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2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

5 February 1985

Dear Chief Secretary

It appears likely that Liverpool City Council will be unable to contain the level of capital expenditure in 1985/6 to which it is already committed within the resources available to it under the Local Government, Planning and Land Act 1980.

On 5 December the City Treasurer reported to the Performance Review and Financial Control Sub-Committee of the Council that, assuming allocations at 1984/85 level (and presumably also assuming no change in the prescribed proportions of capital receipts which authorities are allowed to use on top of allocations), there would be a shortfall of resources to cope with existing commitments.

On 16 January he reported again, in the light of the allocations received and of my announcement on 18 December about prescribed proportions. He said that the Sub-Committee had already approved an examination of the way in which schemes within the Council's capital programme could be financed. However, the gap is so huge that it seems unlikely that it can be bridged.

As I forewarned you and other colleagues at the meeting of MISC 109 on 12 December (MISC 109(84) 1st meeting) I am having to consider the use of my powers under section 78 of the 1980 Act. Under that section, if it appears to me that an authority has failed or is likely to fail to keep its capital expenditure for a year within the statutory limits, I may direct that the authority shall not incur expenditure which would take it over those limits or enter into new capital contracts over a certain size without my consent. Such a direction would be fully in line with the strategy of allowing events to take their course. I should be bound to consider the issue of a direction to any authority in similar circumstances. A breach of such of such a direction would be ultra vires. I understand that Patrick Mayhew has indicated that the Law Officers would if necessary be prepared to institute proceedings against an authority in breach.

We must be clear that the consequences of such action could be serious. Your officials are advising that if we issue a decision and Liverpool breach it, the PWLB could no longer lend. This might precipitate the collapse of the authority. Nevertheless, I think it is right to go ahead. But it would be prudent, particularly in view of the guarded language used by the City Treasurer in his more recent report, to write to the authority in advance of such a direction, telling them what I am minded to do and giving them the opportunity to comment.

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On the question of timing, I am advised that the direction cannot take effect before 1 April. We want to act soon enough to register concern at Liverpool's excessive commitments. I would like to send the warning letter on the occasion of my next visit to Liverpool - 7/8 February. It is going to be difficult if I am not able to say something during the visit. I propose to give the authority fourteen days to make representations.

If we issue a direction, it will mean taking a tough line over consents. With the authority seemingly already heavily over-committed, the general policy would have to be against giving consent. However, each application for consent must be considered on its merits and there might well have to be exceptions, for example for bona fide contracts entered into before the council became financially irresponsible and for emergency work. But it is likely to mean that we shall have to turn down schemes which in other circumstances we would be keen for the authority to proceed with. The existence of the direction must not turn to Liverpool's advantage by giving them scope for getting even further over-committed in a way which would not be open to a normally prudent authority living within the law.

I appreciate that there may be obligations upon the council to incur new capital expenditure. My officials and Keith Joseph's have been unable to agree whether a section 78 direction would override such a statutory duty. The legal advice I have is that it would. The only way of overriding such a conflict is by issuing a consent under the direction. However our general policy would once again have to be the avoidance of as many new capital commitments as possible. I hope we can agree that our aim must be to avoid imposing any fresh requirements on Liverpool which absolutely require expenditure in 1985/6 to which they are not already committed.

The position of contractors under the direction will depend on the circumstances. Contracts are not void simply because they contravene a direction, and contractors are not obliged to inquire into whether a direction has been given or complied with. But I would intend to give considerable publicity to any direction, and to the proposed warning letter, and to draw them to the attention of representative contractors' organisations. The theme of the publicity would be that the City Council is likely to spend in excess of its capital limits; action is needed to stop it spending money it is not entitled to spend. Where a company is or should have been aware of the position before entering into a contract, I doubt whether it could sue Liverpool successfully for resiling from such a contract.

// I attach a draft direction and a draft of the warning letter which, if colleagues agree, my officials will send.

I would be grateful for urgent comments.

I am copying this letter to the Prime Minister and members of MISC 109, Patrick Mayhew and Sir Robert Armstrong.

Your sincerely

Patrick Jenkin

for PATRICK JENKIN

Approved by the Secretary of State & signed in his absence

The Hon Peter Rees QC MP

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DRAFT WARNING LETTER

The Chief Executive
Liverpool City Council

The Secretary of State has seen the report by the City Treasurer to the meeting on 5 December 1984 of the Performance Review and Financial Control Sub-Committee, in which the Treasurer stated his view that in 1985/86 the City Council would be unable to support by its prescribed expenditure block allocations, and by the use of available capital receipts, the level of prescribed expenditure arising in that year from commitments into which it has already entered, if those allocations were to be at the same level as in 1984/85.

The Secretary of State has also seen the further report by the City Treasurer to the 16 January 1985 meeting of the Sub-Committee, in which the Treasurer notes the level of allocation thus far received and the proposed prescribed proportions of capital receipts to be applicable for 1985/86 and refers to an examination of the way in which schemes with the City Council's capital programme may be financed.

Having considered these reports, the Secretary of State believes that there may be a case for the issue of a direction under section 78 of the Local Government, Planning and Land Act 1980 to the City Council in respect of prescribed expenditure and the letting of contracts for the year beginning 1 April 1985. Before taking a decision, he wishes to give the City Council the opportunity to comment and in particular to make representations if it so wishes that a direction would be unnecessary because the City Council is able to comply with section 72 of the Act and intends to do so, or that a direction would be otherwise inappropriate.

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I invite you to let me have the views of the City Council
in writing not later than/14 days from date of letter_7

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DRAFT DIRECTION

The Chief Executive
Liverpool City Council

I am instructed to inform your authority that the Secretary of State, having considered the factors outlined in my letter to you of 1985 /_ and your reply of 1985_/, is of the opinion that the authority is likely to fail to fulfil the requirements of section 72 of the Local Governmnet, Planning and Land Act 1980 in respect of the year beginning 1 April 1985.

Accordingly the Secretary of State for the Environment in exercise of the powers conferred on him by section 78 of that Act hereby directs that after 1 April 1985 the Liverpool City Council shall not without his consent:

- (a) make any payment in respect of prescribed expenditure if the amount of that payment, together with the amount of other payments of prescribed expenditure made in the year beginning on 1 April 1985, exceeds in aggregate the amounts which apply for that year under section 72(3)(a), (c) and (d) of that Act as regards that authority;
- (b) enter into any contract for the carrying out of works of new construction, as defined in section 78(3) of that Act, or undertake any such works the cost of which exceeds /_£15,000_/; and
- (c) enter into any contract under which they would incur liability to pay a sum which exceeds, or sum which /_together_/ exceed, /_£15,000_/.