

PRIME MINISTER

BILATERAL WITH THE CHANCELLOR

Your bilateral with the Chancellor tomorrow will be attended also by the Chief Secretary. (The Lord President is away and you will wish to have a further discussion with him present.) The aim is to discuss the handling of the Public Expenditure Survey.

The Chancellor mentioned some of his thinking to you at the last bilateral. The problem is to decide the stage at which Cabinet will learn of the need to increase the planning totals: July or the autumn? The Chancellor's inclination is to choose the autumn. He argues that to announce the increases in July would give the wrong signal to colleagues, and it would be difficult to handle in public - it would be bound to become generally known - without the context which is provided by the new forecast in the Autumn Statement. The Chancellor suggested that Lord Whitelaw should have the new figures to give him something to work to during the Star Chamber discussions. By implication therefore, the Chancellor would not tell the colleagues at the October public expenditure Cabinet. Instead, they would learn of the changes only at the final public expenditure Cabinet a few days before publication of the Autumn Statement itself.

The Treasury I know arrived at this conclusion only after considerable discussion, and there are risks with it. It assumes that Cabinet in July will sign up to the existing totals without demur, as they have done in the past few years. This may be a correct assessment: everyone knows that in the past few years the Treasury has always found money from its back pocket (i.e. a lower Reserve and higher asset sales and one or two fiddles) which in practice have allowed higher "real" spending on programmes without needing to raise the planning totals in the Autumn Statement. They may well assume the Treasury can do it again. Providing the figures can be

suitably obscured in the Chief Secretary's Cabinet paper, they may this year not even know the totals of the bids, so they will have little idea of the true scale of the problem.

The risk is that one or a group of spending Ministers might challenge the proposal to stay with the existing planning totals. Whatever the Chief Secretary's paper says, enough is known for a particularly astute PFO or the Minister himself to work out that this year's problems look particularly difficult. It would be potentially disastrous for spending Ministers successfully to challenge the Treasury's proposals on the planning totals in July. The whole strategy could be called in question. The Treasury tactic is based on bluff. The consequences could be serious if the bluff is called.

There could instead be positive advantages in taking a decision to increase the planning totals and announce them in July. The Government could say that these decisions were being made specifically to allow greater spending on high priority areas such as education and health. This would also avoid the risk of higher planning totals announced in November being seen as a defeat for you and the Treasury in the battle to maintain priority for tax cuts. If higher spending is inevitable, on this argument go quietly and take full credit for the increase.

Nigel (Wicks) and I disagree about the choice. Nigel believes that if there has been an increase in the planning total in July it should be announced as your deliberate act of policy to increase spending on priority areas of health and education. The Government would then seek to take full presentational advantage. He fears that if the announcement was delayed until the autumn, after a serious bruising battles in the Star Chamber, it would be presented as a defeat for you and the Treasury and we would lose the presentational impact of the increase in spending in the two priority areas.

My own preference is on balance for the autumn. An increase in the spending totals is bound to be seen as something of a defeat however it is presented and whenever it occurs. But in the autumn it can be presented in context (aiming to demonstrate that finance still determines expenditure and not the other way around) and all the announcements of changes in individual programmes would help to distract attention. It would also avoid giving a signal to colleagues as early as July.

Nigel and I both agree that it is vital for you to discuss with the Lord President and the Chancellor the risk of a misfire in July if you go for the Treasury's tactics. What would happen if someone challenged the spending totals? Could the challenge be successfully brushed aside?

Two other points:

(i) the Chancellor may report to you (without the others present) about his discussions with the Attorney on the matter he has come to see you about a couple of times before;

(ii) you could raise with him your concern about spending £130 million to switch to payment of oil royalties in cash (papers below).

*Margo
Duty Clerk*

ff. (DAVID NORGROVE)

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