.

ii. There would be transitional problems in persuading insurance companies to take on the risks before cash reserves had been built up to meet them.

iii. While this proposal would reduce the amount of public money spent on health, it would not reduce the community's spending on health care; on the contrary it would probably increase sharply. Some of this would be consumers' preference for higher quality, shorter delays etc. But judging by overseas experience, the providers of health care would also take advantage of the ever buoyant demand and of the inability of patients or of insurance companies to control costs, or in most cases to make informal judgments about the medical treatments on offer. Competition between doctors and hospitals would be on quality more than price.

iv. Providing help for those unable to afford the insurance premiums would raise vast difficulties. All claimants (perhaps over half the adult population) would have to be means-tested and even if the help were graduated, on negative income tax lines, there would be a sharp disincentive effect; increasing one's earnings, or moving into work from unemployment, would become less attractive.

v. Patients would face extra complications (form-filling etc). Patients or their insurers would need to be invoiced for treatment, and subsidies of some kind would need to be provided to a large part of the population. It would also be necessary to police the compulsory insurance system.

CUTTING THE REAL VALUE OF SOCIAL SECURITY BENEFITS

Proposal

1. The present laws which require most benefits to be increased annually by at least as much as prices would be repealed. New legislation would bring these benefits into line with the present arrangements for child benefit: upratings would become a matter of discretion for the Secretary of State who would attempt to preserve their real purchasing power but only as far as economic circumstances permit. If desired the Government could take the opportunity during the first year of operation of the new legislation to uprate some or all benefits by amounts which would effect substantial, once-for-all cuts in the real value of benefits. The bolder these initial cuts were the less need there would be in future years to hold down upratings below the level of inflation.

Background

2. Social Security expenditure in the current year is estimated at £32 bn, (28 per cent of total expenditure). In the three years to 1981-82 social security expenditure rose by 74 per cent, whilst public expenditure in total rose by 61 per cent; but the disproportionate increase was in large part due to the rise in the number of unemployed receiving benefit. At present most benefits must by law be increased annually at least in line with prices. Since 1972 the basic retirement pension has risen by 28 per cent in real terms while real national disposable income has risen by some 10 per cent. (Nearly all this very large improvement in the value of the pension occurred before 1979).

3. For the purpose of illustration, this option would yield some £3 bn a year by 1990-91 if a 10 per cent reduction in the LTPE projections is assumed. The effect on the real value of benefits depends on future economic performance. On the poor performance case - where the LTPE projections assumed that benefits would be maintained in real terms - benefits in 1990-91 would be 10 per cent below their current level in real terms. On the improved

economic performance case - where the LTPE projections assumed a 1 per cent per annum real improvement in social security expenditure ie increased real value of benefits and coverage - benefits in 1990-91 would perhaps be only a little below their existing real value.

Arguments in Favour

4.

i. The real increases in benefit rates during the 1970s have imposed a very large extra burden on the tax payer and those in work. Implementing the proposal could produce very large savings in public expenditure and lighten the burden on employers and the working population. In relation to the 1982 uprating each 1 per cent point reduction would have saved about £0.3 bn in public expenditure, a third of this being reflected in a reduction in the employer's contribution to the National Insurance Fund.

ii. The reduction in the real value of benefits for those of working age would increase incentives to work and increase the attraction of low-paid jobs.

iii. There would be a consequential saving on public service occupational pensions (eg those for civil servants, local government employees, NHS staff, the armed forces). This is because increases in these occupational pensions are statutorily linked to increases in the state retirement pension. A 10 per cent reduction in the value of these public sector pensions would yield about £300 m a year.

Problems

5.

i. Cutting the real value of benefits would be unpopular, particular in relation to the benefits for pensioners where the largest savings can be made. Pensioners would receive a lower share of the nation's wealth than

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ANNEX E (cont 2)

they do now , at least until the benefits of the new pension scheme become significant (after 1990); this would contrast starkly with what Labour once provided (upratings based on higher prices or earnings).

ii. There would be an increase in real poverty and current problems of social deprivation would be worsened (crime, poor care of children, illness from cold homes and poor nutrition etc).

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CUTTING EDUCATION SPENDING

Proposal

1. Spending on compulsory education for 5-16 year olds would be cut by about £1 bn a year while every effort would be made to maintain essential standards.

Background

2. Economies should be possible across the range of school provision by concentrating on the essentials and cutting out the peripheral. The process would need to start from an analysis of what schooling is intended to achieve and how the important outputs could be maintained at lower cost. Since 70 per cent of expenditure represents teachers' salaries (£4 bn a year at current prices), it would be impossible to achieve a £1 bn reduction without reducing teacher numbers substantially. But the pupil/teacher ratio in both primary and secondary schools has fallen dramatically since the end of World War II, for example in England between 1950-81 when it fell from 31 to 23 in the primary sector and from 22 to 17 in secondary schools. Although it is often claimed that the pupil/teacher ratio is a measure of the "quality" of education, the relationship between this ratio and academic student performance is far from straight-forward. At present the number of teachers is around 520,000, and the LTPE projections imply a fall to around 440,000 by the end of the decade, roughly in line with the fall in pupil numbers.

Arguments in Favour

3.

- i. It would provide an opportunity to weed out the lower qualified and less satisfactory teachers, and achieve a more efficient teaching force, supported by modern information technology to supplement class-room teaching (eg cassette teaching, audio-visual aids, modular courses etc).
- ii. The closure of wasteful poorly attended schools with small classes would be speeded up.

iii. Schools would be required to concentrate, particularly at secondary level, on a "core" of academic and vocational subjects, cutting down resources on other non-academic activities (unless on repayment).

Problems

4.

i. Some mechanism would be required for compelling local education authorities to make the planned cuts, eg in teacher numbers. This would entail new powers of central control, with a fall-back power to take over the functions of LEAs.

ii. There would be other formidable problems in implementing this proposal. In particular -

a. Unless the curriculum were severely pruned - see 3 iii above - schools could be left with a core of teachers each of whom would be required to teach a wide range of subjects.

b. There would be major resistance from the teaching profession.

c. There would be considerable redundancy costs.

iii. There might be a significant fall in the overall quality of education provided by the State system, even if this fall were not immediately reflected in public examination results.

iv. Pupils would have to work more on their own and this could have deleterious effects on classroom discipline and on the morale and achievement of the less able. On the other hand, it might help those who go on to higher education.

v. This approach is distinct from, and probably not compatible with the charging approach discussed in Annex C.

DEFENCE

Proposal

1. LTPE projections assumed that defence spending would increase in volume terms by 3 per cent a year from 1982-83 until 1988-89, with 1 per cent a year thereafter. The United Kingdom commitment to the 3 per cent growth target currently runs only to 1985-86. The proposal is to maintain the 1985-86 level in real terms, which would save about £1½ bn a year by 1990-91 as against LTPE. Internal forward planning in the Ministry of Defence currently assumes no growth in the defence budget after 1985-86. Hence this option could be achieved either by providing for no additions to spending at present planned, or by reductions to make room for some inescapable additions, eg by cancelling Trident. But the present planning assumption is deliberately cautious, to allow for some flexibility, so it does not follow that the option could be achieved without affecting military capabilities.

2. The political and diplomatic difficulties of this option would be reduced if NATO could be persuaded to reduce the 3 per cent target to a level which all or most member countries could realistically be expected to achieve.

Background

3. The present defence base-line is uncertain, in relation both to the level of spending in 1982-83 and to any revisions of plans in the immediate aftermath of the Falkland conflict. But defence spending cannot be ignored in this exercise. It now accounts for about 12 per cent of total public expenditure programmes, and on the basis of the LTPE assumptions (including the assumption that defence prices rise 2 per cent faster than prices generally) it will account for 15 per cent in 1990-91. On these projections, defence is responsible for more than a third of the total expenditure increase (in cost terms) from 1982-83 to 1990-91 - a much larger share than any other programme - though a different base year, or a different assumption about relative prices, would give different results.

Arguments in Favour

4.

i. If defence spending is not slowed down, it will continue to rise in relation to GDP, to around 6 per cent on the projection we have taken. Sooner or later, depending on the performance of the economy, this rise is very likely to be found unsustainable, so that drastic cuts will have to be made. It would be more sensible to plan from the outset for a sustainable rate of defence spending, as in the proposal.

ii. In the past a number of other countries have failed to meet the NATO target (even among those with GDP growth rates higher than the United Kingdom), and after 1980 (the last year for which comparative figures are available) their performance is likely to continue to fall short.

iii. The lower expenditure path would be feasible. It would be broadly in line with the forward planning now being undertaken in the MOD (though this deliberately leaves room for flexibility - para 1). Spending with British industry could still be higher than it is today (£6-7 bn per annum).

iv. A lower rate of spend on defence R & D would free scarce resources (high-quality scientists and engineers) for employment in civil R & D.

Problems

5.

i. There would be political problems, international and domestic, in changing course after 1985-86. Last year the United Kingdom supported the NATO Ministerial Guidance extending the commitment to 1988. Present political pressures are for more defence spending, not less.

ii. The absence of real growth in the defence budget, as against the increase in complexity and cost of major equipment, would entail a reduction in United Kingdom military capabilities.

OTHER PROGRAMMES

1. There is a number of other programmes which have not be included in the list of major options - either because there is no policy issue worth a full-scale review, or because the programme is too small to offer cuts approaching the £1 bn a year threshold, or both.

2. These programmes could nevertheless offer scope for very significant reductions in public expenditure, either by a generalised squeeze or by identifying policy changes. Following is a list of smaller possible areas where there may be scope for review, with figures for present annual spending (in 1980-81 cost terms, from the LTPE report) -

i. Export credits - the LTPE figure of £0.3 bn does not reflect the full extent of commitments, and there may be scope for review.

ii. Employment - £2.2 bn - much of this reflects policy reactions to the state of the labour market and will continue to do so; but there might be some scope for review:

- the Youth Training Scheme might take the place of the last year of compulsory schooling, instead of following it;

- on the training side, a remissible training tax on employers would reduce public expenditure;

- on employment services, privatisation of job centres might be examined.

iii. Regional - counting together expenditure by the Departments of Industry and Environment, this is of the order of £1 bn a year, and is already being reviewed.

iv. Housing - £2.9 bn - has been falling, but the future trend depends mainly on the real level of rents (as well as rate of sales, new building and improvements); a review of rent policy, and of relating subsidy to current rather than historic values, might be worthwhile (though most of the savings would not count as public expenditure).

3. Some other significant areas are -

i. Payments to European Communities - £1.8 bn - depends on future negotiations (in which it maybe necessary to bring in the possibility of alternative defence savings, eg in BAOR).

ii. Other local authority services - £10 bn - there may be more scope for increased contracting out and/or charging, analogous to charging for education (Annex C).

iii. Nationalised industries - £2.3 bn: - privatisation will generate once-for-all gains, but where industries sold are self-financing will have a nil or negative effect on total EFLs thereafter; - continuing deficits might be removed or reduced in the longer term, but this is bound to be a difficult and piecemeal process.

iv. Scotland, Wales, Northern Ireland - £10 bn - extra spending in Scotland in relation to needs has been investigated in the past, and is probably not worth a further full-scale review.

PUBLIC SERVICE MANPOWER

Proposal

1. Ministers would decide on a target for further reduction of civil service manpower, by say 10 per cent during the next Parliament. This would entail giving a high priority to -

- reducing functions, contracting out etc;
- simplifying policies and procedures (tax, social security etc);
- legislation where necessary to achieve these changes;
- expenditure on information technology.

The overall reduction would be allocated among departments and services according to the scope for such changes.

2. Similar targets would also be set for reductions in NHS and local authority manpower. These could be linked with increasing contracting out and privatisation of services.

Background

3. The pay bill for the civil service (industrial and non-industrial) is about £5 bn this year. Numbers will already have been reduced by about 14 per cent since 1979, so that the scope for further reduction merely by a continuing squeeze on numbers is likely to be small. Hence the need for more radical changes in functions and policies.

4. In principle there should be room for at least equal savings in other public services. The NHS employs approximately 1 million people, and numbers increased by 5 per cent between 1979 and 1981. The Government has set targets for reductions in management costs as a proportion of NHS resources over the next three years (in England, a cut of 10 per cent). Local authorities employ about 2 million people, and have reduced numbers by about 3 per cent since March 1979 - mostly in the education service, which employs nearly half the total (hence there is an overlap with Annex F).

Arguments in Favour

5.

- i. Over the rest of this decade, information technology will yield further economies in data processing, storage etc. It is already being applied to Government administrative operations, but the pace could be accelerated.
- ii. To achieve anything like a further 10 per cent reduction in civil service numbers would mean a radical review of present functions to achieve contracting out or privatisation of those services where economic costs might be charged (eg ^{say} PSA, ^{or} ADAS). This would be in line with Ministers' objective of "rolling back the frontiers of the public sector".
- iii. Very worthwhile savings might be achieved by subjecting NHS and local authority manpower to the sort of squeeze which has proved successful in the civil service. Pressure on numbers should lead to the contracting out of functions to the private sector, with gains in efficiency.

Problems

6.

- i. A good deal of effort has already gone into the reduction in Civil Service numbers to 630,000 by April 1984. Further substantial cuts will be hard to achieve unless Ministers are prepared to give up significant aspects of their present functions.
- ii. A separate manpower target can lead to inefficiencies, where it might be more cost-effective to employ staff (eg on social security fraud cases); and if the reduction of unemployment remains a prime objective, any such inefficiencies conflict with that objection.
- iii. In the NHS, given the decentralised system of control and the high proportion of staff closely involved in patient care, it will be alleged that any sizeable cut will mean a reduction in the quality of service.
- iv. In the local authorities, if the target is to go beyond exhortation some mechanism will be needed for enforcement, with familiar difficulties (cf Annex F).

ACCOUNTING CHANGES

a. Local Authority Expenditure. Local authorities at present have a large degree of autonomy, including the right to spend more than the Government's current spending target if they raise the money locally (by rates) to pay for it. Ministers have been considering this in MISC 79. If they decide not to impose direct central control over current spending, there is a case for counting as "public expenditure" only that part of local authorities' spending which is not financed from local revenues - as for nationalised industries and water authorities now, and local authorities in many other countries. This would be easier to justify if there were a limit on Exchequer grant, and non-domestic rates, so that expenditure beyond those limits was entirely a "charge" on local ratepayers/electors for extra services provided; both these changes are under consideration in MISC 79.

b. National Insurance Fund. More than half (£19 bn) of social security payments are met from contributions to the Fund. This will increase with the new State pension scheme, where public expenditure will vary according to the number "contracted out". In other countries contributory benefits are often treated "off-budget" rather than as part of public expenditure. The case for such a change would be stronger to the extent that contributions are regarded as different from ordinary direct taxation, and as buying an "entitlement" to benefits.



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The Rt Hon Sir Geoffrey Howe, QC, MP
Chancellor of the Exchequer
HM Treasury
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Parliament Street
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27 August 1982

Dear Sir

NORTH SEA OIL TAX CLIMATE

While on a recent private visit to San Francisco I talked with some of the senior Chevron (SOCAL) people who are personal friends.

While they are strongly in favour of what we are trying to do in this country I'm sorry to say that they are extremely pessimistic about the North Sea scene.

Projects started before the current tax regime came in will go ahead but they have no enthusiasm for further involvement. Regardless of the world oil climate they argue that the tax structure deters them. Recent adjustments do not impress them. They also adhere strongly to the view that even if there were an improvement in prices, the U.K. will always adjust taxes to cut back the incentive again.

I am of course more familiar than most with oil companies' tendency to cry wolf. But I have not hitherto heard this view put so vehemently and sincerely.

PERSONAL AND CONFIDENTIAL

I must say I think it is the very greatest pity if this should now be our tax reputation in this area. I hope we can change it back soon. North Sea oil and gas are not 'wealth' in themselves but only become so when linked with lasting business confidence and creative new private enterprise in the U.K. A climate to encourage long-term commitment offshore is, I believe, essential if we are to get permanent wealth, jobs and new businesses out of the North Sea operation. And that is what the Chevron people are convinced is now lacking.

This bearish view of Britain's taxation philosophy also seems to colour the thinking of other members of the San Francisco and Stanford financial and investment community with whom I also had informal discussions.

I am copying this to the Prime Minister, whom I minuted on this issue on 20 November 1980 and also to Nigel Lawson.

Gen
David

DAVID HOWELL



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

PRIME MINISTER

THE LONGER TERM

We had a word yesterday, and are to talk again on 31 August, about the handling of Cabinet on 9 September. I have talked to John Sparrow today about the paper which the CPRS are producing on the main policy options. You might like to see the attached draft of the paper which I propose to circulate.

2. I am very anxious to avoid giving the impression that this is simply another Treasury "cuts" exercise, but with bigger cuts than usual. In my paper, I have therefore sought to distance our discussion from this sort of approach. I hope very much that we shall be able to have a more fundamental and broad-ranging discussion about our long-term policy objectives and the size and shape of the public sector. Inevitably, this means looking at the broader political context and the prospects for the economy both at home and worldwide. In the course of this discussion I hope it will be possible to secure colleagues' general acceptance of the main conclusion in my paper: that the prospects suggested by the officials' reports are unacceptable, and that we need to get public expenditure onto a better track.

3. Having, as I hope, agreed on the seriousness of the overall problem and the need for a fresh look at public expenditure, we could then turn to the policy options identified by the CPRS as worth further study. Colleagues will no doubt want to comment on these individually and some will no doubt ask to be exempted from the exercise. On the whole, I hope we can avoid this. At this stage we are proposing only that there should be further



studies, and the exercise will be much more acceptable if all the major departments are seen to be in it together.

4. In the light of this discussion we could return to the particular recommendations at the end of my paper, the first of which (for further studies) is, of course, the most vital. I do, however, attach importance to the three other proposals, in particular the suggestion that, until the further work has been completed and reviewed, we should hold back from new commitments and from repeating pledges which would otherwise expire. I think this should apply equally to new promises on the tax front.

5. These suggestions on handling are of course very much subject to your views - and our discussion on Tuesday.

6. I am sending copies of this minute only to Sir Robert Armstrong and Mr. Sparrow.

A handwritten signature in dark ink, appearing to be 'G.H.' with a flourish.

G.H.

27 August 1982

CONFIDENTIAL

Draft Cabinet paper

THE LONGER TERM

Note by the Chancellor of the Exchequer

The issues we are to discuss on 9 September are among the most important we shall consider at any time in this Parliament. The way we handle them will crucially affect the policies we put forward at the next election, and the performance and shape of the economy for many years to come.

The problem

2. We came to power in 1979 with a firm commitment to reduce the share which the State takes of the nation's income. We argued in the manifesto that when the State spends and borrows too much, "taxes, interest rates, prices and unemployment rise so that in the long run there is less wealth with which to improve our standard of living" . Our experience since 1979, and all experience abroad, has demonstrated how well-founded that judgement was. The report by officials (C(82)) shows, however, how far we still are from fulfilling our manifesto commitment: indeed, if we maintain our present policies, with the expenditure to which they commit us, we could well move in the opposite direction.

3. Since 1979, prospects for the world economy have worsened substantially. It is clear that no-one can now confidently predict more than a fairly modest world growth during the rest of this decade. In addition, the UK economy has faced the particular problems of the pay explosion of 1979-80 and the rise in the exchange rate resulting from the petro-currency status of sterling. The resulting loss of competitiveness will take some time to remedy.

4. It is against this difficult background that the official report describes two "scenarios" for the development of the economy to 1990. Neither is a forecast: they simply illustrate what might happen if we maintain our present expenditure policies against two economic backgrounds, one rather more favourable than the other. On the low-growth Scenario B, the report shows that public expenditure might rise to nearly 47 per cent of GDP in 1990-91 - a higher proportion than at any time since the dismantling of the war economy. This level would be nearly 6 percentage points above that of our first year of office and 3 points above what we have agreed for 1982-83. Such a major departure from one of our central aims for the economy would, surely, be altogether unacceptable.

5. On the somewhat more optimistic assumption of $2\frac{1}{2}$ per cent growth in Scenario A, public expenditure would still be nearly 40 per cent of GDP by 1990. This is somewhat below the level of 1979-80 and about 4 points below that planned for 1982-83. But we cannot be reassured by this. In real terms, public expenditure would still be higher in 1990-91 than in 1979-80 or 1982-83. Moreover, some of the assumptions on which the projections are based are, if anything, over-optimistic. They make little allowance, for example, for the increases in expenditure which public opinion might expect in a period of higher growth. And they ignore "creep" - the apparently inexorable tendency for the planning total for any future year to be added to as it comes closer to the present because new and compelling policy commitments are entered into, or for other reasons. (The effect of this in recent years is clearly illustrated by the chart at Annex A).

6. Moreover, the projections in the officials' report, showing as they do significant increases in the social security, health and defence programmes, imply a degree of restraint in the provision of other public services which may in the event prove politically unacceptable. We need to give ourselves some room for manoeuvre in public expenditure.

7. I accordingly believe that:-

- (a) We must find new ways of permitting some of the demands to be met, both by encouraging people to make extra provision for themselves, at least at the margin, and by finding ways in which those extra services demanded can be supplied without burdening the Exchequer.
- (b) We must consider carefully the extent to which we are denying ourselves room for manoeuvre by past pledges and commitments. We must review these, questioning both the objectives and, in some cases, the underlying assumptions. Where priorities have changed, we must be prepared to drop commitments or modify them, perhaps drastically.
- (c) We must look much more closely at the efficiency of our spending programmes. This means in practice not only policy reviews, scrutinies and stringent control of manpower, but also opening up more of the business of central government, local government and the NHS to private sector competition, as is already being undertaken with local authority direct labour organisations.
- (d) Last but not least, it is essential that we get across to the country at large the nature of the longer-run problems of public spending and then seek its support and understanding for sensible ways of solving them.

Taxation and growth

8. I attach at Annex B a note by the Treasury which considers what the expenditure projections in the officials' report (C(82)...) could mean for taxation.

9. On the face of it the gap between revenue and expenditure in Scenario A in C(82).. does not look too bad. But the better growth of output and productivity reflected in this Scenario is based on an expansion of the private sector encouraged by reductions in interest rates and in taxes, especially taxes and charges on business, such as Corporation Tax, NIS or other National Insurance charges. It will also be important if we are to achieve this better growth performance, to reduce personal taxation so as to improve incentives. We cannot secure the lower interest rates that the private sector needs if we do not hold the PSBR down firmly. The way forward to better economic performance can therefore only be through reducing expenditure.

10. The rates of tax implied by the low growth Scenario B and related expenditure projections would plainly be quite unacceptable. They would be seriously damaging to industry and crippling in their effect on personal incentives. Moreover, the increases which would be needed are if anything understated, partly because the expenditure projections make no allowance for "creep", but also because such high rates of tax would create major problems of evasion and enforcement. They would almost certainly run into diminishing returns and lead to a further growth in the black economy.

Overseas experience

11. The UK is not alone in having to take hard decisions on public spending. Other countries, too, have had to rein back spending plans. They include both rich and poor. Among our major industrial partners, the US, Germany and Japan have

all sought spending economies. The French Government, too, is now seeking stringent cuts in its previously ambitious plans. Even among the Scandinavian countries, with a long tradition of high public spending, economies are being made. In many cases, previously sacrosanct programmes such as social security, health and education have had to share in the reductions. In developing countries in Africa, Asia and Latin America, reductions in public spending plans form a vital part of many of the adjustment programmes agreed with the IMF. Mexico is the most recent to join the list.

Conclusion

12. The record of the past two decades has shown all too clearly the dangers of formulating or accepting policy commitments on the assumption of a continuing economic growth which in the event has not been achieved. It has been a failure of successive Governments that they have assumed growth in the economy without taking the steps necessary to make it possible. Successive expenditure reviews have thus followed a dreary cycle of over-optimism followed, inevitably, by retrenchment.

13. As a Government we need a more robust strategy than this. We must not make the mistake of assuming that faster growth will float us over the rocks. We need to create the conditions for a freer and more prosperous society, in which the public sector is smaller and taxation is lower. This calls in my view for some thorough study and new insights, leading at a later stage to radical decisions affecting most if not all of the major programmes. We cannot neglect any possible approach.

14. I am not now proposing some kind of long-term total for public expenditure, still less specific cuts or changes of direction in any particular area of expenditure. I do, however, invite my colleagues to agree that the prospects suggested by the officials' reports are unacceptable, and that we need to take a

new and fundamental look at levels of public spending. More specifically, I seek their agreement:-

- (a) that (except where work is already in hand) we should as a first step commission further studies of all the main options identified by the CPRS in their paper (C(82)) and possibly some of those in Annex H. These studies should be completed and reported back to the Cabinet in the spring of 1983;
- (b) that meanwhile, to allow ourselves freedom of manoeuvre, we should agree to make no further public commitments which would add significantly to expenditure beyond 1985-86, and that we should avoid repeating former pledges which would otherwise expire;
- (c) that in considering this year's public expenditure Survey we should have particular regard to the longer term implications of our decisions, especially, for the "new" year 1985-86; and
- (d) that we should consider further how these difficult issues might best be presented to our supporters in Parliament and to the country at large.

PUBLIC EXPENDITURE IN THE LONGER TERM
FISCAL IMPLICATIONS

The longer term public expenditure exercise has projected expenditure to the end of the decade on two illustrative macro-economic scenarios, the main features of which are shown at Annex 1 of the Public Expenditure Paper. This note describes a similar projection of tax revenue on each of the same scenarios, and goes on to look at the balance between revenue and expenditure that is implied. Like the expenditure figures, these projections are dependent on the scenarios assumed: they are not forecasts. The margin of error is inevitably wide when looking so far ahead.

Assumptions

2. Like expenditure, taxes have been projected on the basis of unchanged policy. This has been interpreted to mean that income tax thresholds and specific duties are raised in line with prices, that tax rates are unchanged and that existing allowances and reliefs are continued. Local authority rates and National Insurance Contributions are calculated from the projections of local authority expenditure and expenditure from the National Insurance Fund, respectively, on the assumption that an unchanged proportion of such expenditure is met from general taxation. For North Sea taxes the real sterling oil price is assumed to rise by about a third between 1980 and 1990. (This reflects both a rise in the \$ price and a fall in the exchange rate.) Even though some new fields are assumed to come on stream, total production is assumed to be a little below its peak level, which is reached in mid-decade.

The projections

3. If scenario A were to be fulfilled, the projections suggest that tax receipts would rise by about 20 per cent in real terms. This is a rather smaller increase than that assumed for GDP in this scenario so that taxes as a percentage of GDP fall from 39½ per cent to just over 37 per cent. (See table A). However, this mainly reflects a fall in local authority rates and National Insurance Contributions as a percentage of GDP: this would only occur if local authority spending and benefit payments from the National Insurance Fund were in fact held to the levels assumed in the Expenditure projections. Income tax and consumption taxes fall slightly in relation to GDP, the former because the scenario assumes a falling wage share, the latter because the evidence is that a 10% rise in income leads to less than a 10% rise in consumption of goods that bear specific duties. The yield of capital taxes also declines in relation to GDP, largely because of the indexation of CGT. Corporation tax and North Sea taxes, on the other hand, rise somewhat as a percentage of GDP.

4. On scenario B projected tax receipts rise by only 6% in real terms - a good deal less than on scenario A. But GDP also rises more slowly and taxes remain roughly constant as a percentage of GDP at just below 40% (see table B). Local rates - derived from the Expenditure projections - fall in relation to GDP as in scenario A, but NICs remain a roughly constant proportion of GDP because the limited growth in benefit expenditure matches the limited growth in GDP. Capital taxes again fall in relation to GDP. Against this North Sea taxes and income tax rise as a percentage of GDP. (Corporation tax is about constant). The reason why income tax rises in relation to GDP on scenario B, unlike scenario A, is that wages and salaries rise as a share of GDP. 80-90% of the yield of income tax comes from wages and salaries. Consumption taxes, however, fall as a percentage of GDP because of the tendency for expenditure on goods bearing specific duties to rise less fast than income.

Implications

5. On scenario A the projected gap between expenditure and revenue narrows to about 2 per cent of GDP by the end of the decade - no smaller as a percentage of GDP than the target figure set for the PSBR in the last year of the Medium Term Financial Strategy. Moreover, the tax projections make no provision for raising income tax thresholds in real terms or for cutting tax rates to help personal incentives, or to ease the disincentive effects of the poverty trap. Nor do they allow for any reduction in the rate of business taxation*. Corporation tax payments are projected to rise as a percentage of GDP. Without tax reductions to improve incentives and increase net company profitability it is doubtful whether the economic growth postulated could be achieved.

6. If the economy develops less favourably as in scenario B the problem of financing public expenditure is likely to be much more severe. The projections show expenditure - which is little lower than in scenario A - exceeding revenue by 7% of GDP. If this gap were bridged by borrowing the implication is a reversal of progress so far made in reducing the PSBR. Indeed, as a percentage of GDP, borrowing approaches the levels which precipitated the 1976 crisis. But if borrowing were to be restrained to 2% of GDP without cuts in expenditure, taxes would have to be raised by the equivalent of £15 bn at today's prices. The tax burden would rise from 40% to 45% of GDP (having already risen from 35% to 40% since 1978-79. See Chart J).

7. If the £15 bn came from income tax alone, the yield would have to be raised by about half. If it came from the consumption taxes (VAT and specific duties) their combined yield would similarly have to be increased by half. (Raising £15 bn in VAT only would require the VAT^{yield} to be doubled). The response of

* Though if the expenditure projections in this scenario are fulfilled, the combined National Insurance Contribution rates of employers and employees taken together could fall by something like 1½ per cent. (There could also be some fall in local authority rate poundages).

taxpayers to changes on this scale cannot be predicted with any precision. But in crude "ready reckoner" terms what is implied is, at the least:

- raising the basic rate of income tax to about 45p (more if the tax base were reduced through evasion or disincentive effects). Deductions of tax and NIC together would then be over 50 per cent on a marginal £ of income for nearly all taxpayers.

or

- abolishing all allowances other than the single allowance (e.g. the married man's allowance, mortgage tax relief, relief for pension contributions and life assurance) and raising the basic rate to perhaps 33p.

or

- raising VAT to 25% and doubling the real level of all specific duties.

or

- levying VAT at 25% on goods which now bear the 15% rate and those now zero-rated (food, fuel, etc.).

Conclusions

8. The projections are, as stressed above, subject to a wide margin of error. But they demonstrate the difficulty of financing the levels of public expenditure implied by the continuation of current policies. If the economy grows very slowly, as in scenario B, the consequences for taxation and/or borrowing are very serious. The economy would need to grow steadily and strongly, as in scenario A, to permit the sort of expenditure levels envisaged. It is doubtful whether this growth could arise without any further Government action to improve work incentives or to improve businesses' profitability through tax cuts. But if taxes were cut borrowing could not be restrained to 2% of GDP and the inflation and interest rate assumptions would begin to look implausible.

Table A: Tax yields at constant (1980-1) prices and as a percentage of GDP

	£bn 1980-1 prices.			% of GDP		
	<u>1982-3</u>	<u>1990-1</u>		<u>1982-3</u>	<u>1990-1</u>	
		Scenario			Scenario	
		A	B		A	B
Income Tax	25.7	32.3	29.4	11.1	10.9	12.0
NIC's	16.4	18.6	17.5	7.0	6.3	7.1
Consumption taxes (incl VAT and specifics)	26.6	32.7	27.3	11.4	11.1	11.1
LA Rates	10.5	9.3	9.2	4.5	3.2	3.7
Corporation Tax, North Sea taxes and NIS	11.1	16.0	13.1	4.8	5.4	5.3
Capital Taxes	1.8	1.1	1.1	0.8	0.4	0.4
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
TOTAL	92.1	109.9	97.4	39.4	37.2	39.7
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Public Expenditure (incl debt interest)	103.0	116.0	115.0	44.0	39.3	46.8

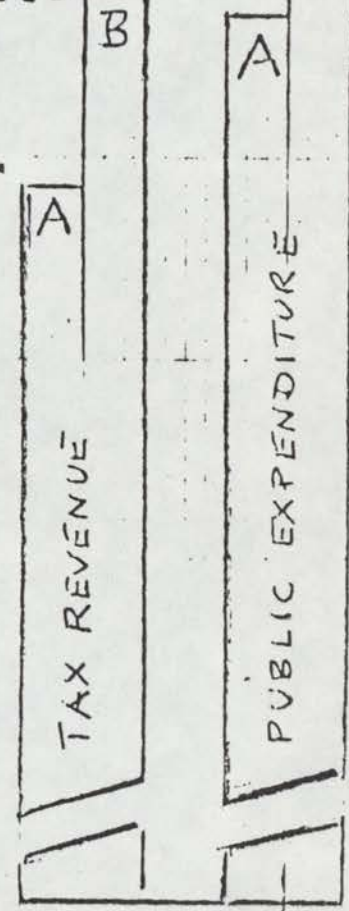
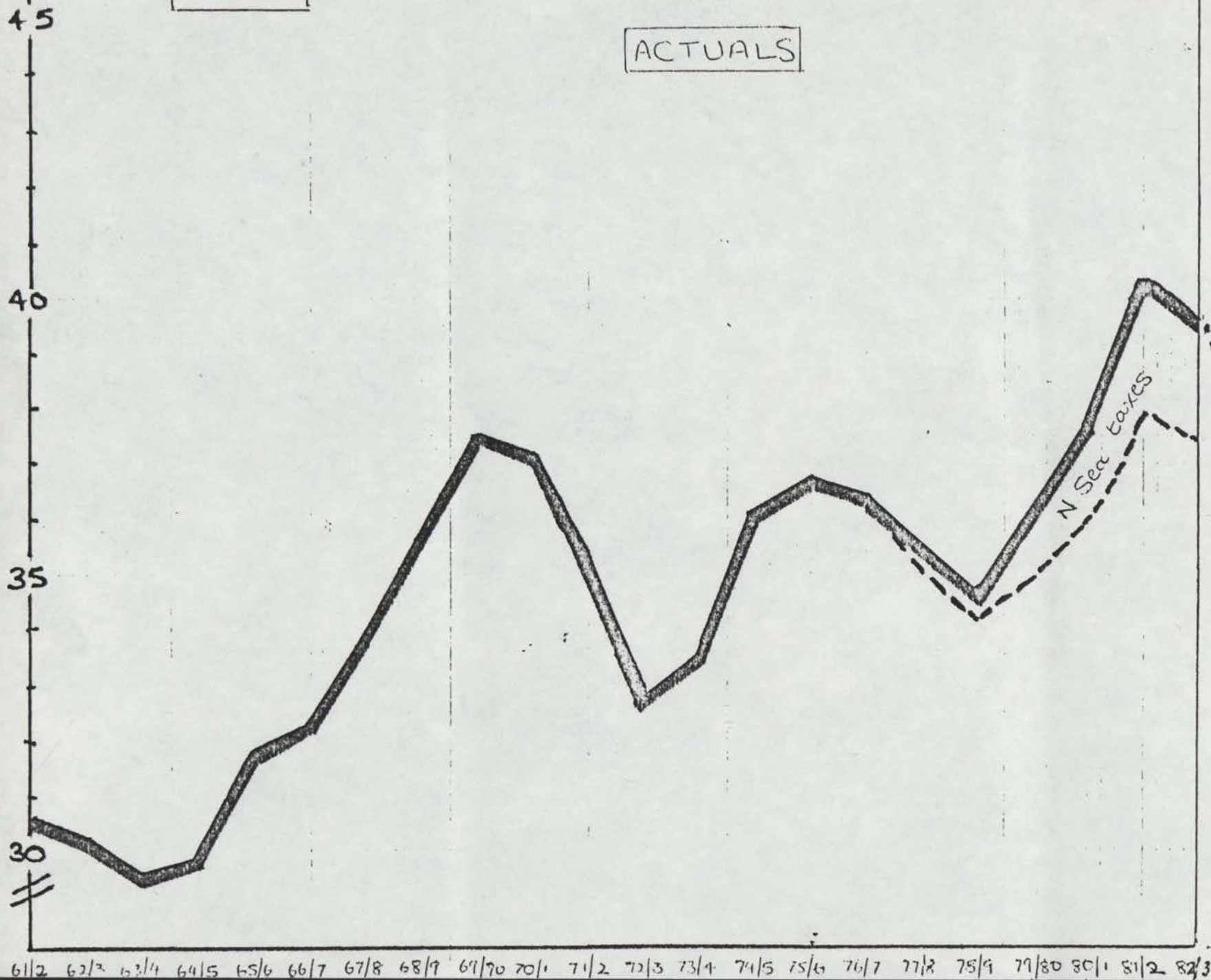
Note: Columns do not add exactly to totals because of rounding

Total Tax Revenue as % of GDP at market prices

Chart 1

ACTUALS

PROJECTIONS



1990-91

cc for information

Mr BUCKLEY

Sir Derek Rayner
Sir Robert Armstrong o/r
Mr Cassels o/r
Mr N E A Moore
Mr A W Russell o/r
Mrs Sloman
Mr Priestley o/r

LONG TERM TRENDS IN PUBLIC EXPENDITURE

In your minute of 3 August to Mr Priestley you asked for some "further thoughts" in connection with the Chancellor's proposal for "a very broad-ranging discussion about the Government's long-term objectives for the size and shape of the public sector" planned for the Cabinet on 9 September. This note draws on a draft left by Mr Priestley to summarise and direct thoughts at the planned discussion on 9 September. Attached to it is a longer paper by Mr Priestley discussing where the MPO might target itself over the new few years.

2. The Chancellor's paper of 28 July suggests that by 1990/91, on favourable economic assumptions, (2½% per annum economic growth and 5% inflation) public expenditure programmes will amount to 36.9% of gross domestic product (gdp) compared to 40.7% in 1982/83. If debt interest is taken into account this rises to 39.3% of gdp (compared to 44% now).

3. But the picture will deteriorate markedly if, say, we have ½ - ¾% economic growth a year in the decade of 1990 with unemployment and inflation at around present levels. On these assumptions public expenditure programmes are projected at 43.8% of gdp (46.8% if debt interest is included).

4. Discussion is likely to be about four key questions:
- (a) Are the levels of public expenditure acceptable?
 - (b) Particularly for the four largest programmes (Social Security, Defence, Health and Personal Social Services, Education), what policy options

are there which would reduce expenditure?
Does the taxpayer have to finance it all?

- (c) How can programmes improve their efficiency and effectiveness per pound spent?

Acceptable levels?

5. The Chancellor says, "Clearly we cannot go on like this [a consistent upward pattern over the past 20 years] we shall need to consider radical changes affecting most, if not all, areas of policy"..

6. It is certainly arguable that if economic growth improves, the projected public expenditure quota is acceptable. But as the officials' paper says, "there is still much to do to improve the flexibility and performance of the economy". The UK is also highly dependent on what happens in the world economy. The outcome is uncertain. A less favourable outcome is therefore a possibility.

Major policy options

7. The promised CPRS paper which I have not yet seen will discuss this more fully. But experience is that a marked change in policies to bring lower expenditure will be hard to agree and harder to deliver.

8. To reduce the share of gdp in 1982/83 by one percentage point, for example, requires programme expenditure to fall by over £2 billion a year.

9. A promising approach would be to look at how expenditure is financed. It may not be necessary for government to pay for all desirable social expenditure from general taxation. There may be wider scope for some programmes to be funded by insurance schemes (eg health insurance) for education vouchers

and the like which would not necessarily meet the full cost of services, leaving the consumer to meet some himself.

Efficiency and effectiveness

10. The Government has already been successful in showing that the costs of administering programmes and taxes are not fixed. The annual cost of running the central government is now about £14 billion a year out of total public expenditure of about £95 billion. The reduction in the civil service from 732,000 in April 1979 to 666,000 in April 1982 is worth at least £500 million a year in salary costs. A further reduction to 630,000 will be worth at least an extra £275 million a year.

11. Hence, Ministers will want to keep plugging away at civil service efficiency. This will involve continuing pressure on manpower after 1984 and attention to the cost of salaries, superannuation and other overhead costs. Bringing these items under effective control will mean investing time, money and effort in efficiency studies and in equipment which saves current costs. Every reduction of 100 clerical staff, for example, saves about £ $\frac{3}{4}$ million a year in salaries and this rises to £1 million a year when the overheads are included.

12. But the running costs of central government are only £14 billion out of about £95 billion of public expenditure. Ministers will also want to look at the efficiency and effectiveness of the remainder. The four largest programmes are largely run outside the civil service. And with the exception of the Armed Forces, staff numbers in these areas have increased more dramatically than the civil service.

Thousands

	<u>Numbers of staff:</u>						
	<u>1969</u>	<u>1974</u>	<u>1979</u>	<u>1981</u>	<u>Growth 1969-81</u>		
Civil Service	688	694	733	695	+7	(1%)	
Armed Forces	380	345	314	334	-46	(-12%)	
NHS	716	954	1197	1264	+548	(77%)	
Local authorities:							
Total	2505	2844	3060	2971	+466	(19%)	
Education	1189	1500	1587	1511	+322	(27%)	
Health and Social Services	257	272	344	349	+92	(36%)	

13. For the most part the Government's policies for good management of the state have made far less impact here than in its own house. What is needed is to apply the techniques of efficiency review to the £80 billion or so of "programme" expenditure and to use Whitehall influence and example to persuade the spending authorities to adopt similar techniques for their operations. We should recognise that the scrutiny programme was set up by Cabinet in October 1979 specifically to extend beyond efficiency in the narrow sense of administrative costs and to tackle the efficiency of policies. And we should work on the principle that, having been established by the Prime Minister as "audit and development" staff responsible to her as Minister for the Civil Service, MPO staffs can in principle go wherever she wishes.

14. This does not mean that the MPO should take over responsibility from Departments, and there are obvious constitutional issues - especially in respect of local authority

staff numbers. But in the context of a wide-ranging discussion there is a strong case for:

- (a) Specific ambitious targets for productivity and value for money improvements, if necessary based on crude measurements.
- (b) - A practical programme concentrating on:
 - i. incentives and requirements for good management in the public services.
 - ii. auditing progress.

15. Generally speaking, we can distinguish two types of target: people and management.

16. It is impossible to over-emphasise the importance of people. The Government needs to make it clear by unmistakable signals in the areas of promotion and retirement that it is investing in success and cutting out the dead wood, ie it is getting the official leadership needed. There is a limit to what government can do outside Whitehall. But signals to its own servants will also get through to other public sector employees.

17. In management the need is:

- vigorous action to get implementation on scrutinies agreed;
- development of management guidelines (such as those already promulgated for succession planning, for the open structure, and for specific tasks such as typing, vehicles etc) to be followed by management "audit" to ensure action is achieved and agreed policies implemented;

- a range of measures to affect management beyond Whitehall, by extending our project to cover programme options and performance and by extending proven efficiency techniques such as scrutinies into areas wider than Whitehall. Scrutinies have typically identified improvements worth 10-15% of relevant central government annual running costs. A similar expectation for non-civil service staff in the Armed Forces, NHS and local authorities seems reasonable. And henceforth most public expenditure programmes ought to be expected to show continuing productivity gains year by year.

18. We shall shortly be coming forward to the Lord Privy Seal with proposals for centrally co-ordinated "efficiency" work in 1983:

- (1) A scrutiny programme, including some of large executive functions such as support for the RAF, the prison service etc^{and some} which tackle the efficiency of policy formulation.
- (2) Multi-department reviews of:
 - (a) Supporting services for administrative work, including information handling and technology.
 - (b) The balance between line management and central management responsibilities, including management audit (in part as follow-up to the Financial Management Initiative.)
 - (c) Contracts and procurement procedures.

- (3) A further programme of "effectiveness" reviews in the "common services" area.
- (4) The allotment of some resources, in departments and the MPO, to the implementation of completed efficiency exercises.

19. This programme will make a contribution at the Whitehall end, where we need no let up in the commitment to efficiency work. So far, in relation to the four largest expenditure programmes the track record is:

Social Security - good work on administrative costs. 4 scrutinies which could yield about £100 million a year. The scrutinies of national insurance validation and the delivery of benefits to the unemployed dealt with policy issues (how much checking the state should do on the citizen's behalf and voluntary registration respectively).

DHSS are doing excellent work through the operational strategy for social security and "one person" reviews. But in such a large field the scope for more of the same is large.

Defence - 10 scrutinies yielding £13 million a year. Large "systems scrutinies" of management audit and financial control. A great deal going on in the Department but so far the choice of central efficiency programme topics has been patchy.

Health etc -

A new development in 1982 with the introduction of its own scrutiny programme into the NHS. Sir Derek Rayner is associated with this work, which will be done by NHS staff with limited DHSS guidance.

Education -

Very little done. The 1981 scrutiny of HMI is the most significant. 3 scrutinies yielding £1.9 million a year. Disappointing and largely untapped.

Summary and suggested line to take

- 20.
- The economic outlook is sufficiently uncertain to justify looking for further ways of constraining public expenditure.
 - Policy options of the size likely to be sought are hard to find and to deliver.
 - Alternative ways of financing desirable expenditure could be explored.
 - Existing central government manpower efficiency initiatives are worth at least £750 million and should be persevered with.
 - The growth in staff in the NHS and local authorities must also be tackled.
 - We need specific ambitious targets and a practical programme for the improvement of management throughout the public sector beyond Whitehall. And we need to audit progress across the full range.

- This will involve action about people in Whitehall, investment in equipment and work to reduce current costs, and extension of the proven techniques for securing change in Whitehall into the wider public sector.

I
B

IAN B BEESLEY
25 August 1982

CONFIDENTIALCC SV Econ Pd
~~SV~~CM
W/8

DEPARTMENT OF THE ENVIRONMENT
2 MARSHAM STREET LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

9 August 1982

END YEAR FLEXIBILITY FOR PUBLIC EXPENDITURE PROGRAMMES

I was keenly interested to see the report by officials attached to your memorandum C(82)29 and am only sorry that we have not yet had an opportunity to discuss it properly.

I appreciate why from your point of view you see difficulty in accommodating the possible cost of a change of practice here. But the existing practice is so inefficient and detrimental to the interests of construction and other industries that I am sure we must find a way forward. I shall wish to pursue this matter further in the context of the public expenditure discussions for 1983-84.

I also hope there will be an opportunity for an early collective discussion of this important issue.

I am copying to members of the Cabinet and to Sir Robert Armstrong.

yes
ML

MICHAEL HESELTINE

The Rt Hon Leon Brittan QC MP

CONFIDENTIAL

Carroll



Foreign and Commonwealth Office

London SW1A 2AH

4 August 1982

N. S. P. M.

AD 4/8

h.a.

Dear John,

Public Expenditure Survey and Net Contribution to European Community

Thank you for your letter of 30 July. We accept the Chancellor's judgement of this matter, and do not wish to pursue it further, although we continue to believe that it would help us presentationally, without any harm to our negotiating position, if we could find some way to overcome the practical difficulties which you outline in leaving the net contribution figures unchanged. If this cannot be done, we shall have to consider in good time how best to deal with any criticism we encounter when these figures are published.

I am copying this letter to the recipients of yours.

Yours over.

(F N Richards
Private Secretary

F N Richards

J O Kerr Esq
HM Treasury



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

30 July 1982

F N Richards Esq
Private Secretary to the Secretary of State for Foreign &
Commonwealth Affairs

Avail F/C-o. reply.

Dear Francis,

AA 3/8.

PUBLIC EXPENDITURE SURVEY AND NET CONTRIBUTION TO
EUROPEAN COMMUNITY

Your letter of 22 July to John Coles, commenting on mine of 13 July, mentioned a suggestion by your Secretary of State that the figures in the last Public Expenditure White Paper for our net contribution in 1983-84 and 1984-85 should be carried forward unchanged into the next White Paper.

The Chancellor fears that this would take us into two separate areas of potential difficulty. One concerns the principle of what figures the Government can publish in the White Paper. The other concerns presentational and negotiating aspects.

In practical terms, the problem is that the White Paper will include figures for the main components of our net contribution as well as the net contribution itself. So it would be necessary to choose between (a) updating all these components other than our budget refunds, and making an equal and opposite change in the refunds, and (b) leaving all the components unchanged as well as the net contribution itself. The Chancellor feels that neither course would be at all satisfactory.

Thus, failure to update the projections for the components - e.g. our gross budget contributions or CAP receipts, or our budget refunds themselves - despite all that has happened since last year on agricultural prices and budget refunds,



would mean a serious departure from the Government's normal practice of providing the best, "central", estimates in the White Paper, even in areas which are subject to considerable uncertainty. (There are many such areas in the public sector, particularly in the demand-led programmes.) The Government's failure to update these projections would not pass unnoticed, and suspicions would be aroused. There would be awkward questions from the Treasury Committee and others, and the Chancellor does not feel that the defence outlined in the penultimate paragraph of your letter would carry conviction.

The alternative of updating the projections for the components other than refunds, while making equal and opposite changes in the refunds figures so as to preserve the net contribution totals unchanged, would be no less problematic. Once again, the sleight of hand would not pass unnoticed. In addition, the Government would no longer be able to say that the White Paper made the 'stylised assumption' of a continuing refund rate of 66%, as in the 30 May settlement. As the projections now stand, the implied rate of refund would in fact be lower. Would this not be dangerous from the negotiating standpoint and convey a damaging signal to the rest of the Community? The other Member Governments would surely spot any departure from the 66% stylised refunds assumption used in the previous White Paper.

A further problem, which would arise equally with either of the above alternatives, is that the rather unusual device of repeating figures for 1983-84 and 1984-85 shown in the last White Paper, despite all that has happened since, could suggest to the rest of the world that the British Government was content to live with net contributions at these rather high levels - however strenuously the text protested the contrary. The Chancellor feels that the avoidance of any weakening in the UK's negotiating position must command a higher priority than trying to temper future domestic criticism (if the final deal should be unfavourable) by dampening domestic expectations.

An alternative approach which would be feasible would be to show in the White Paper the UK's net contribution before refunds, with an explanation in the text that we were determined to negotiate a new refunds regime. The trouble with this, however, is that the omission of refunds would give an unwelcome upward twist to the public expenditure



totals from 1983-84 onwards. Moreover, changes in the White Paper conventions from year to year create suspicion and are better avoided wherever possible.

The Chancellor's conclusion is that, all things considered, it would be best to adopt in the White Paper the convention set out in my earlier letter.

I am copying this letter to John Coles at No.10, Robert Lawson at MAFF, and David Wright in the Cabinet Office.

Yours ever.

J O Kerr

J O KERR
Principal Private Secretary



30 MAY 1982

1 2 3 4 5 6 7 8 9 10 11 12

CONFIDENTIAL



cc:

FCO
DOE
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CDL
EMP
EN
LPS
Ch. Sec HMT
DHSS
CO
CPRS

bc: A. Walters
J. Vereker

SW
Econ Pol

10 DOWNING STREET

From the Private Secretary

29 July, 1982

Long Term Trends in Public Expenditure

The Chancellor minuted the Prime Minister on 28 July about the likely pattern of public expenditure over the next decade.

The Prime Minister agrees that it would be helpful for Cabinet to have a broad ranging discussion, based on the report by officials attached to the Chancellor's minute, about the Government's long term objectives on the size and shape of the public sector. The Prime Minister hopes that this can take place at the meeting of Cabinet arranged for 9 September; I understand that time has been earmarked in Ministers' diaries for an extended discussion on that day. The Prime Minister agrees, too, that it would be useful for the 9 September discussion, if there were to be a CPRS paper pointing up some of the long term options open to the Government, especially as regards the possibilities for major structural changes affecting the larger expenditure programmes.

I am sending copies of this letter to the Private Secretaries to the other members of the Cabinet, to David Wright and to Gerry Spence.

M. C. SCHOLAR

John Kerr, Esq.,
H.M. Treasury

CONFIDENTIAL

BK



10 DOWNING STREET

From the Private Secretary

29 July 1982

Dear Francis,

Public Expenditure Survey and Net
Contributions to European
Community

The Prime Minister has noted the contents of your letter of 22 July.

I am copying this letter to the Private Secretaries to members of the Cabinet and to David Wright (Cabinet Office).

*Yours ever
John Wla.*

Francis Richards Esq
Foreign and Commonwealth Office.

JRW

cf 5V



Prime Minister (2)

To note
We postponed the

circulation of this minute

until after
yesterday's debate.Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

mf

We have earmarked

Sep 9 as the date for Cabinetdiscussion - 1/2 day, after lunch.

LONG TERM TRENDS IN PUBLIC EXPENDITURE

In my minute of ^{Pt 18} 8 March, I suggested that officials should undertake an examination of the likely pattern of public expenditure over the next decade.

Ms 28/7

re-circulated as c (82)32
... 2. This study has now been completed and I attach a copy of a report by a group of officials on which the main spending Departments, and the CPRS, were represented. The report considers what, on the basis of certain hypotheses about developments in the economy on the one hand and expenditure programmes on the other, public expenditure might amount to by 1990.

3. As expected, the picture is bad. Only on hypotheses that are rather favourable as regards the economy, and relatively modest as regards expenditure programmes, does public expenditure as a percentage of GDP come out lower in 1990-91 than it was in 1979-80. In cost terms the prospect on any of the hypotheses is for big increases over this period.

4. The report shows clearly how the balance of our public expenditure programmes has changed and will, on present policies, continue to do so. It also shows the extent to which the four largest programmes - social security, health, education and defence - dominate public expenditure. In 1979-80 the four programmes between them amounted to about 60 per cent of the total. By 1990-91, on these projections, they would amount to about 63½ per cent, even in the "best case". Within that, defence would take a higher proportion and education a smaller proportion of the total.



5. The officials' report looks forward, and shows a generally rising trend of future expenditure. Forecasting in an uncertain world is difficult. But if we look backwards over the last twenty ... years (Table A annexed) a consistent upward pattern emerges, broken only by the two external crises of 1967 and 1976. Even then, the upward trend was soon resumed.
6. Clearly we cannot go on like this. If we are to break the pattern decisively - as we must - then we shall need to consider radical changes affecting most, if not all, areas of policy. Unless we are willing to tackle some pretty basic questions in a fundamental way, then, so far from being able to offer the chance of some easement of the tax burden (clearly desirable for industrial recovery) we should face instead the prospect of endlessly recurring "public expenditure crises".
7. It would, I am sure, be helpful if Cabinet was now able to engage, on the basis of the officials' report, in a very broad-ranging discussion about the Government's long-term objectives for the size and shape of the public sector. We should not be inhibited at this stage by such considerations as the need for legislation, the existence of past commitments or the alleged political impossibility of change. A discussion of this kind would pave the way for some major strategic decisions affecting our programmes as a Government for the next Parliament.
8. Obviously there is some connection between decisions on this year's public expenditure Survey, at any rate as regards the last year 1985-86, and the longer term. Nevertheless I believe that it will be more conducive to the kind of broad exchanges that I have in mind if our discussion of the longer term is distanced somewhat from our preoccupations with the Survey.
9. It seems to me that it would be difficult to conduct an adequate discussion about the longer term within the framework of our regular



Cabinet meetings, and that some special arrangements for this discussion will be needed - perhaps a specially convened meeting of the Cabinet. If such a meeting took place in September, it could also form part of the preparation for this year's Party Conference, at which we shall no doubt be under pressure about various aspects of public expenditure.

10. I should of course circulate a paper of my own for discussion with the officials' report. I hope too that we might look to the CPRS for support in the form of a paper pointing up some of the longer term options open to us, especially as regards the possibilities for major structural changes affecting the largest expenditure programmes.

11. I am sending copies of this minute and the officials' report to members of the Cabinet, Sir Robert Armstrong and Mr. Sparrow.

A handwritten signature in dark ink, appearing to be 'G.H.' with a stylized flourish.

G.H.

28 July 1982

PUBLIC EXPENDITURE IN THE LONGER TERM

A report by an Inter-departmental group of officials

Introduction

This report considers the way in which the costs of the Government's public expenditure policies could develop over the rest of the decade, against the background of some assumptions about economic developments over this period.

2. The aim is not to forecast total public expenditure, or individual programmes, or the course of economic development. The public expenditure figures have been built up on the basis of the continuation of current policies at the programme level, and the economic scenarios have been constructed on specific assumptions. One should beware of any spurious sense of precision. The figures for individual programmes are not to be regarded as bids or targets, and the results cannot be other than very broad brush.

3. The report presents a snapshot of 1990. It also, in the notes on individual programmes in Annex 2, offers some comments on the path by which some of the programmes might achieve the levels shown for them in 1990. In general, however, it is not concerned with possible developments regarding public expenditure in the period between 1984-85 (the last year covered by Cmnd 8494) and 1990-91. But it is clear that if the Government intends significantly to influence the outcome as regards public expenditure in 1990-91, the necessary decisions would need to be taken a number of years in advance.

The Two Economic Scenarios

4. In considering the longer term implications of the Government's public expenditure stance, the report first adopts a set of assumptions about productivity, inflation, growth and unemployment which would represent a substantial and continuing improvement on our recent national economic performance. This is Scenario A. Its principal features are set out in Annex 1. The assumptions are that inflation will fall and remain at a modest level, that wage restraint, combined with lower tax rates and interest rates, permit

rapid rebuilding of profit margins, that productivity continues to grow well, and that economic growth will as a result be sustained at a level well above what has recently been achieved. Such a performance implies an all-round improvement in our affairs, and may not be far short of the best we can expect.

5. But things may not turn out like this. The UK has long suffered from low efficiency and poor productivity, and there is still much to do to improve the flexibility and performance of the economy. We are highly dependent on what happens in the world economy. The world economic environment remains very difficult. In common with our European neighbours, but to a greater extent than some of them, we have lost competitiveness, and despite some recent improvement will not easily regain it. It is accordingly necessary to look at public expenditure against the background of much less favourable economic assumptions than in Scenario A. In Scenario B, which is also described in Annex 1, the main differences from Scenario A relate to productivity growth (1½% instead of 3% per year in the decade of 1990), GDP growth (½-¾% instead of 2½%) and unemployment and inflation (which stick around their present levels instead of coming down).

6. None of this is to say that events will turn out precisely according to either of these scenarios. They are hypotheses, not forecasts; it would in particular be a mistake to suppose that a prediction of the future can be obtained by splitting the difference between them. But they seem to cover an adequate range of possibilities against which to examine public expenditure trends in the light of the Government's objectives.

7. These economic scenarios interact with public expenditure trends in two ways. On the one hand assumptions on economic growth, inflation, unemployment, interest rates, productivity and earnings growth are needed to cost the programmes. On the other hand the taxation and interest rate consequences of public expenditure have implications for the supply side of the economy and for employment and productivity. The presumption underlying Scenario A is that expansion of the private sector provides the main engine for growth in the economy and that this expansion would be promoted by reductions in taxation and interest rates and

hence in total public expenditure as a proportion of GDP.

The Public Expenditure Projections

8. In making the public expenditure projections it has been assumed that the Government will continue to constrain the size of the public sector by privatisation and restraint on expenditure. Firm intentions to privatise have been reflected in the expenditure figures, but no account has been taken of any substantial further privatisation. Allowance has been made for changes in expenditure as a result of demographic changes, and, for some economic services such as transport, for the likely growth in national income. But only limited allowance has been made for the likely increase, if national income grew as assumed in Scenario A, in the public's demand for some of the public services, notably health, education, and environmental services, and for increasing real social security benefits. (Social security benefits, for example, are assumed to increase by less than earnings). International evidence suggests that this demand could increase on a significant scale. The Government is not obliged to meet it and may decide to divert it into privately provided services. But the scope for such diversion is limited over this period. And local authority expenditure, although projected to continue its relative decline, may continue to be difficult to control.

9. The projections have been combined with the two economic scenarios to show what could happen to public expenditure as a proportion of GDP. This proportion is also a measure of the ratio of taxation and government borrowing to GDP; although to the extent that this is reduced by privatisation resources will not be released for expansion elsewhere. Privatisation of a corporation for example will move its borrowing from the public to the private sector, but this will not reduce interest rates.

10. The inflation assumptions in the two scenarios are very different, so it is not easy to interpret differences in expenditure between the scenarios when the figures are set out in current prices. The figures have therefore also been deflated by the inflation indices assumed in the two scenarios. This avoids measurement problems caused by changes in the value of money,

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but takes account of changes in the relative costs of different elements in the various programmes. This means that the programmes, and the totals are expressed both in what are called "cost terms" and as a proportion of GDP.

11. The projections assume that levels of services over the period to 1990 will not, taking one year with another, be squeezed on account of inflation. The levels of service at which it would be appropriate for Ministers to aim if inflation were high is a matter for future decisions.

12. Figure 1 shows how, compared with 1979-80 and 1982-83, total public expenditure could develop on the basis of the two economic scenarios.

13. In cost terms, the 1990-91 programme total⁴ in Scenario A is 20% higher than it was in 1979-80. In Scenario B it is 18% higher. As a percentage of GDP the total in Scenario A falls, compared with 1979-80, by a little over 1 percentage point, taking it back to where it stood in 1971-72. In Scenario B it increases by nearly 6 percentage points.

14. Comparison of 1990-91 with 1982-83 shows the programme total in cost terms at nearly 14% higher in Scenario A and 13% higher in Scenario B; as a percentage of GDP the total is nearly 4 points lower in Scenario A and 3 points higher in Scenario B. But this is in part because public expenditure in 1982-83 as a percentage of GDP has been increased by economic recession; this has reduced GDP and increased social security expenditure. It may therefore be a less satisfactory basis for comparison.

15. Figures 2 and 3 show how the various major programmes could contribute to these changes, expressed both as a proportion of GDP and in cost terms. In both scenarios the share of GDP devoted to

- 4 -

⁴ The term programme total is used here to describe total public expenditure as defined in Cmnd 8494 and previous public expenditure White Papers. Also shown in figure 1 is the wider total including debt interest and some other adjustments, often used for comparisons with GDP. The figures for 1979-80 are outturn and those for 1982-83 are Cmnd 8494 adjusted for the changes in public expenditure announced in the Budget.

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defence would be higher in 1990-91 than in 1979-80; although with no non-pay relative price effect there would in Scenario A be no increase over 1982-83. Health and social security are shown as a broadly constant proportion in Scenario A, and a rising proportion in Scenario B. Education is shown as a declining proportion in both cases. The share of economic services (agriculture, industry, transport, nationalised industry borrowing), tends to fall, as does that of environmental services (housing, water and sewage, etc).

16. In cost terms, increases in major programmes from 1979-80 to 1990-91 on the basis of the assumptions in this report would be

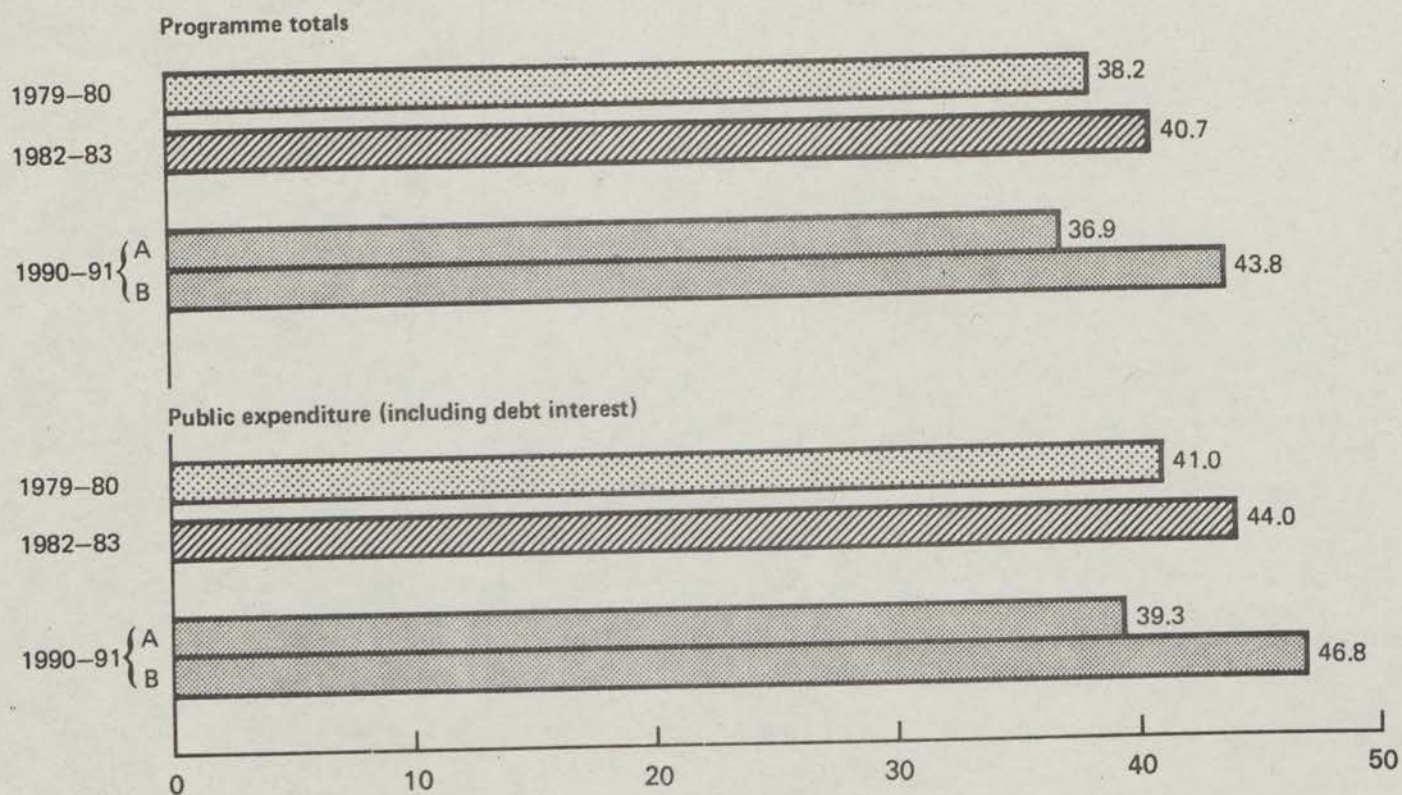
- 35 to 50 per cent in defence expenditure, depending in part on the assumed non-pay relative price effect
- 30 to 35 per cent in the law and order programmes
- 25 to 35 per cent in expenditure on health due largely to demographic pressures
- 20 to 25 per cent in the social security programme, even though demographic changes are relatively favourable for this programme in the 1980s, compared with the 1970s or the 1990s.

The cost of education would be slightly higher in Scenario A than Scenario B if economic growth increased the real earnings of teachers. Different economic situation could affect infrastructure and industry programmes; higher growth is taken, for example, to involve more road buildings; a sluggish economy could involve more assistance to industry and employment and housing expenditure.

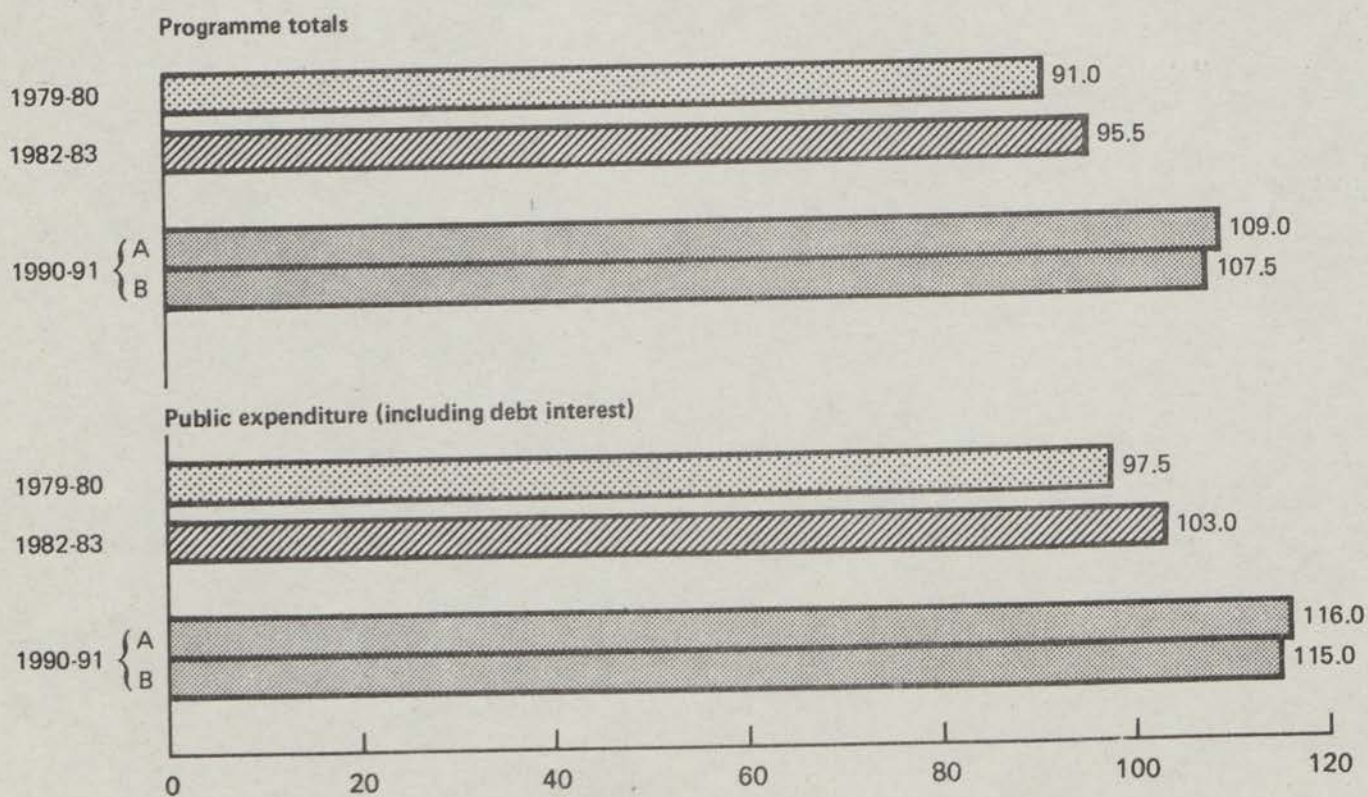
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FIGURE 1

Public expenditure
Percentage of GDP



£billion, 1980-81 cost terms

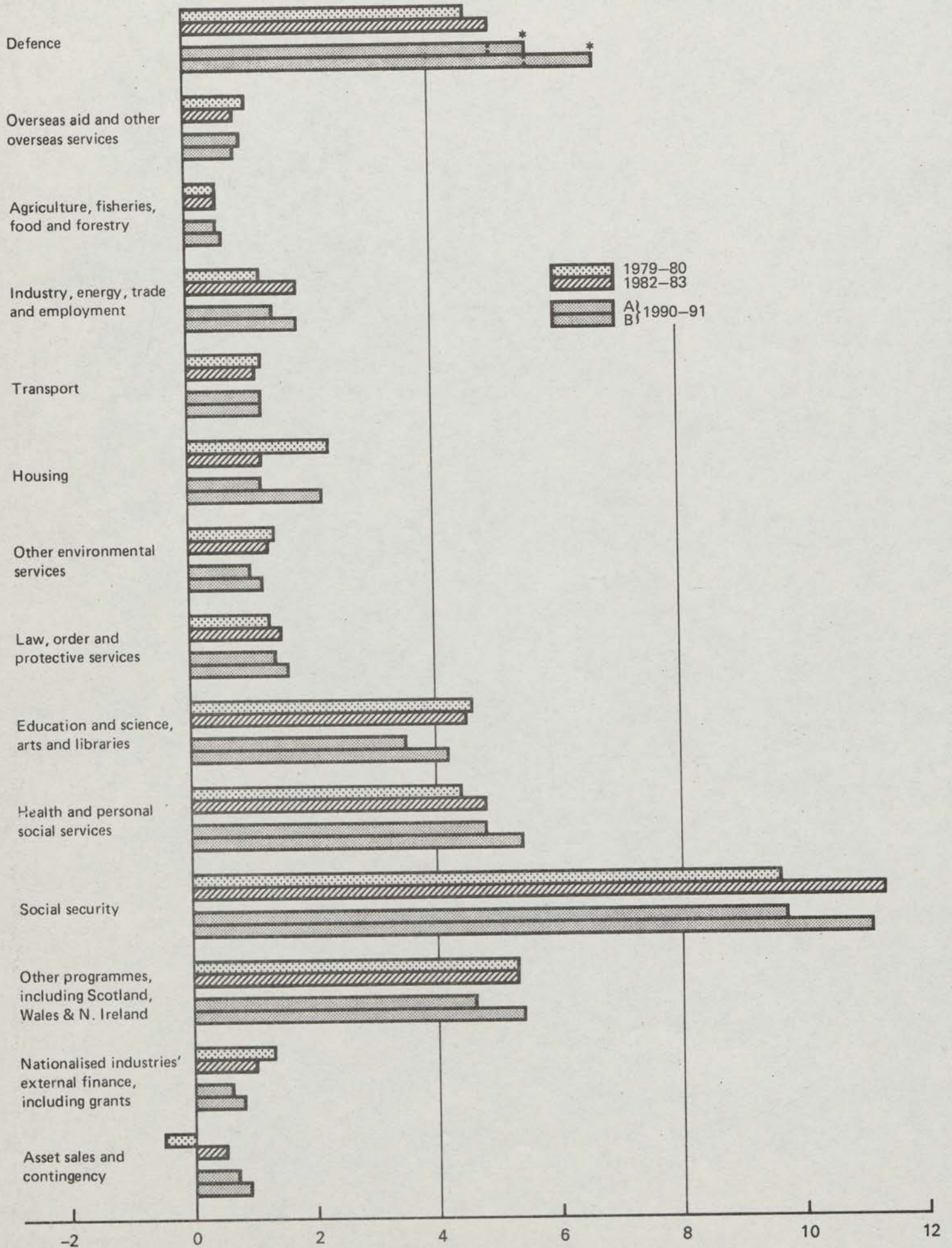


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FIGURE 2

Public expenditure programmes

Percentage of GDP



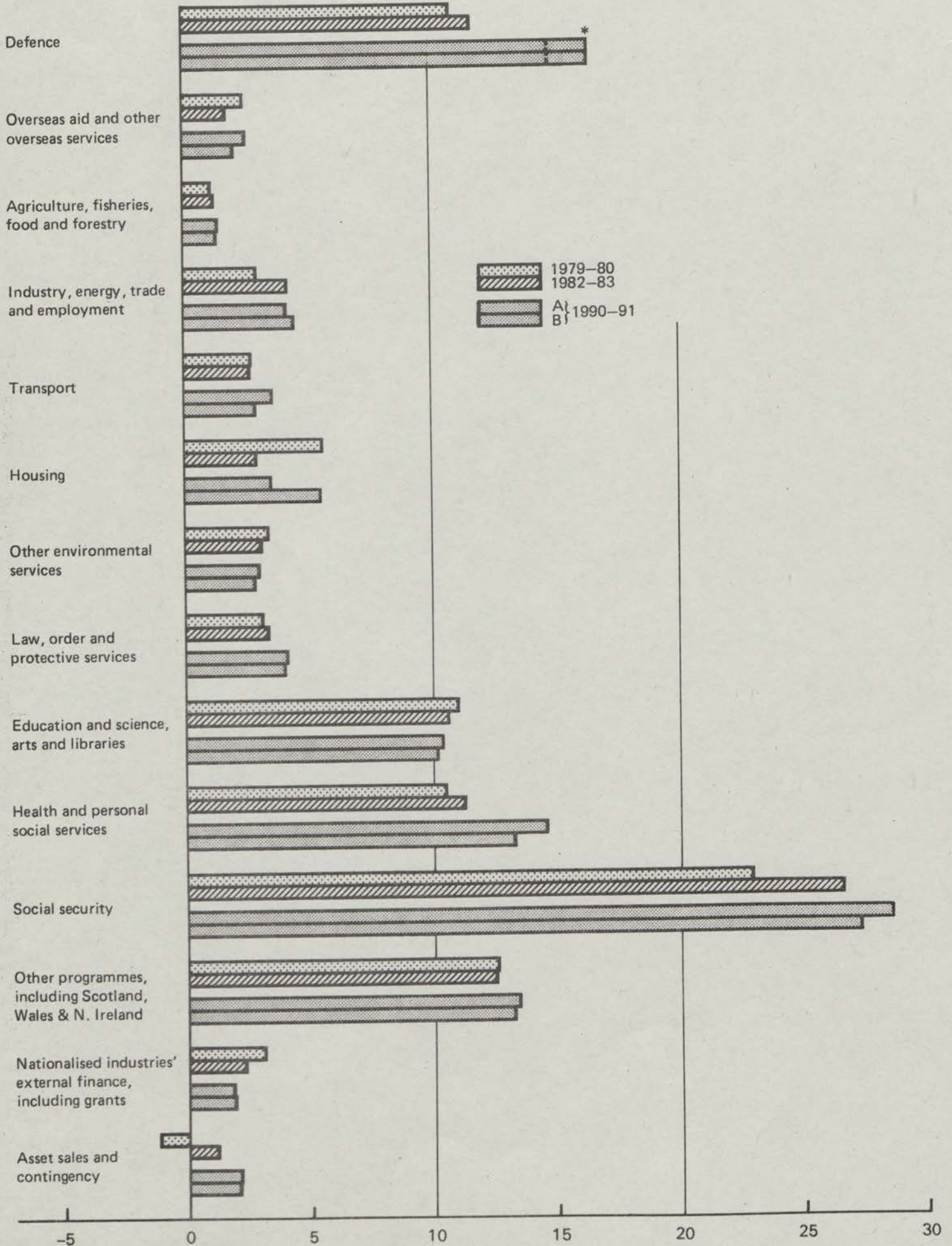
*See Annexe 2, Programme note 1

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FIGURE 3

Public expenditure programmes

£billion, 1980-81 cost terms



*See Annexe 2, Programme note 1

ECONOMIC SCENARIOS

The main assumptions of Scenarios A and B are summarised in Table 1. In Scenario A, economic growth in the 8 years to 1990-91 is similar to that of the 1950s and 1960s. In Scenario B growth is similar to that of the last 8 years. These growth rates are combined with the productivity assumptions and a small growth in the labour supply, to give consistent figures for unemployment.

2. Inflation is assumed to settle at 5% per year in Scenario A and 10% per year in Scenario B, although this has little direct effect on the public expenditure projections.

3. Scenario A assumes high productivity growth but, in the early years, much lower real wage growth. In Scenario B, real wages grow more rapidly than in Scenario A in the early years and more slowly in the later years. Public service wage growth is assumed in both scenarios to fall behind that in the marketed sector to 1982-83; thereafter wages in both sectors are assumed to grow at the same rate.

4. The change in public service wages relative to average GDP prices is a "relative price effect". This "pay-RPE" has been taken into account in projecting the public service expenditure programmes.

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TABLE 1: ECONOMIC SCENARIOS - MAIN ASSUMPTIONS

	SCENARIO A	SCENARIO B
GDP (average annual growth rate from 1980-81)	2½%	¾% to 1985-86 then ½% to 1990-91
Productivity in the marketed sector (average annual growth rate from 1980-81)	3%	1½%
Unemployment (narrow definition, excluding school leavers)	2 million in 1990-91	3 million in 1990-91
Inflation (GDP deflator)	5% per year in mid and late 1980s	10% per year in mid and late 1980s
Real interest rate	2% in 1990-91	2% in 1990-91
Real trade-weighted exchange rate (1980-81 = 100)	83 in 1990-91	83 in 1990-91
Real marketed sector wages (average annual increase from 1980-81)	1½%	1½%
Real public service wages (average annual increase from 1980-81)	½%	¼%

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ANNEX 2

EXPENDITURE PROGRAMMES

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1. DEFENCE

1.1. The likely path of defence expenditure over the next decade is determined by the Government's commitment to the NATO target of 3 per cent annual real growth. At present this commitment does not extend beyond 1985-86. The UK supported the 1981 NATO Ministerial Guidance extending the Alliance's commitment to 1988.

1.2 In both scenarios, 3 per cent per year real growth is assumed, starting from the 1982-83 cost terms figure. It is assumed that the Government's commitment will be extended to the end of the NATO target period (1988-89) and there will be 1 per cent annual growth thereafter.

1.3. For the relative price effect (RPE) of non-pay expenditure alternative assumptions have been adopted of zero and 2 per cent positive from 1982-83. The effect of these assumptions on the projections for 1990-91 is shown in the table below.

TABLE 1.1. DEFENCE EXPENDITURE

	1979-80	1982-83	1990-91			
			A		B	
Non-pay RPE (increase per year) 1982-83 to 1990-91	-	-	0	2%	0	2%
£m (1980-81 cost terms)	10880	11732	14800	16400	14800	16400
% GDP	4.6	5.0	5.0	5.6	5.6	6.7

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2. OVERSEAS AID AND OTHER OVERSEAS SERVICES

2.1 Like most developed countries we are committed to achieving a level of overseas aid of 0.7 per cent of GDP, but in general there is no commitment to a date. At present, the UK aid programme is fluctuating about 0.4 per cent of GDP, slightly above the OECD average. It is likely that cash expenditure on the aid programme will increase less rapidly than nominal GDP up to the mid-1980s.

2.2 The projections assume that in Scenario 'B', the aid programme will return to a level of 0.4 per cent of GDP by 1990-91. In Scenario 'A', some modest progress towards the 0.7 per cent target is assumed, reaching 0.5 per cent of GDP by 1990-91.

2.3 The other programmes for which the ODA is responsible (the aid administration vote; supplements etc to certain overseas pensions plus, from 1982-83 to 1984-85, foreign currency borrowing of £15m a year by the CDC) are de minimis in the context of this exercise, and are assumed to stay at roughly their present level in cost terms.

2.4 Other FCO expenditure will be affected to some degree by planned reductions in civil service expenditure and the general desire to achieve economies, although some of the expenditure (such as international subscriptions) cannot be unilaterally reduced. It has been assumed that this block of expenditure, and the small item covering the Commonwealth War Graves Commission, will remain broadly constant after allowing for inflation worldwide and exchange rate fluctuations.

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TABLE 2.1 EXPENDITURE ON OVERSEAS AID AND OTHER
OVERSEAS SERVICES, EXCLUDING NET PAYMENTS
TO EC INSTITUTIONS

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 Cost terms)	1470	1363	2020	1510
% GDP	0.6	0.6	0.7	0.6

2.5 Net contributions to the European Community Budget are currently much lower than they would have been but for the refunds negotiated under the 30 May Agreement. That Agreement also commits the Community to avoid the recurrence of unacceptable budget situations for any member state. There will be strong pressure operating during the 1980's which will tend to increase the UK's net contributions before refunds: the growing costs of supporting farm incomes and disposing of surpluses this may produce, the extension of the Common Agricultural Policy to cover Mediterranean products and the accession of Spain and Portugal to the Communities. Maintenance of the ceiling on the Communities "own resources", under which they are entitled to the yield of a value-added tax not exceeding the 1 per cent of the value of transactions incorporated in the harmonised spending base, may help to contain EC expenditure on these policies. But a satisfactory outcome for the UK net contributions will depend on our success in persuading the Community to provide budget refunds on an acceptable scale.

TABLE 2.2 NET PAYMENTS TO EUROPEAN COMMUNITY INSTITUTIONS

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 Cost terms)	1010	415	500	500
% GDP	0.4	0.2	0.2	0.2

2.6 Aggregate expenditure on Programme 2 is summarised in Table 2.3

TABLE 2.3 TOTAL EXPENDITURE ON OVERSEAS AID AND
OTHER OVERSEAS SERVICES

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 Cost terms)	2480	1778	2520	2010
% GDP	1.0	0.8	0.9	0.8

3. AGRICULTURAL, FISHERIES, FOOD AND FORESTRY

3.1 A large part of the expenditure covered by this programme is affected by the rules of the Common Agricultural Policy, for which both the future direction of policy and the basis for funding are very uncertain over the longer term.

3.2 The projections are based on the assumption that, apart from the completion of the Thames tidal defences, expenditure by MAFF increases at 1 per cent per year in cost terms from the level of the mid 1980's, as does Forestry Commission expenditure, while expenditure by the Intervention Board for Agricultural Produce increases at about 2 per cent per year throughout the decade. The projections exclude an allowance for capital expenditure by RWA's, as explained in para 8.2 (Other Environmental Services).

3.3 Main programme 3 includes some expenditure outside England, but territorial programmes also include expenditures on agriculture. These are assumed to amount to £200m (1980-81 cost terms) in 1990-91 for both scenarios, ie similar to their relative size in 1980-81.

TABLE 3.1 EXPENDITURE ON AGRICULTURE, FISHERIES,
FOOD AND FORESTRY

	1979-80	1982-83	1990-91	
			A	B
MAFF £ (1980-81 Cost terms) % GDP	650 0.3	577 0.2	520 0.2	510 0.2
IBAP £ (1980-81 Cost terms) %GDP	435 0.2	570 0.2	840 0.3	820 0.4
Forestry £ (1980-81 Cost terms) % GDP	55 -	53 -	50 -	50 -
TOTAL £ (1980-81 Cost terms) % GDP	1140 0.5	1200 0.5	1410 0.5	1380 0.6

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4. INDUSTRY, ENERGY, TRADE AND EMPLOYMENT
(excluding grants to nationalised industries)

4.1. Industry

Expenditure by the Department of Industry on Regional and General Industrial Support should fall in real terms by about one third between the early 1980's and 1990-91. This fall is the effect of the assumption that support for "problem companies" would only be about £200m a year as compared with the peak of about £800m for BL and Rolls Royce in 1981-82. It is assumed that regional and other industrial support will continue at roughly the level of the early 1980's while Scientific and Technological Assistance is on a rising trend and some provision is also made for future "launch aid" projects.

TABLE 4.1

EXPENDITURE BY THE DEPARTMENT OF INDUSTRY,
(excluding assistance to steel and shipbuilding)

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	1135	1085	1170	1170
% GDP	0.5	0.5	0.2	0.3

4.2. Energy

The main items of expenditure by the Department in 1990-91 are likely to be nuclear research and development, non-nuclear research and development including that on alternative sources of energy, and payments to redundant coalmine workers (which do not count towards the NCB's EFL). These programmes are unlikely to be very sensitive to differences in economic growth in the next few years. The level of research and development expenditure on nuclear and other sources of energy, for example, will depend on forecasts of requirements and returns in the much longer term. However, £30m more has been provided for payments to redundant mineworkers in Scenario 'B' to allow for

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further improvements in the terms of the scheme in order to give greater encouragement to men to leave the mines. The forecast assumes a substantial decline in expenditure on development of the Fast Reactor. If the UK enters a collaborative agreement to develop this technology expenditure could be rather higher, if a decision was taken to construct a Commercial Demonstration Fast Reactor it would be significantly higher. No allowance has been made for substantial Government expenditure on a Severn Barrage or on large-scale demonstration of wind or wave power or of combined heat and power schemes.

TABLE 4.2

EXPENDITURE BY THE DEPARTMENT OF ENERGY
(excluding grants to nationalised industries)

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	300	325	250	280
% GDP	0.1	0.1	0.1	0.1

4.3. Trade

Expenditure in 1979-80 was higher than in previous years but is expected to decline as grant in aid to the Civil Aviation Authority ends with the move to full cost pricing. Thereafter, expenditure can be expected to remain roughly constant in real terms at a level similar to that in 1980-81.

TABLE 4.3.

EXPENDITURE BY THE DEPARTMENT OF TRADE

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	230	220	220	220
% GDP	0.1	0.1	0.1	0.1

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4.4. ECGD

With the phasing out of loans to banks to refinance a proportion of their fixed rate sterling export lending, the main expenditure by ECGD will in future be on interest support costs. Future expenditure on this item depends heavily on market interest rates, but the total ECGD expenditure will depend on the rate of repayment of outstanding refinance.

TABLE 4.4.

EXPENDITURE BY ECGD

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	- 55	305	150	150
% GDP	-	0.1	0.1	0.1

4.5. Employment

Much of the Department of Employment's expenditure is related to the state of the labour market. But this does not imply that, in all cases, expenditure can simply be projected on that basis.

Likely policy reactions to continued high levels of unemployment are difficult to judge. But past experience indicates that expenditure on special job creation measures should most realistically be projected on the basis that it is broadly proportional to the level of unemployment (ie negatively correlated with GDP growth). Some allowance should also be made for pressures over time to contain the unit costs of schemes which take on a permanent status.

Expenditure on redundancy payments is also related to unemployment, though to its assumed rate of change rather than its level.

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However, it is doubtful whether there is any straightforward correlation between expenditure on training and the growth of GDP. Following the introduction of the Youth Training Scheme, such expenditure is planned to reach £1.5 billion in cash terms in 1984-85. It may be that faster growth could provide both the incentive and the means for employers to conduct and pay for more of their own training. Alternatively, there could be pressure for more public expenditure to accelerate the process of economic adaptation. These conflicting possibilities cannot be satisfactorily reconciled, and it would be entirely speculative to assume any shift in policy to require employers to increase their contribution to training costs. The projections are therefore based on the maintenance in real terms of planned training expenditure in 1984-85.

TABLE 4.5.

EXPENDITURE BY THE DEPARTMENT OF EMPLOYMENT

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	1455	2216	2320	2660
% GDP	0.6	0.9	0.8	1.1

4.6. Total expenditure on Programme 4, excluding assistance to nationalised industries is shown in Table 4.6.

TABLE 4.6

EXPENDITURE: INDUSTRY, ENERGY, TRADE AND EMPLOYMENT
(excluding grants to nationalised industries)

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	3065	4151	4110	4480
% GDP	1.3	1.8	1.2	1.6

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5. GOVERNMENT LENDING TO NATIONALISED INDUSTRIES

5.1. Grants to and borrowing by nationalised industries are incorporated in Section 16. Grants are subtracted from Programmes 3, 4 and 6 to avoid double counting. It is more appropriate in the context of the study to consider Nationalised Industries' demands for external financing as a whole than to separate grants and borrowing as is done in Cmnd 8494.

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6. TRANSPORT (excluding grants to nationalised industries)

Roads and Local Transport

6.1 Transport is not mentioned in the 1979 Manifesto, and there is some flexibility about levels of expenditure. Successive Roads White Papers have however identified infrastructure projects which assist industry and improve the environment as a priority.

6.2 In general, demand for expenditure on roads reflects the need to increase road space as traffic grows and to prevent uneconomic deterioration in existing roads with later increased costs of repair. Demand for local expenditure on public transport reflects in part objective difficulties of adapting traditional services to increasing competition from the private car and in part subjective judgements of the need to provide services at less than cost to various classes of traveller or to all.

6.3 Road traffic - both private car and lorry - is forecast by Department of Transport to grow despite increasing fuel prices throughout the period and for some decades beyond. If GDP grows at the upper end of the range considered traffic is likely to increase faster than Department of Transport plans at present assume.

6.4 Even though much of the motorway construction programme begun in the 1960s has been completed pressures for expenditure on road construction are likely to continue during the period. The emphasis may begin to shift away from inter-urban road building towards faster improvement of urban roads which will otherwise become increasingly congested. The need for road maintenance is likely to increase particularly in Scenario A. Although levels of expenditure on roads will remain therefore to some extent discretionary substantial reductions might add to costs in the longer term.

6.5 Demand for expenditure on local public transport is unlikely to decrease and there is a contingent threat, unless current policy conflicts with the GLC and Metropolitan Counties are satisfactorily resolved, of increases amounting to £½ to £1 billion by the end of the period.

6.6 The projections in Table 6.1 therefore assume that cost terms expenditure will continue to absorb about 1.1 per cent of GDP in both scenarios.

TABLE 6.1 EXPENDITURE ON ROADS AND LOCAL TRANSPORT*

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 Cost terms)	2410	2390	3250	2640
% GDP	1.1	1.1	1.1	1.1

*Grants to nationalised industries are covered in a separate note

6.7 Transport (excluding Roads and local transport and grants to nationalised industries): The items of expenditure covered in the part of the Department's programme are related to its administration, research and licensing. To be broadly consistent with assumptions for the rest of the programme, they are assumed to change in line with the assumed change in GDP (Table 6.2)

TABLE 6.2 EXPENDITURE ON TRANSPORT (EXCLUDING ROADS AND LOCAL TRANSPORT AND GRANTS TO NATIONALISED INDUSTRIES)

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 Cost terms)	290	288	280	240
% GDP	0.1	0.1	0.1	0.1

Note: Includes expenditure by DOE on other transport services

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6.8 Total expenditure covered in this part of the Transport programme is summarised in Table 6.3.

TABLE 6.3

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	2700	2678	3530	2880
% GDP	1.2	1.2	1.2	1.2

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7. HOUSING

7.1 Public expenditure on housing has fallen sharply over the last few years. This has resulted from substantial rent increases (which have reduced subsidies from central government and from rate funds by more than 50 per cent), combined with less capital expenditure on new dwellings by local authorities, and an increase in receipts from sales under the 'Right to Buy' legislation in the 1980 Housing Act.

7.2 These trends are unlikely to continue beyond the present financial year. Further increases in the real level of rents would be largely offset by higher rent rebates (now part of Unified Housing Benefit, covered by programme 12), so that there would be little net gain to public expenditure. Some increase in gross capital expenditure is needed simply to maintain the habitability of much of the existing stock and to replace significant numbers of post-war dwellings built by industrial methods that are now becoming structurally unsound and in many cases are completely uneconomic to repair. The peak in sales will be this year; capital receipts thereafter are expected to decline.

7.3 Housing expenditure is likely to be greater in Scenario B than in Scenario A. Private sector housebuilding would probably be lower, so that more public sector expenditure would be needed if the demand from newly-formed households was to be met and the condition of the stock maintained at a level necessary to avoid a reverse in the steady post-war rise in housing standards. Sales might be lower if tenants were deterred from buying by higher mortgage rates; while the effect of these two trends on net capital expenditure, and the higher level of nominal interest rates, would increase the costs charged to Housing Revenue Accounts and thus the need for subsidy.

7.4 In constructing projections of housing expenditure in 1990-91, it has therefore been assumed that in Scenario A the same share of GDP is devoted to housing at the end of the decade as in 1982-83 while in Scenario B it has been assumed that the share will rather less than double, with the level of provision being about the same as in 1979-80.

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HOUSING (England)	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	5541	2895	3500	5500
% GDP	2.3	1.2	1.2	2.2

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8. OTHER ENVIRONMENT SERVICES

8.1 Expenditure covered by this programme has fallen in cost terms since the mid-70s. This mainly reflects reduced levels of capital expenditure by the Regional Water Authorities (RWAs) and of capital expenditure on local environmental services (refuse collection and disposal, recreation, administration offices and services, environmental health etc). Partially offsetting these reductions has been an expansion in expenditure on urban areas, both under the Urban Programme and by the newly-created Urban Development Corporations. The reductions themselves do not however reflect a continuing decline in requirements and are not sustainable indefinitely.

8.2 In previous years, capital expenditure by RWAs has counted in PES, but it is now proposed that only finance provided by central government (grants and loans) should be included in the main programme, with net market and overseas borrowing and leasing included in the planning total. The figures in the table below are adjusted to reflect this change in treatment; for convenience and consistency with the treatment in this exercise of nationalised industries, the total External Financing Requirement is included. There has been a corresponding change to programme 3 to exclude land drainage capital expenditure by RWAs.

8.3 About three-quarters of the expenditure in programme 8 is carried out by local authorities. Under block grant, local authority priority on current expenditure on particular services (and hence the amount falling under different programmes) is largely a matter for each authority's discretion. The same applies to capital expenditure, under the new capital control scheme. Partly because of this local discretion and partly because of uncertainty surrounding expenditure in urban areas and the financing requirement of RWAs, it is difficult to establish an objective basis for determining likely expenditure trends for this programme. Nor is it clear what effects different economic scenarios might have, since higher rates of growth while possibly reducing the net cost of urban expenditure are likely to place additional strain on water and other infrastructure. It is therefore assumed that the level of provision will be the same in both scenarios, and will in 1990-91 be 10% below the 1980-81 level.

Because of the reductions already achieved since 1980-81, and assuming the EFR of the RWAs continues to decline in cost terms, this allows for some necessary recovery in expenditure on capital programmes from the present level, assuming always that current expenditure is successfully restrained.

TABLE 8.1 EXPENDITURE ON OTHER ENVIRONMENTAL SERVICES

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	3389	3117	3000	2840
% GDP	1.4	1.3	1.0	1.2

NB Figures for 1990-91 include RWAs' total external finance, and exclude their capital expenditure

9. LAW ORDER AND PROTECTIVE SERVICES

9.1 The Government places considerable emphasis on the maintenance of law and order. Specifically, authorised police establishments and actual strengths are likely to respond to crime, and other pressures. The need to achieve alignment in prisons between resources and demand is likely to present pressing problems. Following a review of the longer term prison building programme, central departments are now considering prison service manpower, the largest element of prisons current expenditure.

9.2 Although the programme is dominated by current expenditure on the police, there is no simple determinant of expenditure. For illustrative purposes the projections are based on:-

a. the projected change in population of England and Wales (plus 2% - 1980 to 1990). It is assumed that the demand for policing grows pro rata with population, other things being equal, and this increase is reflected elsewhere in the criminal justice system;

b. an assumption that the number of serious offences recorded per head of population increases by about one third over the decade, ie broadly in line with Home Office projections, themselves based on trends. Among the other factors which might lead to their modification is the change in composition of the population. For example, although the total population is forecast to increase (see para 9.2a), the number of males in the 15-24 age group, an important client group, is expected to decline by 3% over the decade and the 10-14 age group by over 25%;

c. expenditure is assumed to increase at about half⁺ the rate of "demand", reflecting improved efficiency and the effect of continuing downward pressure on public expenditure as a whole in the long run.

⁺If expenditure increased at $\frac{2}{3}$ the rate of 'demand' rather than $\frac{1}{2}$ the rate, the assumed expenditure in 1990-91 would be increased by some £200m.

TABLE 9.1 EXPENDITURE ON LAW ORDER AND PROTECTIVE SERVICES

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	3049	3417	4070	4000
% GDP	1.3	1.5	1.4	1.6

10. EDUCATION, SCIENCE, ARTS AND LIBRARIES

10.1 The projections for education have been calculated from a disaggregated analysis of the programme. Each major heading has been projected on the basis of underlying demographic determinants where these exist: for example, on the number of children of primary school age, and on a judgement of the levels of provision broadly consistent with the policies underlying the Government's present expenditure plans. These policies are aimed at 'maintaining and improving the quality of education' (Cmnd 8175) to the extent that overall expenditure constraints permit, and are thus largely determined by those constraints; the projections therefore are illustrative only. In the case of capital and some other expenditure there is no simple relationship available for converting demographic and other determinants into a demand for a stock of buildings.

10.2 The demographic basis for the projections is summarised in Table 10.1 for England and Wales.

TABLE 10.1: INDEX OF POPULATION

<u>Age Group</u>	<u>mid 1980</u>	<u>mid 1990</u>
3-4	100	130
5-10	100	96
11-15	100	74
16-18	100	85
19-22	100	104

Source: OPCS population projections 1979-2019

These figures disguise the reduction in the primary school age group in the early 1980s which is followed by an upturn between the mid 1980s and 1991. This upturn is not reflected in the 11-18 age group in the period up to 1991. The 19-22 age group peaks in the early/mid 1980s and declines thereafter. The demographic determinant is most important in the area of compulsory schooling (5-16). Outside this area, that is provision for under fives, for those over school leaving age in school, and for higher and further education (including

adult education and the youth service), there is some discretion over the numbers of pupils or students admitted - although present policy, which reflects the relevant statutory provisions, is to meet demand from 16-18 year olds for full-time courses in school or college.

10.3 The projections of current expenditure for the compulsory age groups are based on broadly constant levels of provision per pupil taking 1980-81 as a base, but with some allowance for diseconomies of scale as pupil numbers fall.

10.4 The main assumptions about the other areas of expenditure are the following:

- a. funding of nursery education based on half the change in the numbers of 3 and 4 year olds implying a decline in participation rates from 40% in 1980-81 to a little over 30% by 1990-91;
- b. funding for 16-18 year olds in schools and for all students on non-advanced courses in colleges according to projections of demand;
- c. provision for higher education (including universities) is assumed to fall by about 10% up to the mid 1980s and then decline further in line with the size of the 19-22 age group. It is assumed that this will lead to a reduction in participation rates from nearly 13% in 1980-81 to just over 11% by 1990-91;
- d. capital expenditure programmes set to stabilise after 1984-85 at some two-thirds of the level in 1980-81.

10.5 The residual components of the programme (mainly science, arts and libraries) are assumed to remain broadly constant throughout the period.

10.6 Constraints on reducing (in cost terms) the level of expenditure on the programme are imposed by:

- a. the constitutional difficulties in securing changes in local authority expenditure (75% of the programme);

b. the contractual position of staff and the extent to which employers are willing to accept redundancies. The closure of educational buildings and staffing cuts are also constrained by national and local pressures from parents of pupils and other interest groups;

c. the high proportion (65%) of the programme which is spending on staff salaries.

10.7 In practical terms, pressures to maintain expenditure levels above those implied in the projections, for example to expand above those implied in the projections, for example to expand the curriculum and to increase participation rates outside the compulsory school age group, may be very great, especially if national income is increasing relatively rapidly.

TABLE 10.2: EXPENDITURE ON EDUCATION, SCIENCE, ARTS AND LIBRARIES

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	11027	10610	10400	10200
% GDP	4.6	4.5	3.5	4.2

11. HEALTH AND PERSONAL SOCIAL SERVICES

11.1 Expenditure on the NHS and PSS needed to provide a given standard of service is determined mainly by demographic change (that is, changes in the total size and age structure of the population), by progress in medical science (including the development of new and better surgical procedures, methods of diagnosis and pharmaceutical products), and social trends affecting eg the number of children in care.

11.2 As regards demography, total current expenditure on the Hospital and Community Health Services in England would rise by about 0.7 per cent a year during the 1980s, if current provision per head in each of the main age groups remained constant. An equivalent figure for expenditure on personal social services is 0.6 per cent in the number of men and women aged 75 and over between 1980 and 1990, compared with 2 per cent for the population as a whole.

11.3 As for the cost of medical progress, DHSS had estimated that an increase in real current expenditure of about half a per cent a year is required as a contribution to the costs of medical advance to finance inescapable innovations without enforcing offsetting reductions in standards elsewhere.

11.4 For the hospital and community health services, the Government's financial provision for 1982-83 will provide for a 1.7 per cent growth in provision if savings of £39m are realised from increased efficiency (Cmd 8494, paragraph 2.11.12 and announcement of special pay offers on 8 March). This was the last year of the commitment in the 1979 Election manifesto. Such an increase would be sufficient to provide for demographic change and inescapable medical developments, with a margin for small improvements or in mental handicap services. It would also permit some "levelling up" in those parts of the country which have had least spent on them. For 1983-84 and 1984-85 Cmd 8494 allows for growth in services of 0.5% a year, to be provided by increases in efficiency, subject to further consideration during the 1982 Survey having regard to the availability of resources and the scope for improved efficiency.

11.5 If current policies were broadly maintained, and with no improvements in levels of efficiency, the annual increase in provision necessary at least to meet the pressures exerted by demographic change and medical advances might be of the order of 1-1½ per cent between 1982-83 and 1990-91. There are however many areas of health care where there is a pressing need for more resources: eg to improve standards in the worst mental handicap and other long stay hospitals, to make hip operations, transplants, dialysis etc more widely available, and to introduce minimum standards for maternity care. Expenditure would need to rise at 2-3 per cent a year to make significant progress in all these areas. On the other hand the Government is committed to securing progressive increases in NHS efficiency. The scope for this is subject to review with health authorities. It seems doubtful (though not inconceivable) that a cumulative improvement of 0.5 per cent a year could continue throughout the decade. The growth of the private sector may take a little of the pressure off NHS acute services. There could also be some small increases in income through charges. For these reasons it is suggested that the minimum net real growth in provision will be 0.5 per cent a year after 1984-85, on Scenario B. With a further 0.5 per cent a year efficiency savings, this would barely maintain present standards. If GDP rises faster there will be strong pressures to use some of the extra wealth to improve standards; health service expenditure normally rises as a percentage of GDP as GDP rises, because wealthier populations chose to spend more on health care, including care for the old and handicapped who depend on state services. It is therefore suggested that the net real growth in provision might be at least 1.5 per cent a year after 1984-85 in Scenario A.

11.6 Expenditure on the Family Practitioner Services is assumed to grow by 2 per cent a year in real terms after 1982-83. This is the assumption in Cmnd 8494 for the PES period, and is at present being reviewed.

11.7 These growth rates are based on the judgement that public expenditure cannot be substantially reduced by increasing income from charges within the present system of financing. Public expenditure could be reduced by radical changes within a tax based system (eg new charges, withdrawing certain services) or by shifting part of the

population (voluntarily or compulsorily) to private insurance. Such options would have major political implications and we have not allowed for such radical changes in the calculations in this chapter.

11.8 Capital expenditure on hospital and community health services, and both capital and current expenditure on central health services, are taken to remain constant in real terms.

11.9 Expenditure on the personal social services is estimated to have risen by some 7.1 per cent in real terms between 1978-79 and 1981-82. The provision made for 1982-83 implies a reduction; but these are services where local authorities have their own discretion. As mentioned in paragraph 11.2 above an increase in just over 0.6 per cent per annum would be needed just to keep up with demographic change. There is also pressure for increased services to meet existing deficiencies and to complement Home Office provision for children (residential care orders, intermediate treatment). An increase of 1 per cent a year in current expenditure in volume terms from 1982-83 is assumed here for Scenario B and 3 per cent on Scenario A. Capital expenditure is taken to run level in real terms, income from charges is taken to rise pro rata with current expenditure.

11.10 The relative price effect for pay is calculated for the NHS and personal social services together on the same assumption as those applied to other public services. For the hospital and community health services the RPE on current expenditure other than pay has been estimated at 1.5 per cent over the period 1976-1980. Whether this RPE will continue is very uncertain, but the same figure has been used here for the period beyond 1982-83 for the purposes of calculation only. For the Family Practitioner Services the relative price effect on current expenditure other than pay is put at 2.5 per cent a year over the period 1976-80 and is again used for the purposes of calculation with the same qualifications applying.

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TABLE 11.1 EXPENDITURE ON HPSS IN ENGLAND (NET OF CHARGES)

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	10494	11341	14110	13330
% GDP	4.4	4.8	4.8	5.4

12. SOCIAL SECURITY

12.1 The Scenario B projections are based on price protection of all benefit levels, no changes in eligibility for benefit and no changes in current take-up assumptions. Scenario A assumes a 1 per cent per year growth in the real value of existing benefits. This is assumed to cover also any structural improvements. This would not cover any major development such as the introduction of a comprehensive disability benefit (which might cost up to some £3b pa). In both Scenarios benefits are assumed to fall relative to wages.

12.2 A number of benefits are covered by legislation requiring annual uprating in line with prices. In some cases, such as pensions, there are firm Ministerial commitments to increase benefits in line with inflation. Supplementary benefit and child benefit is in practice increased in line with prices. Child benefit has been increased in line with inflation in 1981 and 1982. In both cases there is considerable political pressure at least to maintain the real value of the benefits.

12.3 The base taken for the projections to 1990-91 is that of the 1982 White Paper. Apart from the uprating assumptions mentioned above, the major determinants of expenditure in 1990-91 are:

- i. demographic (in particular the number of pensioners and of children);
- ii. unemployment (both number and composition of the unemployed);
- iii. the growing maturity of the new pension scheme;
- iv. increase in the population qualifying for certain benefits (eg sickness benefit and contributory benefits payable to married women).

12.4 Approximately half of the programme is accounted for by retirement, widows' and invalidity pensions. The number of pensioners will not increase greatly by 1991 (although thereafter the number of retired persons as a percentage of the working population increases rapidly). Nor does the new earnings-related pension scheme

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have any major impact during the 1980s. For child benefit the number of 0-16 year olds had been used as an indicator. The population projections show this number falling until 1986 and recovering by 1991 to current levels.

TABLE 12.1 EXPENDITURE ON SOCIAL SECURITY

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	22878	26646	28560	27320
% GDP	9.6	11.3	9.7	11.1

13. OTHER PUBLIC SERVICES

13.1 Expenditure on Other Public Services is subject to periodic increases depending on the timing of Parliamentary elections and censuses. Apart from these items, and the change to Trading Fund status for HMSO, expenditure has been roughly constant in cost terms over the past few years. Most of the programme is accounted for by the costs of the Inland Revenue and Customs and Excise.

13.2 A major item of expenditure occurring after the current Survey period is the computerisation of PAYE, which will involve capital expenditure of around £200m, but result in large savings of staff costs. Apart from this change, the figures below assume that the level of expenditure on this programme remains broadly constant in cost terms.

TABLE 13.1: EXPENDITURE ON OTHER PUBLIC SERVICES

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	1143	1140	1160	1140
% GDP	0.5	0.5	0.4	0.5

14. COMMON SERVICES

14.1 Two major items of expenditure under Common Services are accommodation services, provided by PSA, and civil superannuation.

14.2 A recent PSA report suggested that, with the cuts in the civil service presently planned, rationalisation of the estate could lead to savings of £37m pa (including rates) in London alone. However, offsetting this saving is the need to catch up with capital and maintenance expenditure which have been postponed to reduce the present level of expenditure. Only modest savings beyond those already identified may therefore be possible, unless civil service numbers are further reduced. The figures below assume further savings in cost terms up to the mid 1980's and thereafter a level programme.

14.3 Expenditure on civil superannuation is also partly dependent on the size of the civil service, both because of the additional costs of early retirement schemes, and through the effects on the total number of public service pensions. While showing quite a considerable increase in present plans, due to a retirement 'bulge' (including voluntary early retirement), expenditure in cost terms is expected to revert to a level about 10 per cent higher than that in 1980-81.

TABLE 14.1 EXPENDITURE ON COMMON SERVICES

	1979-80	1982-83	1990-91	
			A	B
£m (1980-81 cost terms)	1195	1358	1170	1100
% GDP	0.5	0.6	0.4	0.4

CONFIDENTIAL

15. SCOTLAND, WALES AND NORTHERN IRELAND

15.1 Projections for territorial programmes have been made using present assumptions for the relationship between them and relevant English programmes. Expenditure outside the territorial blocks is assumed to remain broadly at its 1982-83 level in cost terms.

TABLE 15.1 EXPENDITURE IN SCOTLAND, WALES
AND NORTHERN IRELAND

	1979-80	1982-83	1990-91	
			A	B
Scotland £m (1980-81 cost terms)	5216	5043	5770	5650
Wales £m (1980-81 cost terms)	2087	2016	2290	2250
Northern Ireland £m (1980-81 cost terms)	2888	2950	3130	3110
TOTAL £m (1980-81 cost terms)	10,191	10,009	11,190	11,010
% GDP	4.3	4.4	3.8	4.5

16. NATIONALISED INDUSTRIES

A - GENERAL

Existing Policies

16.1 The Government's policy towards the nationalised industries has three major long-term elements:

- i) Financial targets. These take account of the need for investment programmes as a whole to earn a 5 per cent real rate of return, and of further moves to economic pricing. Financial targets are in place for most of the industries, the main current exceptions being loss-makers such as the National Coal Board, the British Steel Corporation and British Shipbuilders. The British Railways Board at present only has financial targets covering Sealink, the Inter-City services and the freight business. Loss-makers in most cases have a long-term duty to break even after grant.
- ii) Improvements in efficiency both as a result of closer scrutiny by the Government and the Monopolies and Mergers Commission, and through greater competition. The setting and monitoring of performance aims will also have a part to play.
- iii) Privatisation of both whole industries and individual activities and assets. By the early 1990's it is reasonable to assume that the whole of British Airways, and parts of the British Steel Corporation and British Shipbuilders, will have been returned to the private sector, in addition to the British Transport Docks Board and Britoil (which are expected to be privatised within the next year). British Telecom may also have been privatised, although this is still subject to substantial uncertainty. Where an industry or activity with a positive external financing requirement is being returned to the private sector, this will lead to continuing reduction in public expenditure; but most privatisation candidates are

profitable and have small or negative external financing requirements. In these circumstances, there will be no continuing net benefit to the Exchequer after the original sale has been made. The proceeds from sale will generally be counted as part of the special asset disposals programme, and so will have no net effect on total external finance for the nationalised industries.

16.2 Cmnd 8494 carried these policies forward on the basis of a forecast reduction in total external finance for the nationalised industries from £2.7bn in 1982-83 (before adjustment for the effects of the National Insurance Surcharge reduction) to £2.1bn in 1984-85. This expected improvement is also associated with a modest resumption of economic growth.

Long-Term Prospects

16.3 Forecasts of the difference between industries' total revenues and expenditure in cash terms are subject to greater uncertainty than are forecasts of other items of public expenditure; even the later year plans in Cmnd 8494 are subject to large margins of error. Forecasts for the early 1990's cannot give more than a rough indication of possible changes. However, assuming the continued implementation, and success, of the Government's policies, the following general picture emerges:

i) Investment The level of investment will depend in part on economic growth. But many of the industries have excess capacity at present; in others current investment may well be occurring to save costs rather than increase capacity; in yet others output levels and hence investment may be more or less invariant to economic growth. For example, the electricity industry currently has a large quantity of spare capacity; NCB output may be invariant to growth, and the Gas Corporation may well need to invest more with higher growth. Whether the real level of investment changes significantly may well depend above all on changes in technology - eg in the energy sector. Overall, total nationalised industry investment is unlikely to expand very much in real terms from its present level. For the purpose of this paper a reasonable assumption is that it

will remain constant.

- ii) Internal resources Assuming some modest continuation of economic growth, continued restraint on current costs and improvements in efficiency, the industries' internal resources should increase steadily, although even this judgment is hazardous. For example, price competition - itself aimed at improving efficiency - would tend to reduce the industries' operating profits. Movements toward economic pricing may in any event be more or less complete by the mid-1980s.
- iii) External financing In the absence of a major increase in investment, and assuming that the industries' internal resources continue to improve following the implementation of the Government's policies, the nationalised industries' external financing requirements should continue to decline gradually. Within the total, finance for the two main loss-makers (the National Coal Board and British Rail) - already responsible for threequarters of the nationalised industries' total external finance in 1981-82 - will remain predominant. In turn, grant would probably account for the majority of nationalised industry external finance, as is planned for 1982-83. But the pattern depends particularly heavily on the future of British Telecom. If the industry remains in the public sector, and has a continuing large investment programme, there could well be a large external financing requirement - perhaps as high as £500m.

16.4 The projections assume continued implementation and success of government policies in all industries and the picture they show is thus arguably an optimistic one. Some account needs to be taken of important risks - for example that growth will be lower than expected, that hoped-for improvements in efficiency will not fully materialise; and that world energy prices grow more slowly than at present projected. Adverse developments even in one or two industries could well cause the outturn to be significantly worse than the total of the individual industry figures implies. To provide a more realistic view of the prospect for nationalised industries as a whole, a contingency margin of £300m - not allocated

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to any individual industry - has been included in the aggregate figures for Scenario A and Scenario B.

16.5 This produces the following picture for the nationalised industries as a whole (including in both cases an assumed £500m for British Telecom).

Table 16.1

NATIONALISED INDUSTRIES' EXTERNAL FINANCE
(excluding Civil Aviation Authority)

£ million, 1980-81 cost terms

	1979-80	1982-83*	1990-91	
			A	B
Borrowing	1,796	778	700	690
Grants	1,280	1,515	870	920
Total of individual industries' external finance	3,076	2,293	1,570	1,610
Contingency margin	-	-	300	300
Total external finance	3,076	2,293	1,870	1,910
% GDP	1.3	1.0	0.6	0.8

*Figures do not take account of adjustments to EFLs in light of NIS reduction and other changes.

NOTE: Rough adjustments have been made to Programmes 4,6, 8 and 15 to take account of grants to nationalised industries scored as external finance.

National Coal Board

The plans prepared by the Board project declining external financing requirements, particularly through the late 1980's, and a return to profitability. These are also the aims of Government policy. Although capital investment might grow in real terms towards the end of the decade, the key question is how fast the Board's performance on revenue account can improve. Given the difficulties

of adjusting NCB output, higher economic growth with attendant increased energy demands ought to improve this performance and continued emphasis on cutting costs should also lead to a marked improvement over the coming years. In 1980-81 cost terms, it is assumed that the total external financing requirements of the Board will fall from some £1100m in 1981-82 including some £500m in grants to some £200m-£400m, including £100m-£200m in grants, in 1990-91 in Scenarios A and B respectively.

Electricity Supply Industry

The Electricity Supply Industry in England and Wales is projecting some real increase in capital investment during the latter half of the 1980's. Assuming that no significant change is made to the current approach to pricing, the industry should continue to make significant profits before interest. It has been assumed, therefore, that the current negative external financing requirement would become zero by 1990-1991. It has been assumed that there will be no further investment in generation in Scotland following Torness so that the combined external financing requirements of the Scottish Electricity Boards might also fall to zero by 1990-1991.

British Gas Corporation

British Gas Corporation's investment is currently at a high level, owing to the development of the Rough and Morecambe fields and the strengthening of the national transmission system. As these projects are completed and with the privatisation of the Corporation's peripheral activities, there should be a substantial reduction in the Corporation's investment in the later 1980's. On the revenue side, the gas levy can be adjusted to fine-tune the Corporation's net income. Assuming a continued policy of economic pricing, it is likely that BGC will have a zero or negative external financing requirement in 1990-91. In Scenario B, it could have a more substantial negative EFR, at the same rate of gas levy, since the need to develop new capacity and more costly sources of gas would be deferred.

BNOC

BNOC should be taken out of the calculations given the planned

privatisation of Britoil. It is assumed that the external financing requirement of the residual trading body will be negligible.

British Steel

Present policy is to return individual businesses to private hands and to close any unprofitable rump. The speed of moves in this direction will only partially depend on UK economic growth and steel demand, and the £/DM exchange rate (European steel prices are effectively denominated in DM). The assumption is that privatisation and/or closure is complete or at least that any plant remaining in the hands of the State has no EFR.

British Telecommunications

If BT has not been privatised by 1990-91, its external finance will depend on 3 main factors: its efficiency; the extent to which competition (where it can be introduced) still enables it to maintain a high self-financing ratio; and the scale of its investment programme. One possibility is that its investment requirements may tail off after the present bout of modernisation is completed in the late 1980's. But technological change and the wider exploitation of profitable opportunities in "teletronics" could well mean a continuing high investment programme. On this assumption, a figure of £500 million has been included in both scenarios.

Post Office

In recent years the PO has been a small net repayer of debt. In spite of changes which may affect its business during the 1980's - electronic mail, cable systems, etc, it is assumed that there will be no external finance requirement in either scenario.

British Airways

The Government's policy is to privatise British Airways as soon as practicable. It is assumed that profitability and/or capital reconstruction allows this to occur by the middle 1980's.

National Bus

NBC has been set financial targets which, if met, ought to ensure that there is an operating surplus which, together with depreciation, should cover investment. Such a position should obtain in both scenarios A and B. NBC also receive grants from local authorities which are expected to remain constant in real terms, at around £50m in 1980-81 prices.

British Waterways Board

In both scenarios, grant to the BWB is assumed to remain at around its present real level, at £30m (1980-81 cost terms). Borrowing is assumed to be negligible.

British Transport Docks Board

Assumed to be privatised.

Scottish Transport Group

The STG is not expected to be a net borrower in either scenario but is assumed to receive local authority grant totalling £15m in 1980-81 prices.

British Shipbuilders

The present policy is to eliminate subsidies and to privatise. Disposal of BS Ship repair interests and peripheral engineering establishments could take place before the election and privatisation of Vickers after the election, but the prospects are speculative. While direct production subsidies for merchant ships will have ended (the Home Credit Scheme continuing) both merchant shipbuilding and offshore rig building are highly cyclical industries, and BS could well need further finance to cover losses on the down-slopes of the cycles or to finance further contraction in both these areas. It is unlikely that contraction in BS will have run its course as early as 1999-91 but in the good years of the cycles BS could be profitable and dividend-paying though much will depend on the intensity of the Japanese and South Korean competition.

British Airports Authority

The BAA is in normal circumstances self-financing but this will not be possible during the proposed major expansion of its South East airports. On the present timetable the major part of the expenditure on this programme is not expected to be completed until 1990 at the earliest. Depending on the growth of traffic the programme could be extended into the mid-1990s. In any case a requirement for a small EFL (of say £30m in 1990-91) could emerge.

British Rail

In both scenarios the level of grant might be expected to decline from its present historically high point which is due in part to the depth of the recession. Borrowing, on the other hand, is at a historically low level, due to the historically low levels of investment which result from the Board's decision to restrict capital expenditure to reduce their need for external finance.

The future level of both grant and borrowing will depend on BR's ability to restrain their current costs. The forecast assumes that the Board will succeed in reducing their costs in accordance with Government policies and make other changes, including investment, to adapt the railway to the needs of the modern community.

Assuming grant declines to the mid-1980s and then remains constant, and a modest programme of investment (including electrification) peaking in the mid-1980s, the Scenario A case produces borrowing figures of £30m-£50m at 1980-81 prices in 1990-91 and grant of £650m-£700m. Scenario B assumes lower investment and net borrowing of some £20m-£40m. Grant, of around £600m-£650m, would however be likely to be lower than in Scenario A because of the lower assumed growth of wages. (For the purpose of constructing aggregate figures, the mid-points of these ranges have been taken.)

CONFIDENTIAL

Civil Aviation Authority /not strictly a nationalised industry/

Once the major programme of re-equipment is completed capital expenditure should decline and a zero borrowing requirement is projected for the early 1990's. The requirement for a Scottish Development Department grant towards the costs of Highlands and Islands aerodromes is expected to remain constant in real terms, at around £4m at current prices.

17. ASSET SALES, CONTINGENCY RESERVE AND DEBT INTEREST

17.1 Asset sales are assumed to be largely complete by 1990-91, but this depends on the timing of decisions yet to be taken. The assumed rate of sales during the 1980's affects the projected demand for external finance for nationalised industries at the end of the decade.

17.2 The Programme Totals for 1990-91 include a 2 per cent Contingency Reserve, similar to that for 1982-83.

17.3 Projections of net debt interest are very uncertain. However, it is assumed to decline to 2 per cent of GDP in Scenario B; and in Scenario A, with lower inflation and interest rates, it is assumed to decline to 1.5 per cent of GDP.

20 JUL 1982



Maken

MUS 29/7

CONFIDENTIAL

*Top Copy Sealed on
Economic Policy,
Public Sector Pay, Pt 8*

MR. SCHOLAR

cc Mr. Mount
Mr. Walters
Mr. Ingham

Edwards
[Signature]

Public Expenditure: Public Service Pay

In his letter of 26 July to Sir Robert Armstrong's office, copied to you, the Chancellor's Private Secretary explains that the Chancellor will seek a decision from Cabinet on 30 September on the treatment of public service pay in 1983/84 for the purposes of the public expenditure survey. The main decision required is whether there should be an announced pay factor, and if so what.

This timetable, and the decisions which are taken, are central to the handling of the pay negotiations with the local authority manuals, which may be expected to set the pace for the whole of the public service pay round. Hitherto, it has been necessary to announce a pay factor for the Rate Support Grant in the course of September, which has had a considerable impact on the local authority employers' attitude to their negotiations. But the move to cash planning means that a separate pay factor is no longer absolutely necessary, and it would be perfectly feasible for the local authority employers to proceed on the basis of Mr. Heseltine's statement yesterday. I was grateful to you for arranging for that statement to incorporate the passage I suggested on pay; nonetheless, DOE have confirmed to me that, as I suspected, most local authorities will read the statement as broadly endorsing a 5% pay assumption. If there is no other pay factor announced, 5% is therefore likely to become the floor for the public service pay round.

It is not absolutely essential for any separate pay factor to be announced in the course of September, because the negotiations with the local authority manuals are unlikely to begin until early October; but I understand Mr. Heseltine is seeking a meeting with LACSAB (the employers) around 15/16 September, with a view to encouraging them to lower their sights: from that point of view, it would be helpful to have a decision on a separate pay factor before then.

As the Prime Minister already knows from my note of 24 June briefing for the E discussion on the next pay round, we do not

CONFIDENTIAL

/believe

believe that public service settlements even as low as 4% - implying an overall earnings growth of 6% - would be consistent with the Government's objective of a low pay round which would make a significant contribution to employment. We think therefore that there should be a separate pay factor, well below the 5% on which the local authorities are likely to be working; and that it should be announced as early as possible in the autumn. The recent decision by MISC 83, which the Chancellor will be reporting to the Prime Minister shortly, broadly to endorse the recommendations of the Megaw Inquiry, make it all the more important to set strict limits at the beginning of the pay round if public service pay is not to drift back up into double figures. I know from a brief exchange with him that the Chancellor's own mind is not yet made up on the need for a pay factor this time round; I wonder if the Prime Minister might feel that this is a suitable issue for discussion with the Chancellor at her next regular meeting with him?



28 July 1982

CONFIDENTIAL



Mr Ricchetti
 NUS 30/7
 horse
 Farrell
 NUS 30/7

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

D J Wright Esq
 Cabinet Office

26 July 1982

Dear David,

PUBLIC EXPENDITURE AND RELATED CABINET BUSINESS

It might be useful to record the target dates to which we are at present working for the next few Cabinet meetings on these subjects.

Following the Cabinet on 15 July, the Chief Secretary has a mandate to carry out bilateral discussions with spending Ministers. He hopes to start these at the end of July, but most will be in September.

The Prime Minister has agreed that there should be a separate Cabinet discussion of long term public expenditure trends, based on the existing report from officials and on a paper by the CPRS. The idea so far has been that this should be on 9 September.

Following the recent discussion in E Committee about pay, the Chancellor intends to return to Cabinet with further proposals in the autumn. In particular, he will seek a decision then on the treatment in the decisive phase of the public expenditure Survey (and subsequently for the Estimates) of public services pay in 1983-84, and when this should be made known publicly. Because of the Prime Minister's absences, we understand that the most convenient date for this will be 30 September.

This discussion will (we hope) remove remaining uncertainties about the provision to be made for pay in public expenditure programmes, and allow the Chief Secretary to complete his bilateral discussions, and to report back to Cabinet towards the end of October. The provisional date for this meeting is 21 October. Because of the Chancellor's absences and the need to circulate papers a week in advance, the meeting cannot be earlier than this. It will be prudent to assume that Cabinet will want more than one meeting to dispose of the matter. The continuation meeting might be on 28 October (or whenever Cabinet meets that week, if the Prime Minister's visit to Bonn entails any change in the usual pattern.)

It is difficult to look further ahead. If major problems are left, there might need to be a further round of bilateral consultations, leading to a further report back to Cabinet in November. At this point, we do not think these remaining stages can usefully be planned.



I should be grateful for your confirmation that these dates remain suitable. Meanwhile, the Treasury will continue to work on this basis.

I should perhaps also mention that, for internal planning purposes, we are at present proceeding on the assumption that the Budget will next year fall on 15 March. 27 January or 3 February might therefore be a suitable date for a "pre-Budget" Cabinet.

I am sending a copy of this letter to Michael Scholar at No 10.

Yours ever,

J O Kerr

J O KERR

CONFIDENTIAL

ec. JV

VB



Econ 106

10 DOWNING STREET

From the Private Secretary

23 July 1982

Dear David,

End-Year Flexibility for Public Expenditure Programmes

The Prime Minister has seen your Secretary of State's minute of 20 July about end-year flexibility, together with your letter to me of 22 July about the House of Commons Defence Committee's recommendations on this point; and the Chief Secretary's minute also of 22 July. She has also seen Sir Derek Rayner's letter to the Chief Secretary on the same subject.

The Prime Minister thinks that the Chief Secretary's memorandum on this subject (C(82)29) will best be discussed in October.

I am sending a copy of this letter to John Kerr and Terry Mathews (HM Treasury) and David Wright (Cabinet Office).

Yours sincerely,

Michael Scholar

D.B. Omand, Esq.,
Ministry of Defence.

CONFIDENTIAL

do



Foreign and Commonwealth Office

London SW1A 2AH

22 July 1982

Prime Minister

To note

AOL 24.

Dear John,

Public Expenditure Survey and Net Contributions to European
Community

The Foreign and Commonwealth Secretary has seen a copy of John Kerr's letter to you of 13 July about the figures for net contributions to EC institutions which will appear in this year's public expenditure survey.

He understands the Chancellor's concern that the actual figures for 1983 - 84 and later could be worse than the survey figures. The immediate problem is one of presentation in view of the presumption that the same figures will be published in the White Paper next March, unless some agreement is reached in the Community before then. On the one hand, we do not wish to publish figures which are so high as to weaken our negotiating position, but on the other, we may face criticism domestically if the outturn in future years turns out to be considerably worse than the forecast. It is the latter possibility which is of particular concern in relation to the figures proposed in the letter, as indeed the letter points out.

We realise that the new figures are based on revised estimates of our unadjusted net contributions, but these estimates are extremely uncertain, as we have discovered in the last two years, and are liable to be drastically altered as a result of such unpredictable factors as world agricultural prices. The Foreign and Commonwealth Secretary feels strongly that it would be wiser to reduce the risk of overshoot by leaving the estimates for 1983/84 and later unaltered from those in the last White Paper. As far as our negotiating position was concerned, this would mean that our partners found only figures which they had seen before.

/In explaining

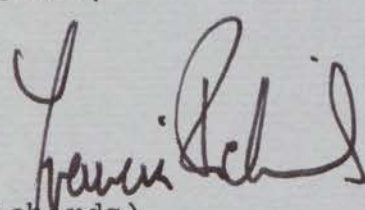


In explaining the figures, we would be able to say that the 1982/83 figures had been changed to take account of the agreement on 1982 refunds, but that for later years the Government had not thought it necessary, in view of the very many uncertain and conflicting factors involved in estimating the unadjusted net contribution and of the delicacy of the estimates in relation to our Community partners, to alter the estimates made in last year's White Paper.

If the Treasury were pressed on the justification for leaving the estimates of the unadjusted net contributions for 1983/84 and 1984/85 unaltered, despite the improvements which should result from the payment in the two years of refunds of £115 m delayed from 1982/83, they could I think take the following line:

estimates for these years are clearly very uncertain and subject to numerous factors which are difficult to quantify. Against the reductions resulting from late payments of 1982 refunds must be set the increases which would result if we assume that the same change in the timing of payments were to repeat itself in respect of refunds for 1983 and 1984. Overall the effect of these factors would be some increase in public expenditure in 1983/84, and no change in 1984/85. However other factors, in particular the lower forecast unadjusted net contribution in respect of FEOGA pointed to some reduction in the 1983/84 forecast. Hence our conclusion that, on balance, it was reasonable to leave the figures as they were.

I am copying this to the Private Secretaries of Members of the Cabinet, and to David Wright in the Cabinet Office.

For covs,

 (F N Richards)
 Private Secretary

A J Coles Esq
 10 Downing Street



10 10 10
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9 2 JUL 1982

10 10 10

Econ Ref
Public Exp PL20



Prime Minister ① cc JV
4 pps

PRIME MINISTER

Please also see the two minutes from Mr Nott and one from Sir D Rayner (attached). I see little alternative but to postpone a Cabinet discussion at X, given that you will not wish to confuse the Sept 9 long-term

END-YEAR FLEXIBILITY FOR PUBLIC EXPENDITURE PROGRAMMES public expenditure discussion with this issue.

The Secretary of State for Defence sent me a copy of his minute to you of 20 July. - attached to Pt 20

Yes not Agree?

PLS 22/3

pt 19 — 2. I fear he has misunderstood the point of my memorandum C(82)29 about end-year flexibility. I was not recommending a scheme for flexibility. I was reporting to Cabinet, as required by an earlier remit, the work which has been done by officials in drawing up such a scheme.

3. The report is worded neutrally. It outlines the kind of scheme which might be practicable if it could be afforded. But as I said in my covering note, allowing the carry-forward of underspending would add to total public expenditure.

4. The Treasury view (which I realise Ministry of Defence officials do not fully share) is that the cost of the limited scheme described in the paper would be of the order of £300 - £450 million a year. The Cabinet decisions on public expenditure on 15 July precludes an addition of this size to the existing planning totals.

* 5. I hope therefore that the Secretary of State will not press his argument. But if he must, I suggest that a decision should be reserved until October, when I report back to Cabinet on the results of my bilateral discussions with spending Ministers, and we can see more definitely the overall position for 1983-84 and

later years. I must advise against a separate discussion now of end-year flexibility for only one Department, because it would involve taking decisions out of their proper context.

6. I am sending a copy of this minute to the Secretary of State for Defence and to Sir Robert Armstrong.

L.B.

LEON BRITTAN
22 July 1982

22 JUL 1982



COMPTON



MO 8

MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1

Telephone 01-~~934 7022~~ 218 2111/3

22nd July 1982

Dear Michael,

END YEAR FLEXIBILITY FOR PUBLIC EXPENDITURE PROGRAMMES

Following his minute to the Prime Minister of 20th July, the Defence Secretary has asked me to draw to your attention the recommendation which will appear in the report to be published today by the House of Commons Defence Committee, in favour of end year flexibility. The relevant extract is as follows:-

"We note that the Treasury is to undertake a complete review of the question of end year flexibility, but is already raising objections to the likely cost of such a scheme (which the Treasury claim to be about £300 million a year for all Government Departments). We do not accept the Treasury's arguments. We recommend that the Ministry of Defence continue to press the Treasury to study possible reforms and that the Treasury agree a satisfactory scheme so that the Ministry of Defence will be able to achieve end year flexibility by the end of the 1982-83 financial year."

(Second Report from the Defence Committee, Session 1981-82
"MOD Organisation and Procurement")

I am copying this letter to John Kerr and Terry Mathews (HM Treasury) and to David Wright (Cabinet Office).

Yours end

(D B OMAND)

David Omand

M C Scholar Esq

MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1

Telephone 51-971 7071



22 JUL 1982

RECEIVED
GENERAL SECRETARY
MINISTRY OF DEFENCE
WHITEHALL LONDON SW1



MO 8

PRIME MINISTEREND YEAR FLEXIBILITY FOR PUBLIC EXPENDITURE PROGRAMMES

pt 19 - I understand that it is unlikely that we will be able to discuss at Cabinet on Thursday the memorandum by the Chief Secretary C(82)29 on end year flexibility. As you know I refrained from raising this detailed subject last week when we had our general economic discussion, but I do feel that we must now move ahead and take a decision to introduce end year flexibility.

2. The Chief Secretary has brought the arguments together in a constructive and helpful way in his memorandum. Limited end year flexibility of the scale proposed will contribute substantially to the major improvements in financial management in the Ministry of Defence. We are all committed to a more efficient and effective civil service, and we must give our financial managers the tools for the job.

3. As regards the substance, I believe that the Ministry of Defence's scheme for Voted flexibility has advantages over the alternatives. But if, as it seems, this does not command general agreement then I should certainly be prepared to support fully an administrative scheme for flexibility along the lines put forward by the Chief Secretary in his paper. If necessary I would be prepared to see this introduced in defence on an experimental basis.

4. I am sending copies of this minute to the Chancellor of the Exchequer, Chief Secretary and to Sir Robert Armstrong.

Ministry of Defence
20th July 1982

JV .



20 JUL 1962



COMPTON



s/c sv

MANAGEMENT AND PERSONNEL OFFICE

WHITEHALL LONDON SW1A 2AZ

Telephone Direct line 01-273 3508
GTN 273
Switchboard 01-273 3000

2 July 1982

The Rt Hon Leon Brittan QC MP,
Chief Secretary to the Treasury.

END-YEAR FLEXIBILITY FOR PUBLIC EXPENDITURE PROGRAMMES

1919 - Your private secretary has sent me a copy of your memorandum
C(82)29 of 8 July 1982.

2. I am pleased that you have favourably reconsidered a proposal that regrettably had to be shelved on grounds of cost when it was put forward in 1980. In writing to John Biffen as your predecessor on 7 August 1980 I expressed my firm belief that the 'annuality rule' led to inefficiencies, and my hope that the then-proposed scheme could be introduced that year. I welcome the scheme now proposed for flexibility on underspending as described in paragraph 19 of the paper attached to your memorandum and I hope a way will be found of implementing it as soon as possible.
3. A solution to the problem of cost in 1984-85 and subsequent years is suggested by paragraph 4(i) of the paper. There need be no net increase in public expenditure as a whole if a way can be found of reducing planned expenditure (on a programme-by-programme or department-by-department basis) to accommodate the underspending carried forward from previous years. I accept that there are difficulties in estimating the amount of the carry forward (which is why schemes such as those operated by the ODA and the Health Authorities provide for adjustment in the next year but one) but the maximum percentage carry forward would be limited in advance, and I believe the benefits to be obtained from a scheme would justify the devotion of some official effort to making it work.
4. I am sending copies of this letter to your Cabinet colleagues.

DEREK RAYNER



2 JUL 1982





20
c.c. BI

Econ Pol.

10 DOWNING STREET

From the Private Secretary

19 July, 1982.

Cash Limits in 1981/82

The Prime Minister agrees to the publication of the White Paper on Cash Limits in 1981/82, attached to the Chief Secretary's minute to her of 15 July. She agrees to the publication on Thursday, 29 July, after Question Time, as proposed.

I am sending copies of this letter to the Private Secretaries to the other Members of the Cabinet, to Murdo Maclean (Chief Whip's Office), and David Wright (Cabinet Office).

M. C. SCHOLAR

Terry Mathews, Esq.,
HM Treasury.

SK



MINISTER FOR LOCAL GOVERNMENT
AND ENVIRONMENTAL SERVICES

Copied to local gov Mar 1987
Water Industry
DEPARTMENT OF THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

Prime Minister (2)

Mus 19/7

16 July 1982

cc to

ms

Dear Geoffrey,

In your letter of 29 June to the Prime Minister on the public sector monitoring report, you asked me to let you know what options I thought we had to put the brake on the special water negotiations.

Since your letter we have of course announced the abolition of the NWC and have put out a consultation document as to which of the present functions of the NWC need to be continued, and, of these continuing functions, what are the best ways in which they could be discharged. One of the key current functions is, of course, the national wage negotiations for the various groups of employees in the water industry. At the present moment it is therefore not clear under what arrangements the special water negotiations and the normal wage negotiations will take place. In this new situation I am very much seized of exactly the dangers that concern you about the possible progress on the separate negotiations. For the reasons that I have mentioned I cannot at this moment give you any accurate forecast of exactly how the immediate situation is likely to develop but my purpose in writing is to confirm that I shall keep in as close touch as possible with developments and with a number of key people concerned and will report to you again as soon as I am able to do so.

I am sending a copy of this letter to the Prime Minister and to those to whom you copied your minute.

[Handwritten signature]

TOM KING

19 JUL 1982



PERSONAL
COVERING CONFIDENTIAL



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

PA

15 July 1982

Michael Scholar, Esq.,
10, Downing Street

New Michael,

*To W Treasury to
postpone until after
economic debate
rus*

LONG TERM TRENDS IN PUBLIC EXPENDITURE

In your letter of 21 June to me you recorded the Prime Minister's agreement with the approach set out in the Chancellor's letter of 15 June to her. I understand that you have since discussed with Russell Barratt how best to inform others in Cabinet of the plan, and have agreed with him that the best scheme would be for the Chancellor to minute again to the Prime Minister, enclosing a copy of the officials' report, and suggesting that it be discussed at a September Cabinet, for which the CPRS might provide a paper. You would then reply, conveying the Prime Minister's agreement. Copies of both minutes would of course go Cabinet-wide.

.....
Could you confirm that this is indeed your understanding of what should now be done? The Chancellor would then minute tomorrow as in the attached text.

Yours ever,
J.O. Kerr
J.O. KERR



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

PRIME MINISTER

LONG TERM TRENDS IN PUBLIC EXPENDITURE

In my minute of 8 March, I suggested that officials should undertake an examination of the likely pattern of public expenditure over the next decade.

- ... 2. This study has now been completed and I attach a copy of a report by a group of officials on which the main spending Departments, and the CPRS, were represented. The report considers what, on the basis of certain hypotheses about developments in the economy on the one hand and expenditure programmes on the other, public expenditure might amount to by 1990.
3. As expected, the picture is bad. Only on hypotheses that are rather favourable as regards the economy, and relatively modest as regards expenditure programmes, does public expenditure as a percentage of GDP come out lower in 1990-91 than it was in 1979-80. In cost terms the prospect on any of the hypotheses is for big increases over this period.
4. The report shows clearly how the balance of our public expenditure programmes has changed and will, on present policies, continue to do so. It also shows the extent to which the four largest programmes - social security, health, education and defence - dominate public expenditure. In 1979-80 the four programmes between them amounted to about 60 per cent of the total. By 1990-91, on these projections, they would amount to about 63½ per cent, even in the "best case". Within that, defence would take a higher proportion and education a smaller proportion of the total.



5. The officials' report looks forward, and shows a generally rising trend of future expenditure. Forecasting in an uncertain world is difficult. But if we look backwards over the last twenty ... years (Table A annexed) a consistent upward pattern emerges, broken only by the two external crises of 1967 and 1976. Even then, the upward trend was soon resumed.
6. Clearly we cannot go on like this. If we are to break the pattern decisively - as we must - then we shall need to consider radical changes affecting most, if not all, areas of policy. Unless we are willing to tackle some pretty basic questions in a fundamental way, then, so far from being able to offer the chance of some easing of the tax burden (clearly desirable for industrial recovery) we should face instead the prospect of endlessly recurring "public expenditure crises".
7. It would, I am sure, be helpful if Cabinet was now able to engage, on the basis of the officials' report, in a very broad-ranging discussion about the Government's long-term objectives for the size and shape of the public sector. We should not be inhibited at this stage by such considerations as the need for legislation, the existence of past commitments or the alleged political impossibility of change. A discussion of this kind would pave the way for some major strategic decisions affecting our programmes as a Government for the next Parliament.
8. Obviously there is some connection between decisions on this year's public expenditure Survey, at any rate as regards the last year 1985-86, and the longer term. Nevertheless I believe that it will be more conducive to the kind of broad exchanges that I have in mind if our discussion of the longer term is distanced somewhat from our preoccupations with the Survey.
9. It seems to me that it would be difficult to conduct an adequate discussion about the longer term within the framework of our regular



Cabinet meetings, and that some special arrangements for this discussion will be needed - perhaps a specially convened meeting of the Cabinet. If such a meeting took place in September, it could also form part of the preparation for this year's Party Conference, at which we shall no doubt be under pressure about various aspects of public expenditure.

10. I should of course circulate a paper of my own for discussion with the officials' report. I hope too that we might look to the CPRS for support in the form of a paper pointing up some of the longer term options open to us, especially as regards the possibilities for major structural changes affecting the largest expenditure programmes.

11. I am sending copies of this minute and the officials' report to members of the Cabinet, Sir Robert Armstrong and Mr. Sparrow.

G.H.

July 1982

070

C.B.I. (pl only)

Prime Minister

(1)

Agree to publication ³⁰

of Cash Limits White

Paper on 29 July?

Yes
not



PRIME MINISTER

15 July 1982

MUS 16/7

CASH LIMITS IN 1981-82

We are now ready to publish the usual White Paper showing provisional outturn of expenditure against cash limits, for 1981-82.

... A draft is attached, following the strictly factual low-key format of previous White Papers. I propose to publish it on Thursday 29 July, after Question Time.

2. Almost all cash limits were correctly observed in 1981-82. In aggregate there was as usual some underspending. Central Government voted cash limits were underspent in total by about £800 million, equivalent to 1.8%. This was rather more than in 1980-81 when it was 1.1% and compares with underspending on central government blocks of 0.7% in 1979-80, 1.5% in 1978-79 and 2.6% in both 1977-78 and 1976-77.

3. There were two cases in which cash limits were breached, though one was rather unusual (see paragraph 5 of page 1 of the draft). This is a better performance than in 1980-81, when there were six. It is lower than in any year since the first two years cash limits were widely used; in 1976-77 and 1977-78. In part at least, it reflects the importance which, as a Government, we attach to cash limits.

4. I would like to take the opportunity of this minute to remind colleagues in charge of spending departments of our collective commitment to cash limits and of the importance of adhering strictly to the cash limits set for this year, and those which we shall shortly agree for next.

5. I am sending copies of this minute and of the White Paper to other members of the Cabinet, to the Chief Whip and to Sir Robert Armstrong.

L.B.

LEON BRITTON



CASH LIMITS 1981-82 PROVISIONAL OUTTURN

(AND 1980-81 OUTTURN)

*Presented to Parliament by the Chief Secretary to the Treasury
by Command of Her Majesty
July 1982*

LONDON
HER MAJESTY'S STATIONERY OFFICE
£ . net

Cmnd.

CASH LIMITS

1981-82 PROVISIONAL OUTTURN (AND 1980-81 OUTTURN)

This White Paper gives provisional outturn figures for cash-limited public expenditure in 1981-82, and revised figures for 1980-81.

2. The cash limits for 1981-82 on expenditure by central government departments were published in the Supply Estimates on 10 March 1981. Also included amongst the original limits is provision for Class IV, Vote 24 which was voted at the time of the Supplementary Estimates published on 4 December 1981, and provisions for Class IV, Vote 25 and Class VI, Vote 6 which were voted at the time of the Supplementary Estimates published on 18 February 1982. The remaining cash limits, on local authority capital expenditure and for certain other bodies, were published in March 1981 in the White Paper "The Government's Expenditure Plans 1981-82 to 1983-84" (Cmnd. 8175).

3. Table 1 shows changes to the original limits announced subsequently, excluding token increases.

4. Tables 2 and 3 gives provisional outturn figures for 1981-82 compared with the cash limits. These figures may be subject to some adjustment when the final accounts are available. The estimated outturns of the external financing limits on nationalised industries in 1981-82 have already been published in Table 21 of the Financial Statement and Budget Report 1982-83.

5. The cash limit for Class VI, Vote 6 in table 2 is for a token amount of £1,000. The outturn is shown as £612,000. The original amount voted allowed sufficient receipts from the sale of shares in the National Freight Company Limited to be appropriated in aid to cover the expenses of sale and the provisionally estimated amount required to fund deficiencies in the National Freight Company's pension fund. As a condition of sale, the Government undertook on the basis of an actuarial valuation to fund the deficiency within seven days of sale, which took place on 22 February. In the event the final cost of funding the deficiency slightly exceeded the provisional estimate of £48 million. An excess vote will be necessary, but for a token amount since surplus receipts from the sale are available to be appropriated to cover the excess expenditure.

6. Table 4 gives final outturn figures for central government cash blocks in 1980-81. Table 5 shows revised figures for the same year for the capital blocks for local authorities and certain other bodies. These may still be subject to some subsequent revision. Provisional outturn figures for 1980-81 were published in December 1981 in the White Paper "Cash Limits 1980-81: Provisional Outturn" (Cmnd. 8437).

CHANGES TO 1981-82 CASH LIMITS, EXCLUDING TOKEN INCREASES

Table 1

Class and Vote/ Cash block (a)		Department	Size of change £ thousand	Purpose of change
CENTRAL GOVERNMENT VOTES				
I	1,2,4&5	Ministry of Defence and Department of the Environment (Property Services Agency)	+318,863 (b)	Additional provision for the Armed Forces pay award, the priority attached to the Defence programme offset by deduction for overspend in 1980-81. Announced on 2 December 1981.
III	3	Ministry of Agriculture, Fisheries and Food	+3,500	Additional provision for adaptation aid to growers of horticultural protected crops. Announced on 12 June 1981.
III	5	Ministry of Agriculture, Fisheries and Food	+10,855	Additional provision for the fishing vessel temporary support scheme 1981. Announced on 30 April 1981.
IV	5	Department of Energy	+70,000	Additional provision to meet further grants to the National Coal Board. Announced on 16 June 1981.
IV	7	Department of Energy	-4,600	Decrease due to savings identified during a review of nuclear research and development expenditure.
IV	13	Department of Employment	-6,090	Transfer to Class IV, Vote 16. Announced on 20 January 1982.
IV	16	Department of Employment	+92,145	Additional provision to meet an increase in demand for places under the Youth Opportunities Programme and to support longer-term training of young persons. Announced on 9 November 1981.
			+22,590	Additional provision to meet the operating costs of Industrial Training Boards, the winding up costs of the ITBs and the enterprise allowance scheme pilot experiment. Announced on 20 January 1982.
IV	17*	Department of Employment	-3,000	Transfer to Class IV, Vote 16. Announced on 20 January 1982.
IV	18*	Department of Industry	+1,060	Additional provision for the development of the small firms services and for publicising the business opportunities programme. Announced on 19 June 1981.
IX	8	Home Office	+7,384	Additional provision to meet the impact on the prison system of the urban unrest in the summer and residual expenditure on last year's prison emergency, offset by deduction for overspend in 1980-81. Announced on 17 November 1981.
IX	12*	Treasury Solicitor's Department	-156	Transfer to Class IX, Vote 3 (not subject to cash limits). Announced on 4 February 1982.
X	2	Department of Education and Science	-500	Transfer to Class X, Vote 8. Announced on 20 January 1982.
X	4	Department of Education and Science	-750	Transfer to Class X, Vote 8. Announced on 20 January 1982.
X	6	Department of Education and Science	-200	Transfer to Class X, Vote 8. Announced on 20 January 1982.
X	7	Department of Education and Science	-200	Transfer to Class X, Vote 8. Announced on 20 January 1982.
X	8	Department of Education and Science	+1,650	Additional provision to purchase two replacement aircraft. Announced on 20 January 1982.

Class and Vote/ Cash block (a)		Department	Size of change £ thousand	Purpose of change
X	9	Department of Education and Science	-435	Decrease due to savings on international subscription. Announced on 25 June 1981.
X	10	Department of Education and Science	-300	Deduction for overspend in 1980-81. Announced on 25 June 1981.
XI	1	Department of Health and Social Security	+6,000	Additional provision to meet payments delayed from 1980-81 by industrial action at some NHS computer centres. Announced on 9 February 1982.
XIII	9*	National Investment and Loans Office	+298	Additional provision to meet shortfall in receipt from fees, mainly because of an unexpectedly low level of local authority borrowing from the Public Works Loans Board. Announced on 25 November 1981.
XIII	10*	Department for National Savings	+1,221	Additional provision due to lower receipts. Announced on 18 February 1982.
XIII	17*	Land Registry	+1,448	Additional provision to meet a greater pressure of work because of the effect of the provision of the Housing Act 1980. Announced on 13 November 1981.
XV	2	Department of Agriculture and Fisheries for Scotland	+11,689	Additional provision for the fishing vessel temporary support scheme 1981. Announced on 30 April 1981.
XV	4	Scottish Economic Planning Department	+7,580	Additional provision to meet an increase in demand for places under the Youth Opportunities Programme and to support longer-term training of young persons. Announced on 9 November 1981.
XV	11*	Scottish Courts Administration	+200	Additional provision to cover lower receipts than expected from sheriff court fines. Announced on 11 February 1982.
XV	14*	Scottish Home and Health Department	-1,444	Transfers to Class XV, Vote 11 and Class XV, Vote 12 (not subject to cash limits). Announced on 11 February 1982.
XVI	4	Welsh Office	+2,561	Additional provision to meet an increase in demand for places under the Youth Opportunities Programme and to support longer-term training of young persons. Announced on 9 November 1981.
XVI	5	Welsh Office	+172	Additional provision for the fishing vessel temporary support scheme 1981. Announced on 30 April 1981.
XVII	1	Northern Ireland Office	+9,610	Additional provision to meet additional costs on the police budget to deal with the civil disturbances mainly associated with the Maze hunger strike. Announced on 26 November 1981.
XVIII	1	Department of the Environment	+4,096	Additional provision on the Rate Support Grants to meet the cost of the police pay award. Announced on 19 November 1981.

Class and Vote/ Cash block (a)	Department	Size of change £ thousand	Purpose of change
XVIII 2	Welsh Office	+536	Additional provision on the Rate Support Grants to meet the cost of the police pay award. Announced on 19 November 1981.
OTHER NON-VOTED BLOCKS			
NID 1	Northern Ireland Departments	+42,740	Additional provision mainly to finance the new arrangements for Northern Ireland electricity tariffs. Announced on 25 January 1982.
DoE/LA 1	Department of the Environment	-21,126	Deduction for overspend in 1980-81, transfer to Class X, Vote 1 (not subject to cash limits) and transfer from UDC 1. Announced on 19 March 1982.
SO/LA 2	Scottish Office	-38,500	Decrease due to several authorities receiving final capital allocations at a lower level. Announced on 11 February 1982.
DoE/NT 1&2	Department of the Environment	-73,400	The two original cash limits were combined and decreased to take account of special disposals. Announced on 27 November 1981.
UDC 1	Department of the Environment	-11,500	Transfer to DoE/LA1 and decrease to allow additional expenditure by local authorities on urban programme revenue schemes. Announced on 19 March 1982.

Notes

- (a) The votes marked by an asterisk were controlled by the Civil Service Department prior to its reorganisation.
- (b) The four cash-limited defence votes are *managed* by agreement with the Treasury *as a single comprehensive cash limit.*

CASH LIMITS 1981-82: PROVISIONAL OUTTURN

Table 2. Central Government Votes

Class and vote number (a)	Accounting department	Description of expenditure	Cash limit £ thousand	Provisional outturn £ thousand	Overspend(+) or Underspend(-) %	
I	1	Ministry of Defence	Pay etc of the armed forces and civilians, stores, supplies and miscellaneous services	4,987,722	4,995,110	} - (b)
	2	Ministry of Defence	Defence procurement	5,805,702	5,830,559	
	4	Property Services Agency	Defence accommodation services etc	635,000	615,400	
	5	Ministry of Defence	Dockyard services	425,780	413,135	
II	1*	Foreign and Commonwealth Office	Overseas representation: diplomatic and consular services	206,972	187,000	-9.6
	2	Property Services Agency	Overseas representation: accommodation services	36,123	30,826	-14.7
	3	Foreign and Commonwealth Office	British Broadcasting Corporation: external services	61,898	61,798	-0.2
	4	Foreign and Commonwealth Office	British Council	34,226	34,117	-0.3
	5	Foreign and Commonwealth Office	Foreign and commonwealth services	26,184	25,220	-3.7
	8	Cabinet Office	Secret service	61,000	60,900	-0.2
	10	FCO: Overseas Development Administration	Overseas aid	979,603	925,500 (c)	-5.5
	11*	FCO: Overseas Development Administration	Overseas aid administration	20,800	19,100	-8.2
III	3	Ministry of Agriculture Fisheries and Food	Other agricultural and food services	82,107	77,257	-5.9
	4	Intervention Board for Agricultural Produce	Central administration	15,624	15,332	-1.9
	5	Ministry of Agriculture, Fisheries and Food	Support for the fishing industry	40,568	32,360	-20.2
	6	Forestry Commission	Forestry	59,195	58,700	-0.8

Class and vote number (a)	Accounting department	Description of expenditure	Cash limit £ thousand	Provisional outturn £ thousand	Overspend(+) or Underspend(-) %
7*	Ministry of Agriculture, Fisheries and Food	Departmental administration	144,887	136,371	-5.9
IV 2	Department of Industry	Miscellaneous support services	60,231	38,607	-35.9
4	Department of Trade	Pay, general administrative expenses, export promotion, shipping services, etc	158,731	144,300	-9.1
5	Department of Energy	Industrial support	312,485	307,753	-1.5
6	Department of Industry	Scientific and technological assistance	234,810	196,000	-16.5
7	Department of Energy	Scientific and technical assistance: nuclear energy	221,375	208,436	-5.8
9*	Export Credits Guarantee Department	International trade: export credit services and insurance of investment overseas (central services)	18,835	17,364	-7.8
11*	Registry of Friendly Societies	Pay and general administrative expenses	1,012	1,003	-0.9
12*	Office of Fair Trading	Pay and general administrative expenses	4,457	3,513	-21.2
13	Department of Employment	Labour market services	183,152	176,620	-3.6
15*	Department of Employment	Advisory, Conciliation and Arbitration Service	12,738	11,005	-13.6
16	Department of Employment	Manpower Services Commission	848,812	809,098	-4.7
17*	Department of Employment	Administration	120,475	104,181	-13.5
18*	Department of Industry	Central and miscellaneous services	49,728	45,210	-9.1
19*	Department of Energy	Administrative and miscellaneous service	15,993	13,488	-15.4
20	Department of Employment	Health and Safety Commission	80,816	72,881	-9.8
24	HM Treasury	Cable and Wireless Ltd	1	-	-
25	Department of Energy	Amersham International Ltd	1	-	-
VI 1	Department of Transport	Roads, etc, England	695,396	639,800	-8.0
2	Department of Transport	Transport services	85,611	78,805	-7.9
4	Department of Transport	Central and miscellaneous services	54,376	46,974	-13.6
5*	Department of Transport	Driver and vehicle licensing	73,410	70,308	-4.2
6	Department of Transport	National Freight Company Ltd	1	612	(d)

Class and vote number (a)	Accounting department	Description of expenditure	Cash limit £ thousand	Provisional outturn £ thousand	Overspend(+) or Underspend(-) %
VIII 2	Department of the Environment	Central environmental services, etc	85,037	78,939	-7.2
4	Department of the Environment	Royal palaces, royal parks, historic buildings, ancient monuments, etc	47,398	44,745	-5.6
5*	Department of the Environment	Central administration and environmental research	151,372	135,431	-10.5
7	Department of the Environment	Urban Development Corporations, England	70,255	37,472	-46.7
IX 1*	Lord Chancellor's Department	Administration of justice: England and Wales	54,946	52,953	-3.6
2	Northern Ireland Court Service	Administration of justice: Northern Ireland	7,319	7,219	-1.4
7	Home Office	Services related to crime, treatment of offenders, community and miscellaneous services	40,597	36,300	-10.6
8	Home Office	Prisons: England and Wales	448,121	437,200	-2.4
9	Home Office	General protective services and civil defence: England and Wales	51,650	41,600	-19.5
11*	Home Office	Central and administrative services	118,056	112,000	-5.1
12*	Treasury Solicitor	Pay and general administrative expenses	8,715	8,366	-4.0
13*	Crown Office	Pay and general administrative expenses	8,907	8,600	-3.4
X 2	Department of Education and Science	Universities, etc	1,166,181	1,166,118	-
4	Department of Education and Science	Educational services	103,282	99,119	-4.0
5*	Department of Education and Science	Central administration	31,924	31,474	-1.4
6	Department of Education and Science	Agricultural Research Council	41,934	41,934	-
7	Department of Education and Science	Medical Research Council	101,539	101,524	-

Class and vote number (a)	Accounting department	Description of expenditure	Cash limit £ thousand	Provisional outturn £ thousand	Overspend(+) or Underspend(-) %
8	Department of Education and Science	Natural Environment Research Council	54,291	54,291	-
9	Department of Education and Science	Science and Engineering Research Council	216,755	216,755	-
10	Department of Education and Science	Social Science Research Council	20,656	20,656	-
11	Trustees of British Museum (National History)	British Museum (Natural History)	8,512	8,493	-0.2
12	Department of Education and Science	Other science	4,206	4,196	-0.2
13	Trustees of British Museum	British Museum	11,116	11,116	-
14	Office of Arts and Libraries	Science Museum	6,448	6,397	-0.8
15	Office of Arts and Libraries	Victoria and Albert Museum	8,850	8,768	-0.9
16	Trustees of Imperial War Museum	Imperial War Museum	3,844	3,710	-3.5
17	Trustees of National Gallery	National Gallery	5,697	5,657	-0.7
18	Trustees of National Maritime Museum	National Maritime Museum	3,622	3,622	-
19	Trustees of National Portrait Gallery	National Portrait Gallery	1,606	1,587	-1.2
20	Trustees of Tate Gallery	Tate Gallery	4,708	4,700	-0.2
21	Trustees of Wallace Collection	Wallace Collection	671	667	-0.6
22	Office of Arts and Libraries	Art, Arts Council, etc	95,221	95,201	-
23	Office of Arts and Libraries	Libraries: England	38,948	38,948	-
XI 1	Department of Health and Social Security	Health and personal social services: England	7,624,882	7,608,000	-0.2
XII 4*	Department of Health and Social Security	Administration and miscellaneous services	552,140	493,000	-10.7
XIII 3*	Privy Council Office	Pay and general administrative expenses	668	654	-2.1

Class and vote number (a)	Accounting department	Description of expenditure	Cash limit £ thousand	Provisional outturn £ thousand	Overspend(+) or Underspend(-) %
4*	HM Treasury	Pay and general administrative expenses	21,879	21,100	-3.6
5*	Customs and Excise	Pay and general administrative expenses	260,396	253,608	-2.6
6*	Inland Revenue	Pay and general administrative expenses	587,969	561,261	-4.5
8*	Exchequer and Audit Department	Economic and financial administration	8,382	6,905	-17.6
9*	National Investment and Loans Office	Pay and general administrative expenses	299	242	-19.1
10*	Department for National Savings	Pay and general administrative expenses	80,400	78,843	-1.9
12	Civil Service Department (e)	Central management of the Civil Service	37,194	36,074	-3.0
13	Civil Service Department (e)	Computer and telecommunications	8,914	7,090	-20.5
14	Civil Service Department (e)	Civil service catering service	1	-	-
15*	Public Record Office	Pay and general administrative expenses	3,563	3,497	-1.9
16*	Office of Population Censuses and Surveys	Pay and general administrative expenses	49,626	44,700	-10.0
17*	Land Registry	Pay and general administrative expenses	49,777	48,700	-2.2
18*	Charity Commission	Pay and general administrative expenses	3,319	3,100	-6.6
19*	Ordnance Survey	Pay and general administrative expenditure on mapping services (net)	18,590	16,609	-10.7
20*	Cabinet Office	Pay and general administrative expenses	10,284	9,826	-4.5
21*	Parliamentary Commissioner and Health Service Commissioners	Pay and general administrative expenses	1,222	1,140	-6.7
22*	Public Trustee Office	Pay and general administrative expenses	1	-	-
24	Her Majesty's Stationery Office	Payments to the trading fund	5,954	5,954	-

Class and vote number (a)	Accounting department	Description of expenditure	Cash limit £ thousand	Provisional outturn £ thousand	Overspend(+) or Underspend(-) %
XIV 1	Property Services Agency	Office and general accommodation services	466,786	440,279	-5.7
2*	Property Services Agency	Administration and miscellaneous services	249,908	234,350	-6.2
3	Central Office of Information	Publicity and departmental administration	41,653	39,675	-4.7
6*	Government Actuary's Department	Pay and general administrative expenses	583	534	-8.4
7	Paymaster General's Office	Pay and general administrative expenses	10,048	9,010	-10.3
XV 2	Department of Agriculture and Fisheries for Scotland	Agricultural services and fisheries: Scotland	68,870	63,590	-7.7
3	Scottish Economic Planning Department	Regional and general industrial support: Scotland	117,627	106,543	-9.4
4	Scottish Economic Planning Department	Manpower Services Commission	104,543	92,211	-11.8
6	Scottish Development Department	Roads, transport and environmental services, etc	142,346	125,000	-12.2
11*	Scottish Courts Administration	Administration of justice: Scotland	1,167	1,004	-14.0
14*	Scottish Home and Health Department	Law, order, protective services and health: Scotland	1,189,015	1,174,459	-1.2
15	Scottish Education Department	Education, libraries, arts and social work: Scotland	99,072	96,131	-3.0
17	Trustees of National Library of Scotland	National Library of Scotland	2,710	2,697	-0.5
18	Board of Trustees National Galleries of Scotland	National Galleries of Scotland	2,263	2,223	-1.8
19	Board of Trustees National Museum of Antiquities of Scotland	National Museum of Antiquities of Scotland	728	728	-
21*	Scottish Record Office	Pay and general administrative expenses	875	779	-11.0
22*	Registrar General's Office: Scotland	Pay and general administrative expenses	6,472	5,300	-18.1

Class and vote number (a)	Accounting department	Description of expenditure	Cash limit £ thousand	Provisional outturn £ thousand	Overspend(+) or Underspend(-) %
23*	Department of the Registers of Scotland	Pay and general administrative expenses	1	-	-
24*	Scottish Office	Pay and general administrative expenses	71,983	67,807	-5.8
XVI 1	Welsh Office	Tourism, roads and transport, housing, other environmental services, education, libraries, arts, health and personal social services	621,580	615,700	-0.9
4	Welsh Office	Manpower Services Commission	54,592	48,865	-10.5
5	Welsh Office	Agricultural services, support for fishing industry, industrial development: Wales	81,189	80,839	-0.4
7*	Welsh Office	Other services	23,881	23,467	-1.7
XVII 1	Northern Ireland Office	Law, order and protective services	335,575	334,446	-0.3
2*	Northern Ireland Office	Central and miscellaneous services	7,329	6,000	-18.1
XVIII 1	Department of the Environment	Rate support grants (1981-82) to local revenues: England	9,031,096	9,031,000	-
2	Welsh Office	Rate support grants (1981-82) to local revenues: Wales	745,036	745,036	-
3	Department of the Environment	National parks, supplementary grants (1981-82): England	4,500	4,500	-
4	Welsh Office	National parks, supplementary grants (1981-82): Wales	1,360	1,360	-
5	Scottish Office	Rate support grants (1981-82) to local revenues: Scotland	1,597,100	1,512,300	-5.3
15*	Crown Estate Office	Pay and general administrative expenses	1,174	1,169	-0.4

Class and vote number (a)	Accounting department	Description of expenditure	Cash limit £ thousand	Provisional outturn £ thousand	Overspend(+) or Underspend(-) %
19	Department of Transport	Transport supplementary grants (1981-82): England	416,500	416,500	-
20	Welsh Office	Transport supplementary grants (1981-82): Wales	40,000	40,000	-
TOTAL CASH-LIMITED VOTES			44,741,243	43,954,206	-1.8

Notes

- (a) The votes marked by an asterisk were controlled by the Civil Service Department prior to its reorganisation.
- (b) The four cash-limited defence votes are *managed as a single comprehensive cash limit.* by agreement with the Treasury
- (c) Virtually all the underspending was to accommodate increased expenditure on the non-voted (attributed) part of the aid programme.
- (d) See page 1, paragraph [5]
- (e) The Management and Personnel Office became the Accounting Department for Class XIII, Vote 12 and the Treasury for Class XIII, Votes 13 and 14, to reflect the provisions of the Transfer of Functions (Minister for the Civil Service and Treasury) Order 1981.

CASH LIMITS 1981-82: PROVISIONAL OUTTURN

Table 3. Local authorities' capital expenditure blocks and for certain other bodies

Department	Cash block	Description of expenditure	Cash limit £ million	Provisional outturn £ million	Overspend(+) or Underspend(-) %
Bank of England	BoE 1	Bank of England administration costs in respect of note issue, exchange equalisation account and debt management	76.3	74.9	-1.8
Department of the Environment	DoE/HC1	Capital expenditure in England on housing financed through the Housing Corporation	491.0	491.3	+0.1
Department of the Environment	DoE/LA1	Capital expenditure in England by local authorities on roads and transport, housing, schools, further education and teacher training, personal social services, the urban programme and other environmental services	3,138.8	2,506.0	-20.2
Department of the Environment	DoE/NT1	Capital expenditure in England by new towns on housing, roads and commercial and industrial investment	106.0	103.0	-2.8
Department of the Environment and Welsh Office	RWA 1	External financing requirements of Regional Water Authorities in England and Wales	453.0	280.0	-38.2
Department of the Environment	UDC 1	External financing requirements of Urban Development Corporations	70.7	38.1	-46.1
Home Office	HO/LA1	Capital expenditure by local authorities on police, courts and probation	44.2	30.6	-30.8
Department of Trade	CAA 1	External financing requirements of the Civil Aviation Authority	46.7	13.5	-71.1
SCOTLAND					
Scottish Office	SO/LA1	Capital expenditure in Scotland by local authorities on roads and transport, water and sewerage, general services, urban programme, police and social work, schools, further education and teacher training	416.5	373.0	-10.4
Scottish Office	SO/LA2	Capital expenditure in Scotland on housing by local authorities, new towns, the Scottish Special Housing Association and on schemes financed by the Housing Corporation, and industrial and commercial investment by new towns	458.3	405.1	-11.6
WALES					
Welsh Office	WO/LA1	Capital expenditure in Wales by local authorities, new towns and the Housing Corporation on roads and transport, housing, schools, further education and teacher training, personal social services, and other environmental services, and by the Land Authority for Wales	260.5	226.3	-13.1
NORTHERN IRELAND					
Northern Ireland Departments	NID 1	Services analogous to Great Britain services covered by cash limits	1,742.5	1,716.4	-1.5
TOTAL			<u>7,304.5</u>	<u>6,258.2</u>	<u>-14.3</u>

**CASH LIMITS 1980-81: OUTTURN
CENTRAL GOVERNMENT VOTES**

Table 4

<i>Class and Vote (a)Number</i>	<i>Accounting Department</i>	<i>Description of Expenditure</i>	<i>Cash Limit £ thousand</i>	<i>Outturn £ thousand</i>	<i>Over-spend(+) or Under-spend(-) %</i>	
I 1	Ministry of Defence	Pay etc of the armed forces and civilians, stores, supplies and miscellaneous services	4,581,206	4,502,487	+0.6(c)	
	2	Ministry of Defence	Procurement	4,891,375(b)		5,095,106
	4	Property Services Agency	Defence accommodation services	620,000		572,071
	5	Ministry of Defence	Dockyard Services	399,623		386,786
II 1*	Foreign and Commonwealth Office	Overseas representation: diplomatic and consular services	180,858	163,231	-9.7	
	2	Property Services Agency	Overseas representation: accommodation services	33,611	29,566	-12.0
	3	Foreign and Commonwealth Office	BBC: external services	54,645	54,145	-0.9
	4	Foreign and Commonwealth Office	British Council	31,617	31,497	-0.4
	5	Foreign and Commonwealth Office	Foreign and commonwealth services	23,880	23,552	-1.4
	8	Cabinet Office	Secret Service	53,500	52,966	-1.0
	10	FCO: Overseas Development Administration	Overseas aid	905,218	901,450	-0.4
11*	FCO: Overseas Development Administration	Overseas aid administration	19,873	18,436	-7.2	
III 5	Ministry of Agriculture, Fisheries and Food	Other agricultural and food services	61,407	60,341	-1.7	
	6	Department of Agriculture and Fisheries for Scotland	Other agricultural services and fisheries and herring industry	56,631	54,607	-3.6
	7*	Intervention Board for Agricultural Produce	Central administration	10,885	9,361	-14.0
	8	Ministry of Agriculture, Fisheries and Food	Support for the fishing industry	30,636	29,863	-2.5

<i>Class and Vote (a)Number</i>	<i>Accounting Department</i>	<i>Description of Expenditure</i>	<i>Cash Limit £ thousand</i>	<i>Outturn £ thousand</i>	<i>Over-spend(+) or Under-spend(-) %</i>
9	Forestry Commission	Forestry	42,535	40,706	-4.3
10*	Ministry of Agriculture, Fisheries and Food	Departmental administration	131,313	127,984	-2.5
IV 2	Department of Industry	Miscellaneous support services	39,979	35,071	-12.3
4	Scottish Economic Planning Department	Industry, energy, trade and employment	105,226	105,163	-0.1
5	Welsh Office	Regional and industrial development	73,977	73,688	-0.4
8	Department of Trade	Pay, general administrative expenditure, export promotion etc	117,870	102,132	-13.4
9	Department of Energy	Industrial support, research & development and miscellaneous services	221,762	212,960	-4.0
10	Department of Industry	Scientific and technological assistance	180,754	167,614	-7.3
11	Department of Energy	Scientific and technological assistance: nuclear energy	189,447	188,706	-0.4
13*	Export Credits Guarantee Department	Central services	19,246	16,967	-11.8
15*	Registry of Friendly Societies	Pay and general administrative expenditure	970	932	-3.9
16*	Office of Fair Trading	Pay and general administrative expenditure	4,207	3,381	-19.6
17	Department of Employment	Labour market services	129,902	128,179	-1.3
19*	Department of Employment	Advisory conciliation and arbitration service	13,518	12,210	-9.7
20	Department of Employment	Manpower Services Commission	639,546	634,486	-0.8
21	Welsh Office	Manpower Services Commission	41,156	39,558	-3.9
22	Scottish Economic Planning Department	Manpower Services Commission	74,803	73,552	-1.7
23*	Department of Employment	Administration	85,672	84,328	-1.6

<i>Class and Vote (a)Number</i>	<i>Accounting Department</i>	<i>Description of Expenditure</i>	<i>Cash Limit £ thousand</i>	<i>Outturn £ thousand</i>	<i>Over-spend(+) or Under-spend(-) %</i>
24*	Department of Industry	Central and miscellaneous services	45,894	42,263	-7.9
25*	Department of Energy	Administrative and miscellaneous services	14,632	12,572	-14.1
26	Department of Employment	Health and Safety Commission	70,970	69,899	-1.5
VI 1	Scottish Development Department	Roads and transport services	101,406	100,644	-0.8
2	Welsh Office	Roads and transport services	94,581	94,550	—
3	Department of Transport	Roads, etc England	548,360	543,059	-1.0
4	Department of Transport	Transport services	100,559	96,152	-4.4
7	Department of Trade	Shipping and civil aviation services	67,064	60,916	-9.2
8*	Department of Transport	Central and miscellaneous services	49,601	46,673	-5.9
VIII 4	Department of the Environment	Central environmental services, etc	80,838	74,634	-7.7
6	Department of the Environment	Royal palaces, royal parks, historic buildings, ancient monuments	44,998	41,104	-8.7
7	Scottish Development Department	Royal parks, historic buildings, ancient monuments and central environmental services	9,708	9,466	-2.5
8	Welsh Office	Other environmental and agricultural services and support for fishing industry	5,608	5,394	-3.8
9*	Department of the Environment	Central administration and environmental research	154,059	139,028	-9.8
IX 3*	Lord Chancellor's Department	Administration of justice: England and Wales	44,781	43,190	-3.6
4*	Northern Ireland Court Service	Administration of justice: Northern Ireland	6,124	5,980	-2.4
5*	Scottish Courts Administration	Administration of justice: Scotland	1,147	1,108	-3.4

<i>Class and Vote (a)Number</i>	<i>Accounting Department</i>	<i>Description of Expenditure</i>	<i>Cash Limit £ thousand</i>	<i>Outturn £ thousand</i>	<i>Over-spend(+) or Under-spend(-) %</i>
6	Home Office	Services related to crime, treatment of offenders, community and miscellaneous services	39,913	38,024	-4.7
11*	Scottish Home and Health Department	Law, order and protective services (central support and other services)	48,297	46,567	-3.6
12	Home Office	Prisons: England and Wales	400,721 (b)	401,756	+0.3
13	Home Office	General protective services and civil defence England and Wales	46,498	41,096	-11.6
15*	Home Office	Central and administrative services	107,805	105,097	-2.5
16*	Treasury Solicitor	Pay and general administrative expenditure	8,775	8,156	-7.1
17*	Queen's and Lord Treasurer's Rembrancer	Pay and general administrative expenditure	7,283	7,037	-3.4
X 2	Scottish Education Department	Education, libraries and arts: Scotland	82,152	80,500	-2.0
3	Welsh Office	Education, libraries and arts: Wales	11,832	11,400	-3.7
5	Department of Education and Science	Universities, etc	1,118,455	1,108,460	-0.9
7	Department of Education and Science	Educational services	97,507	93,512	-4.1
10	Office of Arts and Libraries	Libraries: England	35,899	35,899	—
11	Trustees of National Library of Scotland	Libraries: National Library of Scotland	2,520	2,369	-6.0
12*	Department of Education and Science	Central administration	29,579	28,832	-2.5
13*	Office of Arts and Libraries	Administration	580	565	-2.6
14	Department of Education and Science	Agricultural Research Council	37,477	37,477	—
15	Department of Education and Science	Medical Research Council	72,737	72,737	—
16	Department of Education and Science	Natural Environment Research Council	46,730	46,730	—

<i>Class and Vote (a)Number</i>	<i>Accounting Department</i>	<i>Description of Expenditure</i>	<i>Cash Limit £ thousand</i>	<i>Outturn £ thousand</i>	<i>Over-spend(+) or Under-spend(-) %</i>
17	Department of Education and Science	Science Research Council	204,017	201,446	-1.3
18	Department of Education and Science	Social Science Research Council	19,919(b)	20,219	+1.5
19	Trustees of British Museum (Natural History)	British Museum (Natural History)	7,432	7,420	-0.2
20	Department of Education and Science	Other science	3,720	3,718	-0.1
21	Trustees of British Museum	British Museum	10,290	10,141	-1.4
22*	Office of Arts and Libraries	Science Museum	5,987	5,917	-1.2
23*	Office of Arts and Libraries	Victoria and Albert Museum	8,898	8,774	-1.4
24	Trustees of Imperial War Museum	Imperial War Museum	3,277	3,107	-5.2
25	Trustees of National Gallery	National Gallery	5,603	5,545	-1.0
26	Trustees of National Maritime Museum	National Maritime Museum	3,411	3,381	-0.9
27	Trustees of National Portrait Gallery	National Portrait Gallery	1,482	1,474	-0.5
28	Trustees of Tate Gallery	Tate Gallery	4,591	4,558	-0.7
29	Trustees of Wallace Collection	Wallace Collection	676	617	-8.7
30	Board of Trustees of National Galleries of Scotland	National Galleries of Scotland	2,063	2,057	-0.3
31	Board of Trustees of National Museum of Antiquities of Scotland	National Museum of Antiquities of Scotland	665	661	-0.6
32	Office of Arts and Libraries	Arts, Arts Council etc	88,814	88,811	—
XI 1	Department of Health and Social Security	Health and personal social services: England	7,061,035	7,019,783	-0.6
3	Welsh Office	Health and personal social services: Wales	439,407	434,372	-1.1
5	Scottish Home and Health Departments	Health: Scotland	1,032,332	1,020,863	-1.1
7	Scottish Education Department	Social work in Scotland	9,539(b)	9,484	-0.6

<i>Class and vote number(a)</i>	<i>Accounting department</i>	<i>Description of expenditure</i>	<i>Cash limit £ thousand</i>	<i>Provisional outturn £ thousand</i>	<i>Over- spend(+) or Under- spend(-) %</i>
XII 4*	Department of Health and Social Security	Administration and miscellaneous services	419,122	415,465	-0.9
XIII 3*	Privy Council Office	Pay and general administrative expenditure	620	611	-1.5
4	Treasury	Pay and general administrative expenditure	20,145	18,843	-6.5
5*	Customs and Excise	Pay, general administrative and capital expenditure	238,453	232,756	-2.4
6*	Inland Revenue	Pay and general administrative expenditure	551,680	542,551	-1.7
7*	Department of Transport	Driver and vehicle licensing	69,110	64,808	-6.2
9*	Exchequer and Audit Department	Economic and financial administration	7,759	6,704	-13.6
10	National Investment and Loans Office	Pay and general administrative expenditure	1	—	—
11	Department for National Savings	Pay and general administrative expenditure	65,475	64,089	-2.1
13	Civil Service Department	Central management of the civil service	34,390	33,170	-3.5
14*	Civil Service Department	Computers and Telecommunications	6,174	4,534	-26.6
15*	Public Record Office	Pay and general administrative expenditure	2,905(b)	2,945	+1.4
16*	Scottish Record Office	Pay and general administrative expenditure	863	832	-3.6
17*	Office of Population Censuses and Surveys	Pay and general administrative expenditure	22,591	18,826	-17.7
18*	Registrar General's Office Scotland	Pay and general administrative expenditure	3,163	2,949	-6.8
19*	Land Registry	Pay, general administrative expenditure and capital expenditure	43,429	43,420	—
20*	Department of the Registers of Scotland	Pay and general administrative expenditure	1	—	—

<i>Class and Vote (a)Number</i>	<i>Accounting Department</i>	<i>Description of Expenditure</i>	<i>Cash Limit £ thousand</i>	<i>Outturn £ thousand</i>	<i>Over-spend(+) or Under-spend(-) %</i>
21*	Charity Commission	Pay and general administrative expenditure	2,877	2,769	-3.8
22	Ordnance Survey	Pay and general administrative expenditure on mapping services (net)	17,502	15,225	-13.0
23*	Cabinet Office	Pay and general administrative expenditure	7,373	7,039	-4.5
24*	Scottish Office	Other services	68,141	65,552	-3.8
25*	Welsh Office	Other services	22,953	22,816	-0.6
26*	Parliamentary Commissioner and Health Service Commissioners	Pay and general administrative expenditure	1,209	1,021	-15.6
27	Public Trustee	Pay and general administrative expenditure	1	—	—
29	Her Majesty's Stationery Office	Payments to the trading fund	4,837	4,837	—
31	Civil Service Department	Increase in remuneration	1	—	—
XIV 1	Property Services Agency	Office and general accommodation services	416,109	402,326	-3.3
2*	Property Services Agency	Administration and miscellaneous services	224,271	216,937	-3.3
3	Central Office of Information	Publicity and departmental administration	44,434	37,892	-14.7
6*	Government Actuary's Department	Pay and general administrative expenditure	614	526	-14.3
7*	Civil Service Department	Civil service catering services	1,845	1,416	-23.3
8*	Paymaster General's Office	Pay and general administrative expenditure	8,893	8,180	-8.0
XV 1	Northern Ireland Office	Law, order and protective services (Northern Ireland)	300,126	299,696	-0.1
2*	Northern Ireland Office	Central and miscellaneous services (Northern Ireland)	5,395	4,794	-11.1

Class and Vote (a)Number	Accounting Department	Description of Expenditure	Cash Limit £ thousand	Outturn £ thousand	Over-spend(+) or Under-spend(-) %
XVII 1	Department of the Environment	Rate Support Grants to local revenues: England and Wales (1980/81)	9,376,000	9,176,000	-2.1
1a	Department of the Environment	Rate Support Grants (1979/80) to local revenues, England and Wales	215,000	215,000	—
2	Department of the Environment	National parks supplementary grants (1980/81)	5,200	5,200	—
3	Scottish Office	Rate Support Grants (1980/81) to local revenues, Scotland	1,441,900	1,441,000	-0.1
3a	Scottish Office	Rate Support Grants (1979/80) to local revenues, Scotland	19,000	19,000	—
13*	Crown Estate Office	Pay and general administrative expenditure	1,155	1,045	-9.5
17	Department of Transport	Transport supplementary grants: England and Wales	396,000	396,000	—
18	Department of Transport	Transport supplementary grants (1979/80), England and Wales	2,000	2,000	—
TOTAL			40,683,813	40,237,140	-1.1

(a) Central responsibility for expenditure control was exercised by the Treasury or the Civil Service Department depending on the nature of the expenditure concerned. The blocks controlled by the Civil Service Department are indicated by an asterisk.

(b) This figure does not include provision granted in the Spring supplementary Estimates in the expectation that the previously announced cash limit would be overspent.

(c) The four cash-limited Defence Votes are *managed* by agreement with the Treasury *as a single comprehensive cash limit.*

**CASH LIMITS 1980-81: OUTTURN FOR
LOCAL AUTHORITIES' CAPITAL EXPENDITURE BLOCKS
AND FOR CERTAIN OTHER BODIES(a)**

Table 5

<i>Department</i>	<i>Block number</i>	<i>Description of block</i>	<i>Cash Limit £ million</i>	<i>Outturn £ million</i>	<i>Over-spend(+) or Under-spend(-) %</i>
Bank of England	BoE 1	Financial management	69.2	68.0	-1.7
Department of Education and Science	DES/LA 1	Value of building projects started in 1980-81 under the aegis of the Department of Education and Science, local authorities, and other public bodies and the universities, for schools, further education and teacher training and higher education (England) and for universities (Great Britain)	221.2	220.3	-0.4
Department of Employment	DEM/LA 1	Capital expenditure by local authorities on employment services	1.2	0.8	-33.3
Department of the Environment	DoE/LA 1	Borrowing allocations made for capital expenditure within the locally determined sector in England and Wales	115.0	115.0	—
	DoE/LA 2	Gross capital expenditure on housing by local authorities and new towns (other than that included in DoE/LA 1) excluding lending associated with the sale of public sector houses	2360.5	2384.9	+1.0
	DoE/LA 3	Value of housing associations projects approved by the Housing Corporation	368.4	182.0	-50.6
	DoE/LA 4	Capital expenditure by local authorities on reclamation of derelict land, acquisition of land for development and coast protection work	39.9	41.5	+4.0
	DoE/LA 5	Urban Programme: expenditure by local authorities	202.1	199.9	-1.1
	DoE/NT 1	New towns' industrial and commercial investment (net)	36.2	36.2	—

<i>Department</i>	<i>Block number</i>	<i>Description of block</i>	<i>Cash Limit £ million</i>	<i>Outturn £ million</i>	<i>Over-spend(+) or Under-spend(-) %</i>
Department of the Environment and Welsh Office	RWA 1	External financing requirements of the regional water authorities in England and Wales	395.0	353.4	-10.5
Department of Health and Social Security	DHSS/LA 1	Value of capital projects for personal social services approved by the Department of Health and Social Security	58.4	40.3	-31.0
Home Office	HO/LA 1	Capital expenditure on police, courts, probation and civil defence	26.9	26.9	-
Department of Transport	DTp/LA 1	Key sector loan sanctions for capital expenditure on roads and other transport in England and Wales	154.7	153.9	-0.5
SCOTLAND Scottish Office	SO/LA 1	Capital expenditure by local authorities on roads and transport, water and sewerage, general services, urban programme, police and social work, school buildings, further education and teacher training	366.1	342.9	-6.3
	SO/LA 2	Gross capital expenditure on housing by local authorities, new towns, the Scottish Special Housing Association and the Housing Corporation excluding lending associated with the sale of public sector houses; and new industrial and commercial investment by new towns	470.6	469.4	-0.3

<i>Department</i>	<i>Block number</i>	<i>Description of block</i>	<i>Cash Limit £ million</i>	<i>Outturn £ million</i>	<i>Over-spend(+) or Under-spend(-) %</i>
WALES					
Welsh Office	WO/LA 1	Gross capital expenditure (other than that included in DoE/LA 1) by local authorities, new towns and the Housing Corporation on housing; capital receipts from the sale of land and dwellings; capital expenditure by new towns on roads and commercial and industrial investment; net expenditure by the Land Authority for Wales; expenditure by local authorities on coast protection and urban programmes	159.3	153.5	-3.6
	WO/LA 2	Value of building projects started in 1980-81 under the aegis of the Welsh Office and local authorities in Wales for schools, further education and teacher training, and higher education	15.9	15.9	—
	WO/LA 3	Value of capital projects for personal social services approved by the Welsh Office	3.1	0.8	-74.2
NORTHERN IRELAND					
Northern Ireland Departments	NID 1	Services analogous to Great Britain services covered by cash limits	1581.2	1576.1	-0.3
TOTAL			6644.9	6391.7	-4.0

PART

19

ends:-

draft press statement of 15/7/82

PART

20

begins:-

CST to PM rate of 15/7/82

