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RSG SETTLEMENT: 1985/6

All the proposals under discussion involve significant real term cuts in local authority spending.

Treasury and DoE cannot agree about the exact size of the cuts generated by the various packages, because they are engaged in a technical dispute about different measures of local spending.

Such technical difficulties can, however, be ignored because both the local authorities and the newspapers will focus on what is called 'relevant current' spending. This is the measure that affects the provision for services like education.

The most important figures are these:

	Facts	Chief Sec's Package	DoE Package
1985/6 LA Relevant Current Spending	Est. £22,203m		
1986/7 Public Expd. White Paper Provision	£21,750m		
1986/7 Predicted LA Spending		£22,100m	£22,420m
Difference between Predicted 1986/7 spending and 1985/6 Budgets:			
a. Cash terms		-0.4%	+1.0%
b. Real terms		-4.9%	-3.5%
Predicted Overspend against Public Expd. White Paper Provision		£350m	£670m

As you can see from the table:

- the Chief Secretary's package yields a smaller predicted overspend, but forces local authorities to make a cut in cash terms; whereas

- the DoE package allows a larger predicted overspend, but yields a more moderate real terms cut.

The precise effects of the multitude of sub-variants offered by Lord Whitelaw are unknown and unknowable. For example, it is not clear whether spending would rise more sharply if targets were removed from all authorities (as DoE want) or if they were removed only from those authorities below GRE (as the Treasury would prefer): paragraph 6 of Lord Whitelaw's minute explains the two sides of the arguments clearly - and there is some truth in both of them.

In other words, there is no clever wheeze that can get Ministers off the hook. If you want half-way decent public spending totals, you have to accept politically difficult cuts. All the options on offer will cause major political rows. The problem is to find the least costly package that you can get away with politically.

There are four principles that help to solve this problem:

i. Removing targets though risky, makes it politically easier to achieve bigger cuts; both because this will be a news item in itself, helping to counterbalance the 'destruction of local services' story; and because rate rises in the boroughs and districts affected by GLC/MCC abolition will be lower if targets go by the board.

ii. Cuts in total spending are easier if you keep Aggregate Exchequer Grants high, because reductions in aggregate grant force the rates up dramatically. (The significance of this effect varies with the package chosen and the assumptions made: if you take the worst case, a reduction of £750 million in Aggregate Exchequer Grant could cause average shire district rates to rise by 12.0% instead of 1.2% - with the same predicted local authority spending).

iii. A cut is easier to defend if, in some terms, it is not a cut. For example, a 4.5% real terms cut is much easier to explain than a 4.9% real terms cut, because Ministers can truthfully say that (given the Government's estimates of inflation in 1986/7) it represents a 'standstill in cash terms'.

iv. It is better to have a severe cut with some compensating 'bull' points than an anaemic cut with no compensating good news. Announcing a big cut in overall real terms spending, but with more money for popular items like capital spending and proper restructuring of teachers' pay, will win far more friends than announcing a 'not so harsh' RSG settlement.

Conclusion

Bearing these principles in mind, we recommend that you should seek an arrangement on these lines:

1. A cash standstill in 1985/6 Budgets (a 4.5% real terms cut, leading to a predicted overspend of about £450 million against the Public Expenditure White Paper).

2. A reduction of £100 million in Aggregate Exchequer Grant. This gives the Treasury a small contribution towards tax cuts, but keeps down rate rises in sensitive areas like the Outer London Boroughs. For example, Barnet would have a rate rise of about 7% instead of the c.20% rise which it would have if the grant were reduced by £750 million.

3. Removal of targets (providing the 'good news' item).

4. Agreement that if the teachers accept Keith Joseph's restructuring package, the money (a maximum of £100 million) should be additional to the RSG settlement.

Our informal soundings with Treasury and DoE officials suggest that a package of this sort might win grudging acceptance from both sides.

It might be possible to reduce current spending still further - down to the Treasury's preferred levels - if Ministers agreed to take a more relaxed attitude to capital spending. This would to some extent pre-judge a decision that has yet to be made. But the local authorities would very much like the hint of relaxation, since they think that the Government is unfairly preventing them from spending money which they were previously encouraged to raise.

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