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Local Government

P.0812

PRIME MINISTER

Rate Support Grant Settlement 1983-84

(E(82)59)

BACKGROUND

The discussion in 1981 of the Public Expenditure Survey, Local Authority Current Expenditure and Rate Support Grant (RSG) was long drawn out. The RSG settlement for 1982-83 was not announced until very late - too late to influence local authority budgets. It was therefore agreed earlier this year between the Chief Secretary, Treasury, the Secretary of State for the Environment, and other Ministers with local government responsibilities that the Government should try to announce in July its intentions for local government finance in the following financial year - in particular, the total of current expenditure which it thought reasonable, and the likely amount of aggregate Exchequer grant (RSG, plus specific grants for certain services, such as the police). The memorandum by the Secretary of State for the Environment (E(82)59) has been produced in accordance with that agreement.

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2. The memorandum by the Secretary of State for the Environment (E(82)59) therefore seeks authority for an early statement to the local authorities covering the total provision for local authority current expenditure, expenditure targets for each authority, the amount of aggregate Exchequer grant before holdback, and a promise of a severe holdback scheme (unspecified) for overspending local authorities.

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3. In a minute to you of 16 July the Secretary of State for Wales seeks broad agreement for the approach to Welsh local authorities, subject to discussion of detailed points with the Chief Secretary. In a letter of 19 July to the Chief Secretary, the Secretary of State for Scotland says that he is not yet ready to circulate proposals for Scotland but makes two general points - that Scottish authorities should be set a similar reduction from current levels of expenditure to that proposed for authorities in England and that a decision should be delayed on the amount of aggregate grant not just in Scotland but in England and Wales as well.

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Description of the existing system

4. The RSG system in England is exceedingly complicated. Essentially, it is based on:

- a. an assessment of each local authority's need to spend on current account; and
- b. an attempt to equalise resources between local authorities.

Need to spend is measured by the so-called grant related expenditure assessments (GRES). RSG is then paid in support of local authority expenditure in a way which compensates for disparities in rateable resources so that, broadly speaking:

- i. authorities spending at the level of their GRE can levy the same rate poundage; and
- ii. authorities spending similar amounts more than their GRE can do so by levying similar additions to their rate poundage.

5. The system is also operated so as to discourage local authorities from increasing their expenditure too far above GRE. This is done by ensuring that, as a local authority's expenditure rises above GRE, the Exchequer contribution is progressively less and the contribution from the rates progressively greater.

6. To help contain public expenditure, a system of expenditure targets and grant holdback has been superimposed on the system described above. Each local authority is given an expenditure target; if it spends more than that target it may suffer a reduction in grant additional to whatever effect may flow from the basic system.

7. There is no reason why the GRE and the expenditure target of an individual local authority should always be identical: in particular, it may be unrealistic to expect an authority spending much more than its GRE immediately to reduce expenditure to match GRE; and targets have been set below GRE, though this has been criticised, and the Government has been forced to concede that local authorities spending above target, but at or below GRE, will not be penalised in 1982-83. In 1982-83 however, the totals of individual GRES, and individual expenditure targets,



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were made identical, and equated, allowing for differences in definition, to the public expenditure provisions. These totals do not have to correspond, unless the Government wants them to, because they are constructed for different purposes, ie:

The total of GREs indicates what the local authorities need to spend.

The total of expenditure targets indicates the level above which the Government will impose grant penalties.

The public expenditure provision is the Government's publicly announced view of what local authorities will actually spend (although they usually spend more).

8. The Government also has to take a view at some stage of the distribution between services of local authority current spending, both to build up the public expenditure figures and to serve as a foundation for the calculation of GREs. (For example, if the Government wants to encourage expenditure on education, and therefore makes more generous provision for it than for some other services, a local authority with high education needs will have a correspondingly high element in its GRE). But the service distribution can, if necessary, be treated as a second-stage process after the relevant totals have been set.

9. The other important element in the system is fixing the grant total. The amount of grant paid to local authorities collectively depends on the size of the Aggregate Exchequer Grant, the cash limited total of RSG and most other grants paid to local authorities. In the past the Aggregate Exchequer Grant has been discussed and presented as a percentage of the relevant local authority expenditure provision in the Government's public expenditure plans - "the RSG percentage". The Secretary of State for the Environment with the support of the Chief Secretary and the other Ministers concerned propose this year to emphasise the cash total of grant, in line with the Government's general emphasis on cash planning. The amount of grant received by any individual local authority, for a given level of expenditure relative to GRE, depends on its rateable resources, with wide variations around the average.

10. The Welsh RSG system is constructed on the same principles as the English,



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though with some differences of detail. Expenditure targets for individual Welsh authorities have been set for 1982-83 although overspending has been less marked in Wales than in England.

11. The Scottish RSG system is different from that in England and Wales in several respects. The Scottish RSG includes separate elements to compensate authorities for low resources and to assist them in meeting expenditure needs (the system which prevailed in England and Wales until 1980). The system does not provide for automatic reductions in Government support for high spenders; but the Secretary of State for Scotland has the power to take strong selective action against individual authorities (as in the case of Lothian).

The Secretary of State for the Environment's proposals

12. This year the Secretary of State for the Environment's proposals start from consideration of the system of expenditure targets. He divides authorities into three groups depending on the relationship between their 1982-83 budget and "effective targets" (the higher of target and GRE):

a. 1982-83 budget no greater than 101 per cent of 1982-83 effective target:
1983-84 target = 104 per cent of 1982-83 budget

b. 1982-83 budget between 101 and 106 per cent of 1982-83 effective target:
1983-84 target = 105 per cent of 1982-83 effective target

c. 1982-83 budget greater than 106 per cent of 1982-83 effective target:
1983-84 target = 105 per cent of effective target subject to:

i. no authority having to reduce expenditure in cash terms by more than 1 per cent year-on year; provided that

ii. no target is more than 20 per cent in cash terms above the lower of their original and revised budgets for 1981-82.

The virtue of this system is that it tries to strike an appropriate balance between realism and discouraging overspending for each local authority. The exemplifications at Annex A show how it would work in practice.



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13. The Secretary of State assumes that in aggregate authorities will spend at the level of their targets. The total of targets for 1983-84 is £20.1 billion; allowing for differences of definition, this translates into public expenditure provision of £19.5 billion, £0.9 billion more than the provision in the White Paper on the Government's Expenditure Plans 1982-83 to 1984-85 (Cmnd 8494).

14. £19.5 billion is 9 per cent more than the expenditure provision for 1982-83. The Secretary of State does not wish to increase the total of GREs by 9 per cent, since to do so would imply that local authorities needed to increase expenditure by that amount. He suggests that total GREs should instead be increased by 5 per cent. This entails a gap of £700 million between total provision and total GREs. The Secretary of State suggests that this should be treated as an unallocated provision for realism.

15. The Secretary of State suggests that Exchequer grant should be set at a level which will permit authorities on average, if they adhere to their targets, to require little or no increase in rates. He recommends aggregate Exchequer grant of £11.8 billion (implying RSG of 53.2 per cent of relevant expenditure, compared with 56.1 per cent in 1982-83). In order to deter authorities from increasing rates and using the extra revenue to increase expenditure, he proposes a 'severe' holdback scheme for 1983-84, but does not offer details.

16. The Secretary of State proposes that an announcement of the Government's decisions should be made later this month, and should be followed up by meetings with the major Conservative local authorities to press for maximum cooperation.

MAIN ISSUES

17. The main issues appear to be as follows:

- i. targets and total provision;
- ii. service distribution and the unallocated margin;
- iii. amount of Exchequer grant;



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- iv. holdback arrangements;
- v. announcement and tactics.

Targets and total provision

18. It is important to realise that, as the Secretary of State conceives his proposals, the target system and the total provision for current expenditure are inextricably linked: a different system of targets would affect authorities differently; and their expenditure would change in consequence. Hence a decision that the target system should be significantly changed would require reconsideration of the proposed expenditure provision.

19. Some of your colleagues may well criticise the proposed system of targets. Because it is related to budgets in 1982-83 it gives higher targets to authorities who are actually spending more now, rather than authorities needing to spend more. It takes the whole RSG system further away from the assessment of needs. On the other hand, high-spending authorities will be required to make substantial reductions - a reduction in cash as well as real terms. It can be argued that to ask for more is simply not realistic. We understand that the Chief Secretary is content that the proposed system of targets is about right.

20. As for the amount itself (£19.5 billion), we understand that it is acceptable to the Chief Secretary. The increase of £0.9 billion over Cmnd 8494 is less than the £1.3 billion which the Secretary of State for the Environment previously indicated as his likely bid, on grounds of realism, for local authority current expenditure in 1983-84. The danger, in fact, may be that it is too low for genuine realism. It is unlikely that the local authorities collectively will spend no more than the sum of individual targets. The chances depend partly on how severe and effective the holdback scheme for 1983-84 turns out to be.

Service distribution and the unallocated margin

21. If Ministers approve both the system of targets and the total for the current expenditure provision, there may then be some discussion of distribution between services. The first point to establish will be whether Ministers agree that the total for GREs should be less than the total current expenditure provision. There

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is a good argument for leaving this unallocated margin for realism which we believe that the Chief Secretary is likely to accept.

22. Some Ministers may then argue that it would be desirable to settle the distribution between services before moving on to announce decisions about the expenditure provision. In practice however it is extremely unlikely that this could be done quickly and something should be said very soon to local authorities to influence their budgets for 1983-84. The right course would therefore be to invite the Chief Secretary to arrange for further discussion of these questions, and the service distribution, with spending Ministers. Some Ministers, notably the Secretary of State for Education and Science, will be reluctant to have decisions taken about the local authority element in his programme in isolation from the programme as a whole. At some stage, in the autumn, the Home Secretary's Group, MISC 21, will probably have to be convened to settle these and other detailed aspects of local authority expenditure.

Amount of Exchequer grant

23. The Secretary of State for the Environment proposes aggregate Exchequer grant of £11.8 billion, on the grounds that if local authorities collectively stick to their expenditure targets they will then need no increase in domestic rates (in fact, according to Annex D to E(82)59, they should be able to reduce them). The implied grant percentage is 53.2 per cent compared with this year's 56.1 per cent. There is however a risk that local authorities will in practice increase rates and use the extra cash to increase expenditure - particularly expenditure on pay. As the Secretary of State recognises, to avoid this will need a severe holdback system. This may prove impossible to get accepted when the time comes. You may therefore wish to explore the possibility of a lower amount of Exchequer grant, which would allow average rate increases in line with, or a little below, inflation if authorities collectively stick to their targets. On the other side of the argument the Secretary of State for Scotland in his letter of 19 July suggests that the proposed level of grant is too low and that the Government will be blamed for putting up rates.

24. Since the decision on the level of grant is a difficult one, some Ministers may doubt the wisdom of announcing a figure for Exchequer grant at this stage. Clearly to

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do so will set a floor below which it will be very difficult indeed to go. On the other hand, it should be a particularly effective way of concentrating the minds of local authorities on the need for economy in 1983-84. You may think it right to endorse the idea of announcing a figure provided that the Committee is satisfied:

- a. that the amount of Exchequer grant is low enough, and the holdback scheme can be made severe enough, to achieve the expenditure targets; and
- b. that it can be made clear to the local authorities that this is not a decision that the Government has any intention of reopening.

25. If, on the otherhand, the Committee decides that no figure should be announced, there is little point in taking a decision on the figure; it would serve no immediate operational purpose, and might well leak.

Holdback arrangements

26. As noted above, the Secretary of State for the Environment is pinning a good deal on being able to install a severe holdback scheme, though he gives no details. You may wish to ask the Secretary of State for a clearer outline of what he has in mind, and whether he is confident that it will command the necessary political support.

27. One specific point on holdback has been left open - whether local authorities who exceed their targets but not their GRE should, as this year, be immune from holdback. Mr Heseltine suggests that one option might be a gradual scale of holdback for such authorities. If Ministers consider that it is not politically possible to impose holdback at all on local authorities in this category, it would be better to face up to this now, since it will mean in effect that expenditure is likely to be about £150 million higher. This might, as Mr Heseltine suggests, argue for a lower grant total.

Scotland and Wales

28. You will not wish at this meeting to deal with Scotland and Wales. The respective Secretaries of State might be invited to have discussions with the Chief Secretary with a view to arrangements which, allowing for the differences in their systems, are broadly consistent with those adopted for England.



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Announcement

29. If the Committee agrees on the substance of the proposals, there is everything to be said for an early announcement. You will not doubt wish to invite the Secretary of State for the Environment to clear a draft with the Committee.

HANDLING

30. You will wish to ask the Secretary of State for the Environment to introduce his memorandum and the Chief Secretary, Treasury to comment. All Ministers with substantial responsibilities for local government services can be expected to comment (Home Secretary, Secretaries of State for Scotland, Wales, Education and Science, Transport, Social Services, Employment); but you will wish to encourage them to concentrate on the general issues, rather than narrow departmental matters. The Lord President and the Chancellor of the Duchy may have more general political points to make.

CONCLUSIONS

31. You will wish the Committee to reach conclusions on the following:

- i. whether expenditure targets for 1983-84 should be as proposed in paragraph 8 of E(82)59;
- ii. whether the public expenditure provision for local authority current expenditure in 1983-84 should be £19.5 billion;
- iii. whether the total of GREs should be £18.8 billion, with the remaining £700 million left unallocated to services;
- iv. whether the total of Aggregate Exchequer Grant should be £11.8 billion before holdback;
- v. whether the proposals at i. to iv. above should be announced as soon as possible;

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vi. whether, in addition, anything should be said about holdback in 1983-84, apart from the promise that it will be severe;

vii. whether the question of distribution between services should be left to be pursued by the Chief Secretary with individual spending Ministers;

viii. whether the Chief Secretary should be invited to discuss with the respective Secretaries of State arrangements for Scotland and Wales broadly consistent (allowing for the usual differences) with those adopted for England.

PLG

P L GREGSON

19 July 1982