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PRIME MINISTER

Rate Support Grant Settlement 1986/87

Following our discussion with you on 25 June, I am pleased to be able to report that I have now reached agreement with the Ministers primarily concerned on the broad shape of the Rate Support Grant Settlement for 1986/87.

2. You will recall that when we discussed this on 25 June you concluded that there were persuasive arguments for seeking to abandon targets; that there were attractions in an unchanged percentage (48.7 per cent) for Aggregate Exchequer Grant (AEG); and that a cash standstill in local authority current expenditure as between 1985/86 and 1986/87 (an overspend of about £450 million over present provision for 1986/87 in the Public Expenditure White Paper (PEWP)) would be defensible. The Secretary of State for the Environment was asked to arrange for further exemplifications to be made, along the lines of our conclusions, so that I could chair a further meeting to resolve the issues.

3. On 27 June I chaired a meeting of the Chancellor of the Exchequer, the Secretary of State for Education and Science, the Secretary of State for the Environment, the Chief Secretary, and the Minister for Local Government. We achieved agreement on a targetless package involving an overspend of about £500 million on PEWP levels with a cash standstill (which implies a percentage reduction) in AEG.

4. I am particularly pleased that we managed to agree on a targetless settlement. We promised in this year's settlement that we would give serious consideration to the abolition of



targets. They are an unpopular form of rough justice, based as they are on past spending. To retain targets would have involved serious risk of difficulties with the successor authorities to the Greater London Council and the metropolitan county councils, including the possible need for them to levy high rates. There is a risk in abandoning targets of higher expenditure but we decided on balance that this was a lesser risk which we were prepared to run. We should be able to derive considerable credit from this decision to abandon targets.

5. At your meeting you saw the attractions of holding AEG constant in percentage terms (at 48.7 per cent) even though this would require an increase in its cash level. When we discussed this with you, we thought this might require an addition of £235 million to AEG. However, further work showed this to be an underestimate. To hold AEG constant in percentage terms would in fact require an increase of £450 million in AEG. Treasury ministers were strongly opposed to any increase in the cash level of AEG. Increases in the cash level would not simply mean lower rate increases; they would imply rate reductions unless local authorities chose, as they might well do, to increase the level of their spending accordingly. Agreement was reached on a cash standstill for AEG which Patrick Jenkin had proposed earlier, in the packages he had recommended to E(LA).

6. On local authorities' current expenditure, we reached broad agreement on a settlement just above cash standstill - an increase of £500 million in the provision for 1986/87 announced in PEWP. Keith Joseph saw potential difficulties in such a figure on the grounds that it would not accommodate the extra provision of £600 million for 1986/87 above PEWP levels which he feels is necessary to maintain education expenditure in real terms. There is potentially a similar problem with police expenditure. I hope this will prove not to be a real difficulty. We are not dealing with

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actual expenditure by local authorities in 1986/87 but with the signals we should give them as they develop their plans for that year. Nevertheless, I have asked officials in the departments concerned to do further work and report to me quickly to see if there is a problem.

7. Subject to that proviso, however, I believe we now have a Rate Support Grant Settlement for 1986/87 which meets our objectives. We can take considerable political credit for the abolition of targets; the rate poundage increases which it implies - even in respect of successor authorities - that should result should be acceptable; and it gives local authorities clear signals about the continuing need to restrain their expenditure. It will be particularly important for us to emphasise these positive features when the Government makes its announcement about the broad shape of the settlement.

8. I am sending copies of this minute to the Chancellor of the Exchequer, the members of E(LA), the Parliamentary Secretary, Treasury, the Paymaster General, the Minister for Local Government and Sir Robert Armstrong.

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Privy Council Office
1 July 1985