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CCBG

CONFIDENTIAL

The Rt Hon John MacGregor OBE MP  
Chief Secretary to the Treasury  
Treasury Chambers  
Parliament Street  
LONDON  
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12 February 1986

Dear John,

PUBLIC EXPENDITURE : 1985-86 OUTTURN

Thank you for your letter of 7 February setting out your position following our meeting on 4 February.

You do not mention our discussion of the implications for Scotland of the substantial and continuing capital overspending by English local authorities. I remain wholly unconvinced by the argument that we should disregard the indefensible distortion which it introduces into the normal operation of the arrangements for the Scottish and Welsh blocks and the blatant inequity involved in relation to access to the Reserve. (This inequity is starkly illuminated by the fact that you are already citing difficulties with the 1986-87 Reserve, to which the forecast £300 million overspend by English local authorities must be a major contributing factor at this early stage, as a justification for imposing penalties on my local authority capital programmes next year.) However, in view of my need to resolve the outstanding points involved in our discussion of my calls on the Reserve this year, I am prepared to leave for longer term discussion, in the context of the forthcoming Survey, the need to recognise the genuine level of provision for comparable programmes in determining the Scottish and Welsh blocks.

Turning to the immediate problem of this year, my main priority is to secure your agreement to the use by the SDA and HIDB of their increased capital receipts. Since our meeting this problem has come to the attention of the media and brought closer the possibility of the serious political damage which both George Younger and I had predicted. The problem has been linked by the media with several other issues which in themselves require careful political handling, including the review of the SDA and the closure of Gartcosh. It is imperative politically that I am able to announce a favourable outcome on the receipts issue as soon as possible. You will be aware that the amount of money involved has diminished significantly, due to changes in the timing of some of the receipts, and it seems to me absurd to risk a major political reverse for the sake of sums which must be marginal to your calculations on the



Reserve. I have to point to the fact that political considerations have in the past been deemed sufficient by colleagues to justify refraining from additional restrictions through the local authority capital expenditure control system in England, which would have enabled the scale of overspending to be curtailed by amounts which dwarf those at issue in relation to my problems with the SDA and HIDB. I hope therefore that you can agree immediately that I should inform the SDA and HIDB that they may spend their increased receipts, which would not add to my claims on the Reserve.

In order to move towards a solution of our other disagreements, I am happy to make an offer to cover the balance of the additional expenditure on assistance to industry, £14.1 million, without prejudice to the outcome of your separate correspondence with Paul Channon. I would propose to meet this primarily from the reduction in the NSHEB's EFL surrendered in December, in response to your request to George Younger for help with your problems on the Reserve which now amounts to £12.3 million. I suggest that the first £1.8 million of the reduction which I have agreed to make in my SO/LA2 cash block should be regarded as contributing the balance. (I have examined all my other Votes and am unable to offer alternative reductions.)

I appreciate that earmarking £1.8 million of the reduction in SO/LA2 for this purpose would, if we cannot agree my right to call on a share of Paul Channon's forecast underspend on RDG, leave less of my increased obligation to pay housing support grant covered by definite offsetting reductions. In the circumstances, I would be prepared to set aside my objection in principle to your proposal that I should be penalised in 1986-87 by loss of end-year flexibility on both the SO/LA2 and SO/LA1 cash blocks. However, I can only do so if you are prepared to go further than you have gone in relation to the possibility of a substantial tax payment by the SSHA next year.

I explained at our meeting that reductions are only available from within SO/LA2 because of the substantial unallocated margin which was kept, in good faith, to cope with the uncertainty about SSHA tax. You suggest, in effect, that I should be able to do the same thing next year. Quite apart from the question whether it would be justifiable that I should be asked to do so, you are mistaken in suggesting that there should be little practical difficulty. Virtually all of the SO/LA2 provision has already been notified to authorities through provisional allocations. Such unallocated margin as there is has to meet my legal commitment to allow authorities to carry forward their underspending from this year. This claim arises to the extent that underspends exceed overspends which attract penalties. In other words the same circumstances which would maximise the net underspending on the cash block this year and thus provide you with the greatest help with the Reserve will give me the greatest problems next year. Having already reaped this benefit yourself, it is surely reasonable that you should give a firm undertaking to help me with the problem of the SSHA's tax liability if it arises.

As I have mentioned above, your approach to Paul Channon's underspending on RDG is central to the overall arithmetic of my difficulties. I continue to believe that it is contrary to earlier understandings that you should seek to deny me access to that underspending on the grounds that Paul's programmes make other calls on the Reserve. However, even if one were to accept your view on that point I find it very difficult to regard as reasonable the terms of your



letter of 7 February to Paul. I had understood your difficulties with the Reserve to be a matter of simple arithmetic. The planning total has been collectively agreed and we all accept that its relationship to outturn is a matter to which some importance is normally attached. On that basis I, and other colleagues, have done our best to meet you in terms of matching pluses and minuses. Your letter to Paul, however, attaches considerable importance to more abstract concepts, such as ring fencing, which you use to argue that some reductions in public expenditure do not count as minuses in the balancing up exercise on which we are all engaged. I am bound to say that I find this approach artificial. At various stages this year my programmes have suffered very real, and politically difficult, reductions and you continue to press me, while at the same time apparently ruling out of account quite substantial reductions in public expenditure on grounds which seem to me to be divorced from those hard realities.

I am copying this letter to the Prime Minister, Nicholas Edwards, Paul Channon, Kenneth Baker, other members of E(A) and Sir Robert Armstrong.

*Yours ever,*  
*Malcolm Rifkind*

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