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PRIME MINISTER

Rate Support Grant Settlement 1986/87
(Minute to you of 24 June from the Lord President of the
Council)

BACKGROUND

1. E(LA) has failed to reach agreement about the future of local authority targets and the public expenditure provision for local authority spending for 1986-87. The Lord President of the Council has minuted you reporting E(LA)'s failure and setting out the issues for decision.

Proposals

2. The Secretary of State for the Environment recommends:

(a) that targets should not be retained for 1986-87; instead, block grant pressures, involving a steepened slope, should control local authority expenditure;

(b) an overspend of £670 million above Public Expenditure White Paper (PEWP) figures for current expenditure by local authorities for 1986-87;

(c) a cash standstill in Aggregate Exchequer Grant (AEG). This is shown as "Package 670 without targets" in the Annexes.

3. The Chief Secretary recommends:

(a) that targets be retained for 1986-87, but with GRE-exemption (Grant Related Expenditure Assessment-exemption), ie no authority would have a target below its GRE;

(b) an overspend of, at the most, £350 million above PEWP for current expenditure by local authorities in 1986-87;

(c) a reduction of £750 million in Aggregate Exchequer Grant.

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This is shown as "Package 360T with targets" in the annexes.

4. The Secretary of State for Education and Science has bid for extra provision for education in 1986-87 of £600 million above PEWP levels; and the Home Secretary has bid for extra provision of £170 million for the police.

5. The rate poundage implications of these packages are spelt out in the coloured annexes to the Lord President's minute. Each annex illustrates a different level of Aggregate Exchequer Grant.

MAIN ISSUES

6. The main issues are:
 - (a) the public expenditure provision for local authorities - really the key issue;

 - (b) whether to abandon targets for 1986-87 or to retain them (with a GRE-exemption);

 - (c) the level of Aggregate Exchequer Grant;

 - (d) rate poundage implications.

Public Expenditure Provision for Local Authorities

7. As long as the Government stands by PEWP, any overspending by local authorities will need to be balanced by cuts in other expenditure programmes. E(LA) recognised this but did not believe that the PEWP figures for local authorities were realistic, based as they were on a 6½ per cent real terms cut.

8. The Chief Secretary is prepared to go up to an overspend of £350 million. Mr Jenkin is recommending an overspend of £670 million (a real terms cut of 3½ per cent). Sir Keith Joseph is looking for an extra £600 million to maintain education expenditure in real terms; and the Home Secretary is bidding for an extra £170 million for police.

9. E(LA) doubted whether a realistic settlement could be



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achieved with an overspend of less than £500 million (a real terms cut of 4.2 per cent). The level of overspend that can be agreed will rest on a political judgement of the wisdom of making compensating cuts in other expenditure programmes against the need to reach a realistic and defensible RSG settlement. The trick is to keep the pressure on while not having a settlement so low that it ceases to be credible.

Targets

10. In this year's settlement, Ministers gave assurances that they would seriously consider whether targets could be abandoned in the 1986-87 settlement. To abolish targets would have political attractions.

11. The Chief Secretary supports the retention of targets but with a GRE-exemption, ie no authority would have a target below GRE. This would meet a major criticism of targets, namely that they can be set below GRE, which is often seen as the Government's own perception of need.

12. The Department of the Environment model forecast expenditure to within $\frac{1}{4}$ per cent (£50 million) of the level of local authorities' budgets for 1985-86. But this model has had no experience of working with a no-targets regime. Mr Jenkin believes that while the predictions for individual authorities under a targetless system may be more uncertain, for expenditure overall the model's predictions should be no more uncertain without targets than with them. He also believes that 1986-87 outturns will be particularly uncertain, because of the abolition of the Greater London Council (GLC) and Metropolitan County Councils (MCCs), and because it is difficult to assess the extent to which authorities benefitting from GRE-exemption will spend up to their targets to avoid being penalised by low targets the following year (the Chief Secretary believes few would; Mr Jenkin observes that two-thirds of the headroom was used up in 1982-83 when the GRE-exemption was last in operation and believes the effect would be at least as great this time).



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13. Mr Jenkin sees many difficulties in devising defensible targets for successor authorities because appropriate information about the interborough distribution of the expenditure of the former authorities is not available. He believes that boroughs will take legal action against the targets they have been allotted and that the Government may face defeat in the Courts. He believes grant disregards would have to be issued to successor authorities to forestall this and that this could shift targets upwards by between £50 million to £100 million. The Chief Secretary does not deny there are difficulties in setting targets for successor authorities, but believes Mr Jenkin is exaggerating the problems. The difficulties were, however, sufficient to persuade E(LA) as a whole, the Chief Secretary apart, that targets should not be retained for 1986-87.

Aggregate Exchequer Grant (AEG)

14. The Chief Secretary favours a cut of £750 million in AEG as part of the Government's policy of reducing the proportion of local authority spending subsidised by the national taxpayer and to make local electors more conscious of the cost of local services. The Secretary of State for the Environment favours a cash standstill in AEG (which would of course still be a reduction in the proportion of local authority spending financed by AEG). The Department of the Environment's computer model suggests that changes in the level of AEG would not have a major influence on the level of local authority spending, but cuts in AEG could lead to marked increases in rates.

Rate Poundage Implications

15. The rate poundage implications for the various packages are set out in the coloured Annexes 2 to 5 attached to the Lord President's minute.

What is an acceptable level of rate poundage increases is very much a matter of political judgement. It will probably be



particularly important to ensure that rate increases are not markedly acute in the outer London boroughs and in successor authorities. If they were, the rise might be attributed to the abolition of the Greater London Council and the wisdom of the Government's abolition policy called into question.

HANDLING

16. You will wish to invite the Lord President of the Council to report on the E(LA) discussions and the Ministerial meetings he has chaired. I suggest that, so far as possible, you should then take the issues one by one: Public Expenditure; targets or not; and Aggregate Exchequer Grant. On each you will wish to invite the Secretary of State for the Environment to put forward his views and the Chief Secretary to respond. The Secretary of State for Education and Science may wish to comment on the public expenditure aspect in particular. The Chancellor of the Exchequer may wish to comment throughout.

CONCLUSIONS

17. You will wish to reach conclusions on:

(a) what should be the level of overall public expenditure for local authorities in 1986-87: £350 million overspend; £670 million or something else.

(b) whether to abandon targets for local authorities for 1986-87, or to retain them with a GRE-exemption; and, if the latter, whether to give a commitment that targets below GRE will not be re-introduced.

(c) what should be the level of Aggregate Exchequer Grant for 1986-87; cash standstill, a reduction of £750 million or something in between.

C J S BREARLEY

wk.
24 June 1985

GRG