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PRIME MINISTER

Rate Support Grant Settlement 1986-87

1. I have seen the Lord President's minute of 1 July on the outcome of discussions about the broad shape of the Rate Support Grant Settlement for 1986-87. Your Private Secretary's letter of 2 July records your agreement with the outcome but makes no reference to the proviso in the Lord President's minute that an increase of £500m in the provision for 1986-87 raises serious difficulties for education. Although as the Lord President points out we are here concerned with the public expenditure signals which we should give to local authorities as they prepare their budgets next year, we shall also be giving them signals about the policies that we expect them to adopt for education.

2. I have naturally looked to see whether I can reduce my request for an extra £600m for education in 1986-87. This figure already involves a real-term cut of 2.5% and not, as the Lord President suggests, the maintenance of present spending levels. I can go some way to help. I attach a note by my officials which describes ways of reducing the requirement to £390m. These figures, of course, involve a sharp reduction in the areas identified by the Audit Commission as ripe for efficiency savings. £140m of the difference is however accounted for by the unavoidable overspend on school meals which for the purposes of our plans I would choose simply to ignore on the grounds that our provision for school meals is based on the most efficient practice and we believe it to be right. I shall campaign to try to secure all these savings and to persuade LEAs to make economies in school meals - although those who have most scope for savings are politically those least likely to be persuaded. But £390m is as low as I could possibly go. It involves presenting our plans for education in terms of a real-term reduction in expenditure of 4.5% from 1985-86 budgets.

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3. Even though in the event local authorities will not make savings of this magnitude, presenting our plans on the basis even of my reduced bid for an extra £390m will still sharply increase the pressures on education for savings - which lie behind so much Government unpopularity. If I am obliged to reduce further, I could not avoid having to tell local authorities to make cuts in those areas of education provision essential to making progress with our Better Schools policies and on which the seriousness of our intentions about standards will be judged.

4. There will be legitimate calls by other local government services - notably the police - on the total of £500m extra available. A pro rata share of it for education would contribute around £250m to the £390m I require, leaving £140m still to find. Given the general wish of colleagues not to add more than £500m explicitly to provision, it seems to me that we should instead acknowledge that there will be expenditure by local government in excess of the plans and earmark a part of the Reserve to meet it. It is already clear - as we explicitly recognized at the Lord President's meeting on 27 June - that the 1986-87 outturn will produce an overspend on local authority current expenditure and that will be a charge on the Reserve. When we consider the size of the Reserve next week, we should expect to have to take this into account.

5. No doubt it will be argued that earmarking a part of the reserve will set precedents but we are in the business of finding the least damaging presentational device to reconcile our public expenditure signals with our policies for local services. What I have in mind is a new kind of unallocated margin, which is not built into planned provision but is acknowledged to be a prior claim on the Reserve. It need not be as large as the full extent of the overspend that we realistically expect - £140m is necessary for education although you may think that to keep to that figure, which we know will be overspent is unnecessarily masochistic and that £200m would be preferable - but carefully presented it would preserve the credibility

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of our policies without significantly weakening our overall message to local government or adding to public expenditure provision. Without some such device, I should have no option but to admit that we have failed to make the provision necessary for our Better Schools policies.

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

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5/ July 1985

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Annex

Education Expenditure in 1986-87

1. The local authorities' assessment of the cost of their present policies on education and school meals in 1986-87 is £11265m or £660m above Cmnd-9428 plans. This assessment, which takes into account the latest information about financial outturn and demographic changes, is in the view of the Department an overestimate of the requirement. Savings of £60m would be obtained if LEAs were to:

	£m
(1) Maintain the Cmnd 9428 policy of a reduction in the school teacher force of <u>6000</u> a year from <u>1985</u>	25
(2) Achieve a 2% annual reduction in secondary schools education support and administrative staff to reflect falling rolls	10
(3) Tighten AFE student:staff ratios to <u>11.6:1</u> (from 10.4:1 in 1984-85). Implies a reduction of 2000 lecturers between January 1985 and 1987	10
(4) Tighten NAFE student-staff ratios (from 8.5:1 in 1984-85 to 8.9:1 in 1986-87 - a reduction of 2300 in the lecturer force	10
(5) Reduce administration costs	5

2. In addition it would be possible to advocate and defend further policy changes which required LEAs to

(1) Reduce still further school non-teaching costs in response to <u>falling school rolls</u> and rein back on the additional provision LEAs plan for repairs and maintenance	35
(2) Tighten further student:staff ratios in AFE and NAFE to 12:1 and 9:1 respectively - an overall reduction in aggregate of 6000 lecturers in both sectors between 1985 and 1987	15
(3) Reduce non-teaching costs in AFE and NAFE by 1% in real terms from efficiency savings	20

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3. Each of these policy changes represents a direct response to recent Audit Commission recommendations. They constitute in relation to teaching staff very ambitious targets of a kind which LEAs have not previously achieved. It should be noted that:

- (a) the forecasts for 1986-87 already assume savings of £60m on account of falling school rolls. This is based on the evidence that LEAs will continue to make progress in taking surplus places out of use. The continuing fall in secondary pupil numbers and new closure proposals now coming forward cannot contribute to savings in 1986-87.
- (b) the tighter staff-student ratios proposed for the further education sector assume a run-down of lecturer staff equivalent to the whole of natural wastage ie a recruitment freeze. To go further would involve incurring redundancy costs which would sharply offset the savings available in 1986-87
- (c) the reduction in non-teaching costs in both AFE and NAFE recognizes the scope for further efficiency identified by the Audit Commission. (Unit costs in AFE have already fallen by some 20% in the last 5 years).
- (d) The Audit Commission report on further education strongly implies that the resources released through increased efficiency should not be used to the benefit of the taxpayer but should be used to train more young people, particularly the young unemployed. (See paragraph 22 of the report).

4. On school meals and milk it might be possible to take the position, as in previous years that for the purposes of the GRE total we would ignore the anticipated overspend of £140m in 1986-87 and set the total at the figure implied by our policies. The prospects of reducing this overspend are negligible until legislation can be put in place

- (a) to require competitive tendering for the school meals service; and
- (b) to remove local authority discretion to provide free school meals to the children of families above the SB level.

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5. This presentational device has worked in the last 3 years because it has been possible to imply that the difference between the allocated total and actual expenditure is attributed within the unallocated margin for which our plans have provided. Without an unallocated margin, it would be necessary to stick to the line that the Government's plans were based on most efficient practice and were right in principle.

6. Taken together the measures proposed in paragraphs 2-6 reduce the original requirement of £660m (decreased to an estimated £600m by the savings outlined in paragraph 1) to £390m.

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