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Treasury Chambers, Parliament Street, SW1P 3AG  
01-270 3000

16 June 1987

The Rt Hon Nicholas Ridley MP  
Secretary of State for the Environment  
Department of the Environment  
2 Marsham Street  
LONDON  
SW1P 3EB

Prime Minister

Agree to write a strong  
support of the Chancellor on the  
need for reform of the present  
Byzantine system of needs  
assessment?

DRW 19/6.

#### LOCAL AUTHORITY NEEDS ASSESSMENT

As part of our work in E(LF) to prepare for the introduction of the "Paying for Local Government" regime, we need to review the present system of needs assessment, "... with a view to making it less complex and more stable" as the Green Paper puts it. I believe that we should aim for a radical simplification. What we want is to achieve a distribution of needs grant under the new regime that is stable and thus broadly predictable from year to year; that is, so far as possible, clearly objective in its determination of relative needs; and that is based on a mechanism which is easily understood.

The 'GRES' which underlie the present system of assessing relative needs fall a long way short of these requirements. They have become largely discredited both in the eyes of the local authority associations and our own supporters in the House and the shires.

The technical problems with present GRES are well known to you and colleagues. But the financial and political repercussions are much worse. The complexity in the system leads to unforeseen and often unwelcome changes in grant distribution; this in turn generates pressure for more grant. E(LA) has found that the impact of annual GRE reassessments makes it difficult to take decisions on public expenditure provision and grant with any confidence about the likely consequences for particular groups of authority. The many, often small, annual revisions to GRES do not in practice help give us the flexibility to achieve acceptable patterns of rate changes across the country. On the contrary, they make the outcome on grant distribution unpredictable, volatile and quite simply inexplicable to anyone but the statisticians. And this complexity



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makes it impossible to defend a particular outcome as fair and logical to aggrieved local authorities and often to our own supporters.

... We must find a way of determining relative needs under the PLG system that will provide a distribution of needs grant between areas of the country which we can defend. In the attached paper I set out some ideas for introducing a simpler and more transparent system for allocating shares of needs grant under the new system. It is based on six objective and intuitively logical indicators. If applied now it would achieve 94 per cent of the current distribution of GRES, with the needs of most authorities being assessed at broadly the same relative levels as they are at present. There would of course be gainers and losers from any such new system; but these could partly be taken care of under the transitional safety net arrangements when the new system is introduced.

We must take the opportunity afforded by the Green Paper reforms to break away from the arcane and complex approaches to needs assessment adopted over the last decade and move to a much simpler and more stable system. I commend the attached paper to you and colleagues as a basis for further more detailed work.

I am copying this letter and paper to the Prime Minister and other members of E(LF).

A handwritten signature in dark ink, appearing to be 'Nigel Lawson'.

NIGEL LAWSON



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## SIMPLER NEEDS ASSESSMENT

The present system for assessing local authorities needs - their grant related expenditure assessment (GRES) - starts with the worthiest of motives, to achieve objectivity and fairness. But the quest for these has become bogged down in complexity. That complexity in turn means the system produces unforeseen and sometimes perverse results. The resulting shifts in grant - often quite large - destroy the link between what the authority spends and what the local taxpayer pays. That is bad for local accountability.

2. The Green Paper, "Paying for Local Government" sets the objective of basing the new lump-sum needs grant on simpler and more stable GRES. This note reports on how that might be achieved.

The present system

3. The starting point of the present system is the Government's decision on how much local authorities need to spend in total and on each of their services and sub-services. Statistical indicators are then applied to determine each local authority's share. Over 70 such indicators are used at present. Some are straightforward, like number of school children. But others are obviously spurious and some are manifest absurdities:

- shopping floor space is used to estimate the need for spending on museums
- there were prolonged arguments recently about whether the need for spending on winter road maintenance would be better measured by the numbers of days of air frost or the number of days of grass frost.

The attached extract from the Rate Support Grant Report for 1987-88 gives some idea of the complexities of the present system.



4. Each year, GREs are re-examined in detail by working groups of officials from central and local government. But the system is so complex that one minor change can have quite unintended consequences. In 1986-87 it was decided to increase the needs assessment for Newcastle's metro: the consequences was a shift of grant into London and higher rate rises in the shires.

#### A new system

5. Treasury officials have been looking to see if there is a viable alternative to this system. Existing GREs range from around £385 per head in Vale of White Horse, Oxfordshire to £887 per head in Islington. Preliminary work here suggests that 94 per cent of the variation can be explained by using just 6 of the present indicators:

- the total number of school children;
- the number of children under 5;
- the population over 65;
- population density;
- the mileage of local authority roads;
- a general social conditions indicator.

For two-thirds of authorities this simple assessment was within 5 per cent of the GRE produced by the 70 complex indicators used at present.

6. Local authorities would inevitably criticise a simpler system as presenting rougher justice. There would be gainers and losers (though the effects are likely to be much less significant than those which will flow from the removal of resource equalisation as rates are abolished). There would be a few significant losses causing vociferous complaints, although the transitional safety net arrangements would phase the effects in over several years.



7. Once fully established, the advantages of a new system could be considerable:

- a simpler system would be much more transparent; unforeseen distributional consequences arising from technical tinkering should be a thing of the past;
- the system should therefore be much more stable.

8. There will inevitably be opposition to these changes, but transparency and stability are vital if we are genuinely to have a grant which reinforces rather than undermines local accountability. In principle local authorities should welcome these objectives. But they have grown addicted to the annual haggle to refine GREs. It might be argued that a system which is no longer based on a separate needs indicator for each individual service will undermine Departmental influence over local authorities. But in reality their influence under the present system is very limited.

9. The Green Paper reforms offer the obvious chance to implement such changes. The Treasury believes that that opportunity should be used to move once and for all to a system of simple and stable needs assessments. The aim should be to set up a simple system and forswear tinkering with it for several years.



EXTRACT FROM THE RATE SUPPORT GRANT  
REPORT (ENGLAND) 1986/87

*C12. Concessionary fares for the elderly and handicapped. Calculated as:*

- (i) the number of persons of pensionable age in the area of the authority (the sum of Indicator A16 and the number of women aged 60-64 years) as at 30 June 1984;

multiplied by:

- (ii) the square root of predicted bus vehicle miles per hectare in the area of the authority as defined below, expressed to four decimal places;

this product expressed to the nearest whole number.

*Predicted bus vehicle miles per hectare.* The sum in the area of the authority of (a) and (b) below:

- (a) The proportion of persons in households without a car or van as estimated by the Secretary of State on the basis of the 1981 Census, multiplied by Indicator A1, multiplied by 97.848;
- (b) Indicator A1 multiplied by -7.998;

divided by Indicator B1; this quotient expressed to six decimal places.





2 MARSHAM STREET  
LONDON SW1P 3EB  
01-212 3434

The Rt Hon Nigel Lawson MP  
Chancellor of the Exchequer  
HM Treasury  
Parliament Street  
SW1P 3AG

My ref:

Your ref:

30 June 1987

*Dear Nigel*

*NBL*

LOCAL AUTHORITY NEEDS ASSESSMENT

*attach*

Thank you for your letter of 16 June on simplified needs assessments, on which the Prime Minister commented in David Norgrove's letter of 22 June.

We are, I believe, all agreed that the present needs assessments are much too complex and unstable, and we must aim for more comprehensible and stable arrangements under the community charge system. At the same time new assessments must command a high degree of acceptability since the community charge actually levied will visibly and crucially depend on them.

Needs assessments are important in the new arrangements both in terms of the distribution of grant and in terms of accountability. The only real test of an authority's spending behaviour will be the comparison of its spending relative to need. I am concerned therefore that your proposal does not produce assessments for individual authorities but only at the chargepayer level. This means that the chargepayer will be unable to sort out from the information he receives the contribution towards his bill of the various levels of authorities through their expenditure decisions. It is vital that the chargepayer should be able to identify clearly those authorities responsible for high charges.

Our initial assessment of your proposal is that it would mean considerably higher community charges in most inner London boroughs than we have looked at so far. This will exacerbate the already severe problems we face on transition.

Nevertheless I am grateful for your work in this area. We too have been developing a number of options for assessing needs in the future and I expect to put forward proposals for joint consideration shortly. I will certainly include your approach within the options.

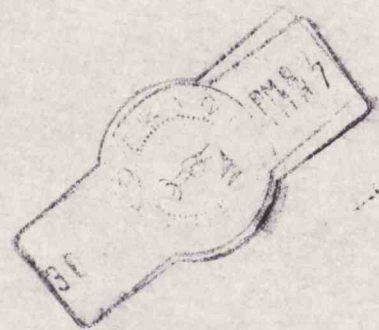
I am copying this letter to the Prime Minister and other members of E(LF).

*Lawson*

*Nicholas Ridley*

NICHOLAS RIDLEY









10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

22 June 1987

Dear Robin,

## LOCAL AUTHORITY NEEDS ASSESSMENT

The Prime Minister has seen the Chancellor's letter to your Secretary of State of 16 June which proposed a radical simplification of the present system of local authority needs assessment. The Prime Minister agrees very strongly with the Chancellor that the present Byzantine system must be drastically simplified. The final recommendations for change must of course include a full set of exemplifications of the effects on rate bills.

I am copying this letter to the Private Secretaries of the members of E(LF) and to Trevor Woolley (Cabinet Office).

Yours,  
David.D R Norgrove

Robin Young, Esq.,  
Department of the Environment.



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PRIME MINISTER

19 June 1987

LOCAL AUTHORITY NEEDS ASSESSMENT

The Chancellor has sent Nicholas Ridley a note advocating a much simpler system of assessing local authority needs than the present GRE system. You are familiar with this system's complexity and absurdity - some 70 indicators such as the square root of bus miles per hectare (expressed to four decimal places).

Although the local authority associations make much of the need for a complicated system in order to produce a "fair" distribution of resources between authorities, I have found no support for this view amongst local authority Treasurers. Some of them say that they regard the system as so capricious as to be little more than a lottery. Others point out that some of the indicators used penalise behaviour that is consistent with Government policies and reward the reverse. All of them say they would trade a simpler system for the present one even if they lost out, provided it was more predictable and more stable. The benefits of being able to plan ahead would quite likely offset any losses.

On the other hand the system is popular with officials in spending departments because an industry has developed in refining the indicators and officials can jostle to get this or that bit of their service slightly more weighting in the overall indicator. So I have found little support for a simpler system amongst officials in the DOE or spending departments.

On the other hand, a simpler, more stable system should help Ministers when determining the annual RSG settlement. At present what happens is that the aggregate sum available is determined several months before the final GRE's are



decided. Any exemplification of the effect of the aggregate decision on individual rate bills can change substantially so that what looks satisfactory initially looks much less so at the end. This leads to the familiar political difficulties with the RSG settlement.

I have  
done  
no

We therefore recommend that you support the Chancellor's suggestion that there should be more detailed work on the basis of the Treasury's paper. You need to give a strong personal steer in favour of a simpler system to counter the inertia in favour of the present one.

The only note of caution is that a full exemplification of the effects of any new system on individual rate bills is needed before final decisions are taken. We need to be sure that the effects are manageable.

#### Conclusion

We strongly support the Chancellor's proposal for more detailed work on a simpler local authority needs assessment. This should include a detailed exemplification of the effect on individual rate bills.

Peter Stredder

PETER STREDDER