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LOCAL AUTHORITY CAPITAL CONTROL SYSTEM

Lord Whitelaw is coming to see you tomorrow morning about E(LA)'s conclusions on Nicholas Ridley's proposals for a new local authority capital expenditure control system. It has already been agreed to bring leasing within the control system in 1987/88 by secondary legislation though a decision has yet to be announced.

Under the present capital control system local authorities are allowed to spend on capital in any year:

- their allocations plus 10% 'tolerance'

- a proportion (20% for housing, 30% for other services) of the sum of the capital receipts generated in the year and capital receipts from past years not already used to justify spending;

- 'non-prescribed' expenditure eg leasing (although as noted above it has been decided that leasing will not justify additional spending from 1987-88 onwards).

The problems with this system are that:

- spending power from receipts and 'non-prescribed' expenditure is increasing year by year thereby leaving less and less room for allocations. This means regular bad publicity for the Government when it announces a total for allocations lower than the previous year;

- this makes it increasingly difficult to direct spending power where it is needed. Under the present legislation the Secretary of State may not take account of spending power from receipts when distributing allocations. Since in general (although there are exceptions such as Wandsworth) areas that need to spend (particularly on run-down housing stock) are not well endowed with receipts, the Government is also increasingly vulnerable to the charge that it is failing to deal with the problems of the inner cities.

There is a further problem in 1987-88 because the Government has given a commitment that allocations will be at least 80% of the 1985-86 level. This commitment can only be met by an increase in public expenditure which (in return for the leasing change) the Treasury have now conceded. But there is no commitment of this kind for 1988-89 and later years.

Nicholas Ridley has proposed a new system designed to overcome the disadvantages of the present system. It includes a number of changes:

a. All capital expenditure will in future be 'prescribed' (ie controlled). Non-prescribed spending power disappears;

b. The cash from receipts which still justify spending power may already have been used to redeem debt. Those receipts have already in commonsense terms been used. Under the new system they will not justify additional spending. This reduces the total of accumulated receipts by £3 billion.

c. In order to reduce receipts justified spending power further and make it easier to control expenditure receipts will only count from the year after they arise. This reduces receipts available by £2 billion.

d. In order to maintain an incentive to generate receipts and ensure that the total of receipts starts to diminish the proportion of receipts that authorities are allowed to spend will increase, probably to about 40%, and local authorities will be <u>required</u> to use up spending power from receipts <u>before</u> they use their allocations. At present, authorities may not need all the spending power available, many carry forward unused spending power from receipts into later years;

e. in order to distribute allocations to where the need is greatest, the Secretary of State will be able to take account of spending power from receipts. The working assumption is that he will take account of 50% of such spending power. But he need not take account of any of it. It is this provision which will make the main contribution to changing the distribution of resources;

f. as a quid pro quo for loss of other spending power, authorities will be able to add to capital spending power from revenue (including rents). It is hoped that the pressure on current spending (particularly when the community charge is in place) will keep this within bounds but there will be a reserve power to limit such spending. These pressures will not bite on rents and John MacGregor is insisting that the housing benefit cost of the change should be met in full by a reduction in provision for local authority capital.

E(LA) agreed on Tuesday that the new system is desirable in principle. But many of them expressed doubts about the political wisdom of proceeding such a measure in an election year for the following reasons:

- it was not clear that the Bill could be ready in time to <u>guarantee</u> its passage before the summer recess next year;

- some of the key features of the Bill, particularly the reduction in the receipts that could be used to justify additional spending, might not survive passage through Parliament.

- the main effect would be to transfer resources from the Shires (which would be criticised by the Government's supporters) to the Cities (for which the Government would attract no credit).

The meeting concluded that Lord Whitelaw should discuss the position with you. We consider that the balance of advantage is <u>against</u> legislation in an election year. We share the reservations above although we accept the case for a change in the longer term. Provided the leasing change goes ahead the legislation is not needed to control public expenditure in 1988-89 as the 80% commitment no longer applies. The main effect of the new system therefore is to reduce spending power for some authorities and increase it for others. The distribution of gainers and losers is unattractive (based on a DoE estimate), as follows:

	Gainers	Losers
Shire Districts, Counties and Outer London	129	226
Metropolitan Districts and Inner London	29	19

Inner city authorities are partly to blame for both their lack of reciepts and the condition of their stock (compare Lambeth and Wandsworth). In our view the answer is not to increase their spending power since this does not deal with the fundamental problems of poor management and monolithic ownership of rented housing.

A more fruitful approach is likely to be the transfer of run-down estates to private sector housing associations at a price reflecting the cost of ~~to~~ borrowing to finance renovation. Provided there is an appropriate regime of rent control (which in some cases means rents above 'fair' rent levels) this is a practicable way not only of renovating the stock without a call on public funds but also of encouraging efficient management and diversifying tenure.

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