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PRIME MINISTER 2

RA

HAMMERSMITH AND FULHAM

You will remember the rumpus earlier in the year over the swap transactions entered into by Hammersmith and Fulham and a number of other local authorities. Since then, the question of possible legal action by the banks has been hanging fire, even though the authorities involved started to default on the transactions some time back. But you may wish to be aware that Hywel Harris Hughes has now learned that legal proceedings may be initiated next week by Deloittes.

Phic.

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PAUL GRAY

25 May 1989

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FA
2 Marsham Street London SW1P 3EB

28 February 1989

RESTRICTED
Department of the Environment
From the Deputy Secretary, Finance and Local Government
F (Derek) A Osborn

Prime Minister ²

Dear Andrew,

*Rec'd
28/2*

HAMMERSMITH AND FULHAM

I enclose a copy of the decision letter which I have issued to Hammersmith and Fulham's request for sanction under Section 19(1) for certain payments. The terms of the letter have been considered and approved by our Ministers, and by the Attorney General though this latter point should not be mentioned publicly.

We have also put out a press statement - copy attached. You will see that this is careful not to go beyond the terms of the decision letter in any material way. We have been advised that there are very strong market and legal sensitivities on these matters, and we must be at pains not to assert publicly any facts which cannot be substantiated from documents that we are at liberty to quote, nor to make any comments that go beyond what could be regarded as fair comment. Detailed questions about the extent of Hammersmith's commitments, liabilities and exposure should be firmly directed towards Hammersmith themselves, who should be pressed to make public the Auditors Public Interest Report as soon as possible and to give their own explanation of the scale of operations they have been conducting.

My Secretary of State proposes to give very brief radio and television interviews today if requested by the news programmes, but not to hold any press conference where he could be subjected to lengthy cross-questioning on matters he is not at liberty to discuss in public. This may however change as more facts come out into the open, or if he is pressed within a day or two to answer questions on the matter in Parliament.

I am copying this letter to Paul Gray at No 10, Ian Plenderleith at the Bank of England and Howard Davies at the Audit Commission.

Yours,
F A OSBORN
Derek

Andrew Edwards Esq
Deputy Secretary
H M Treasury
Parliament Street
London SW1



2 Marsham Street London SW1P 3EB

01-276 3570

Department of the Environment
From the Deputy Secretary, Finance and Local Government
F (Derek) A Osborn

28 February 1989

Dear Sir,

CAPITAL MARKET TRANSACTIONS

I refer to the letters of 24 February and 27 February from the Director of Finance by which he sought the Secretary of State's sanction for certain payments and receipts due to be made or received in the period from 22 February to 6 March in respect of the Council's capital markets activity.

The Secretary of State is advised that the effect of a sanction would be to preclude the Council's Auditor from seeking a declaration under section 19(1) of the Local Government Finance Act 1982 and the court from ordering any of the remedies specified in section 19(2) in respect of an item of account which had been sanctioned. A sanction would not however render lawful the item of account to which it related and neither would it preclude action in respect of any illegality being taken against the Council in proceedings brought by a person other than the Auditor or by the Auditor under powers other than section 19. To sanction a payment or receipt would not in the Secretary of State's view legalise the action of the Council in making it.

In the light of the information which you have made available to him, and having regard to all the circumstances of the case, including the scale, nature and possible consequences of the Council's capital markets activity, the Secretary of State does not consider it appropriate to sanction these payments and receipts.

Yours faithfully,

F A OSBORN

F. A. Osborn

A Eddison Esq
Chief Executive
London Borough of Hammersmith & Fulham
Town Hall
King Street
London W6 9JU

STATEMENT

HAMMERSMITH AND FULHAM: INTEREST RATE SWAPS

Environment Secretary, Nicholas Ridley, today declined to give protection to those responsible in Hammersmith and Fulham Council from action by the auditor, which can lead to surcharge and disqualification, in relation to financial deals which may be found to be illegal.

Mr Ridley said:-

"On Friday, 24 February the London Borough of Hammersmith and Fulham sought sanction from the Department in respect of twelve payments totalling approximately £2.3 million, and on Monday, 27 February they sought sanction in respect of receipts of approximately £650,000, all of which were due in the period 22 February to 6 March. These payments and receipts arise from interest rate swap transactions, and options for such swaps.

"What they seek is protection for those responsible from legal action by the auditor, which can lead to surcharge and disqualification if the courts declare that it is illegal for the Council to make or receive these payments. In the light of the information available to me and having regard to all the circumstances, including the scale, nature and possible consequences, I have decided that it would not be appropriate for me to sanction these payments and receipts.

"I believe that it would be quite wrong, by issuing such a sanction, to prevent the auditor from proceeding under s.19 of the Local Government Finance Act 1982 if he decides to do so. In any event, a sanction could not legalise the action of the Council in making payments if they are illegal and could not therefore prevent any other action which might be brought against the Council."

He added:-

"In view of the possible implications for the ratepayers and the doubts about the legal issues, I consider that it would not be right for me, by sanctioning payments, in effect to pre-empt by administrative action the courts from deciding where the financial consequences of what has happened should lie."

Note to Editors

S. 19 of the Local Government Finance Act 1982 enables a local authority's auditor to go to the courts for a declaration that any item of account (e.g., a payment made by the authority) is contrary to law. If the court gives such a declaration, the court may order

1. that any person responsible for incurring or authorising any expenditure declared unlawful to repay it in whole or part to the body concerned

2. that councillors responsible should be disqualified for a specified period if the expenditure exceeds £2,000
3. rectification of the authority's accounts.

However, by issuing a sanction, the Secretary of State can prevent the auditor from going to the court for these purposes.

Hammersmith and Fulham's auditors yesterday made a 'public interest report' to the Council about this matter. The relevant provision (s. 15(3) of the Local Government Finance Act 1982) enables the auditor to make an immediate report on any matter coming to his notice in the course of the audit in order that it may be considered by the body concerned or brought to the attention of the public.

Even if a sanction were given, others - for example, ratepayers - could still seek judicial review of the Council's actions.



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RA

(Dawson) CC PH

2 MARSHAM STREET
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01-276 3000

My ref:

Your ref:

Paul Gray Esq
Private Secretary to
The Prime Minister
10 Downing Street
LONDON
SW1A 2AA

28 February
March 1989

Dear Paul

HAMMERSMITH AND FULHAM

The Secretary of State is expecting to issue his decision letter refusing sanction to the payments which Hammersmith and Fulham have requested him to sanction this afternoon. This is in line with the preliminary view taken by the Prime Minister's meeting on this subject last week.

I attach a line to take which the Prime Minister may use at Questions this afternoon, should the matter arise. I have been asked to emphasise the cautionary point in the background note. All the issues are highly market sensitive and we have been warned that the Government itself could be in danger of legal challenge if it makes allegations about Hammersmith's financial position and credit worthiness which cannot be substantiated or which go beyond fair comment. It is better to say too little at the moment rather than too much, until the full facts have come out into the open following the auditor's report to Hammersmith Council. This is likely to be later this week.

As I told you on the 'phone, I will confirm that the Secretary of State is happy with the attached line to take as early as possible this afternoon.

Roger Bright

ROGER BRIGHT
Private Secretary

HAMMERSMITH AND FULHAM

Line to Take

1. I understand that the matter is likely to come before the courts very soon.
2. It would not be right for the Government to intervene.
3. In view of the scale and nature of the Council's activities and the doubts about their legality my Rt Hon Friend the Secretary of State for the Environment has decided that it would not be appropriate to sanction any of the payments concerned. It must be for the courts to decide first on the legality of these transactions, and then what the consequences for all those concerned should be.

Background Note

All the issues are highly market sensitive, and are likely to expose the Government itself to legal challenge if the Council's financial position is misrepresented. Therefore great caution in going beyond this line is needed.

28.11.87
9.11.87



COPIED FROM



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2 MARSHAM STREET
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My ref:

Your ref:

Carys Evans
Private Secretary to
The Rt Hon John Major MP
Chief Secretary
HM Treasury
Parliament Street
LONDON
SW1P 3AG

RA

23 February 1989

Dear Carys

AUTHORITY X

So far as we are aware, the position of Authority X in relation to its swaps and options deals has not yet become public knowledge. There was a meeting between the auditors and leading members of the Authority last night however and as more people become aware of the situation the chances of its becoming public knowledge increase. In any case, the auditor may be obliged to make a public interest report in the near future. When it does become public knowledge, we shall be asked our views of the matter. It is desirable that in that event you and other relevant Press Offices should know the line which we shall be taking here. I enclose some briefing which has been prepared with the assistance of Treasury officials. The Supplementaries are of course for use only if necessary.

I am sending a copy of this letter to Paul Gray at No 10.

Roger

R BRIGHT
Private Secretary

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HAMMERSMITH AND FULHAM: INTEREST RATE SWAPS

Line to take

The Government is naturally concerned about the problems of Hammersmith and Fulham now reported by the auditors. It is for the local authority, its auditors and the courts as necessary to resolve the problems.

Supplementary briefing

1. When was the Government informed?

The general extent of the the Council's activities in this market were known last summer when the Audit Commission uncovered it and set about trying to put things right. The Government was made aware formally of the Council's concern about their legal position at the end of last week when the Director of Finance, at the request of the council's auditor, asked to meet DoE officials.

2. Who will bear the costs?

Cannot speculate about where the initial or final costs are likely to fall.

3. Will the Government bail out the counter parties?

The Government has made it clear that it does not stand behind local authorities' debts: banks and other financial institutions which enter into unconventional financing arrangements do so at their own risk.

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9. What about the council's ability to borrow?

This is a specialist market. The ability of this authority and other authorities to borrow depends on their general financial position about which there is no reason for concern.

10. Will the Secretary of State issue a sanction to help the Council?

A general inquiry has been received, but he has not been informed of specific items of account which it is desired he should sanction. But he has said that on the information so far, and in all the circumstances, his preliminary view is that it would not be appropriate for him to issue a sanction.

11. Will the Secretary of State legislate to help the Council?

He has no plans to do so.

Background note

Since early in 1987, Hammersmith and Fulham have undertaken interest rate swaps and options on a very large scale. Considerable net sums are due to be paid out under these arrangements over the next few years - the precise amount will depend upon movements in interest rates. The auditors have now indicated their concern that the programme of swaps undertaken by the authority was in excess of their legal powers, according to legal opinions obtained both by the Council's Director of Finance and earlier by the Audit Commission but not yet tested in the Courts.

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4. Did the authority have Government approval for these transactions?

No. The Audit Commission had in July 1987 warned authorities against entering into swaps and circulated to all local authorities in July 1988 a legal opinion which indicated clear limits on the type and scale of swaps which were acceptable. Moreover, Hammersmith and Fulham did not seek any guidance from central government before undertaking or sustaining the programme of swaps built up over the last 18 months or so.

5. Are other local authorities in the same position?

The Government is aware that a small number of other authorities have undertaken interest rate swaps. But none of these is thought to have exposure on anything like the scale undertaken by Hammersmith and Fulham.

6. Surcharge proceedings?

A matter for the council's auditor.

7. Will legal action be taken?

Also a matter for the auditor. But it is quite possible.

8. Will there be a public inquiry?

The auditor's powers to take proceedings ought to enable those responsible for the situation to be identified, and he also has powers to take action against them if necessary.

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L. C. R. R. 7V36



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10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

21 February, 1989.

SUBJECT CC MASTER

LOCAL AUTHORITY SWAPS AND OPTIONS: HAMMERSMITH AND FULHAM

The Prime Minister discussed this evening with your Secretary of State and the Chief Secretary the paper attached to your letter to me of today's date.

I should be grateful if you and Carys Evans, to whom I am copying this letter, would ensure that it is seen only by named individuals on a strict need to know.

Your Secretary of State explained that the level of the Council's exposure had arisen from active trading in futures. Some 200 agreements had been entered into, which were now falling due at the rate of one or two each week. He understood that this evening the Director of Finance, having been advised by the auditor that an agreement falling due today was illegal, had reneged on a payment. News of this was likely to come out quickly; in any event, members of the Council were being advised of the position tomorrow.

Continuing, your Secretary of State said that future developments depended on the formal action the auditor decided to take. He faced three options:

- (i) To exercise the new "stop power" to prevent the Council from proceeding with payments falling due under the Agreements.
- (ii) To apply for judicial review.
- (iii) To seek a declaration from the courts that the transactions under the Agreements were illegal.

If either of the last two options were adopted, the position would fall to be settled in the courts. But if the auditor decided to use the swap power, the only body who could appeal to the courts for the power to be removed was the local authority itself, and they were most unlikely to do this. In that case the financial institutions and traders who were the counter-party to the agreements would be likely to start actions for damages.

Your Secretary of State said that he had concluded that it would not be appropriate to take the action open to him under Section 19 of the Local Government Finance Act 1982 (Option 2 in the paper). Any action taken under this section would have the effect of prejudging on whom the financial burden should fall. This would be wrong, and it should be left to the auditor and the courts to resolve the legal position.

The Chief Secretary said that careful consideration had been given to the market implications of the Government delaying any action (Option 4 in the paper). The conclusion was that some disruption would result, but this would be bearable in market management terms, and would be unlikely to spread beyond the swaps and options market. Your Secretary of State added that the Council was in a strong financial position, with balances of some £65 million, and so Option 4 would not precipitate a financial crisis for the Council.

In further discussion it was agreed that another advantage of the Government not intervening at this stage was that all concerned in the financial transactions would be obliged to face up to the consequences of their actions.

Summing up the discussion, the Prime Minister said it was agreed that the Government should take no action at this stage. It would be for consideration whether any subsequent action would be appropriate in the light of the position reached in the courts.

I am copying this letter to Carys Evans (Office of the Chief Secretary, HM Treasury).

Paul Gray

Roger Bright, Esq.,
Department of the Environment.



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My ref:

Your ref:

Paul Gray Esq
Private Secretary to
The Prime Minister
10 Downing Street
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21 February 1989

Dear Paul

LOCAL AUTHORITY SWAPS AND OPTIONS: HAMMERSMITH AND FULHAM

As promised, I attach a paper prepared earlier this afternoon on the situation that has arisen in Hammersmith and Fulham, setting out the options for possible Government response.

As I explained to you on the telephone, the situation is developing rapidly and in some respects the position and the options described in the paper have already been overtaken by events. However, my Secretary of State thought it was important to let the Prime Minister have the paper as it stands so she can have some idea of the nature of the problem before she sees him and the Chief Secretary at 9.30 this evening. My Secretary of State will bring her up-to-date at that meeting on the most recent developments, and the options currently thought to be available.

I am copying this to Carys Evans in the Chief Secretary's office.

R Bright

R BRIGHT
Private Secretary

ACTION TO ASSIST LOCAL AUTHORITY X

Memorandum by the Department of the Environment

This paper discusses whether the Government ought to take any immediate action to assist a major local authority ("authority X") which has, either wholly in excess of its legal powers or seriously in excess of them, taken a badly over-extended position in the market for interest rate swaps and options.

Background

2. Over recent years a market has grown up to assist a wide variety of corporate borrowers to manage and minimise their interest rate liabilities by swapping their liabilities between themselves. Typically, a borrower with fixed rate liabilities may swap them with another institution having variable rate liabilities (there is a wide variety of possible arrangements including options to swap). Typically in return for an immediate premium the authority takes the risk of substituting a variable interest rate for its fixed rate. A range of financial institutions (domestic and foreign) are active in this market as traders, taking positions which they, in effect, hedge and reinsure. Since about 1982 up to 30 local authorities have taken positions in this market in what have been regarded as legitimate deals with financial institutions to minimise their interest rate payments on borrowings.

24.7 3. In 1987 and 1988, the Director of Finance of authority X became extremely active in making such deals, to the extent that it entered liabilities in respect of interest on £4,788 million of notional principal. It is thought that this authority accounted for some 80% of local authority activity in the market. The notional principal sum far exceeded its current actual outstanding loan debt, which is about £350m. In the view of the authority's private sector auditors, the authority had not, and does not have, the computer infrastructure and intellectual expertise to operate on this scale in this unusual market.

4. It is unclear how far the Director of Finance has entered these deals with the knowledge and authority of the leader and chairman of the Finance Committee, or whether he has entered them on his own authority. If the latter, it is equally unclear whether the courts would take the view that counter-parties could legitimately have regarded him as acting with the ostensible authority of the Council.

The Legal Position

5. In mid-1988, the Audit Commission became concerned about the involvement of local authorities in this market and sought a legal opinion on their vires, which in turn caused other authorities to seek similar opinions. Three differing views have been expressed:

- (a) that a local authority has no vires at all for interest rate swaps and swap options;
- (b) that a local authority may only enter such transactions by reference to particular loans to the authority; and
- (c) that an authority may only enter such transactions to the extent that the total of liability swapped is no more than the authority's total liability for interest on its external debt.

The point has never been tested in the courts.

Authority X's present situation

6. These opinions alerted authority X and their auditors to the potential financial risks to which the authority was exposed. It was agreed that the liabilities should be reduced in as quick and orderly fashion as possible. In this way (which has required the authority to enter new swap and option agreements to match earlier ones), the principal sum to which outstanding liabilities relate has been reduced to a little over £2,500 million.

7. Meanwhile, however, interest rates have moved against the authority. If they remain, at current levels for any considerable time, the auditors have calculated it is likely to cost the authority some £30 - 100 million over a period of 4 - 5 years to unwind its liabilities. If the authority were obliged to manage the existing liabilities without being able to substitute new ones (see below) and if interest rates remain the same, the losses are estimated at £30 million in the next year.

8. Very recently, the authority's auditors, on the advice of their solicitors, have become concerned about their own legal position. Even in the most favourable of the three positions set out in paragraph 5 above, authority X have acted far in excess of their legal powers; that is so, too, in the case of new action to minimise losses and reduce the liabilities to a level which may be lawful. The auditors consider that they must within a very few days issue an immediate statutory report on the matter as being one which in the public interest ought to be considered by the authority or brought to the attention of the public (S.15(3) of the Local Government Finance Act 1982); and that they must then, by way of judicial review, ask the Court to settle the law on the matter.

The consequences

9. The effect of the report and application will be to make the authority's position public and officers of the authority consider that they will be unable to make any further payments in respect of existing swap and option agreements, and to write any new agreements - because of the possibility that they might be ultra vires and thus might expose the Director of Finance and others involved to the possibility of surcharge and possibly disqualification. (Payments under existing agreements are due within a few days.) There is also the possibility that if the agreements were beyond the authority's powers, or could be regarded as having been entered without the Council's authority, they may be void or voidable. It is therefore to be expected that, the auditors' report and application may quickly be followed by numerous writs from the counter-parties to the agreements. There could be wider effects (see paragraph 13 below).

The options

10. In these circumstances, the officers of authority X and its auditors have consulted the Department of the Environment. The officers' aim is Government action to enable the authority to go on honouring the agreements and to unwind the position in an orderly way, which will inter alia ensure that the counter-parties receive payments when they are due under the agreements and avoid the prospective litigation.

11. In response, there are four options:

- (1) to do nothing and to leave the various legal actions to take their course
- (2) to use existing legislation to sanction payments now under existing agreements (if they are found to be unlawful) so that the authority can go on meeting payments due to counter-parties, and manage the liabilities so as to minimise losses
- (3) to seek immediate legislation to ^{enable} ~~improve~~ authorities to meet obligations arising from existing agreements; this would have to be against the background of a clear policy on local authorities' activities in this market and would probably need to restrict the scope for it
- (4) to do nothing immediately, but when the court has declared whether or not authority X's agreements are unlawful to be prepared to assist, preferably by way of sanction or if necessary by way of legislation, if authority X decides that it is willing for its ratepayers to foot the bill and asks for assistance at that time.

Under options (2), (3) and (4), the cost of unwinding the position would be met by the rate/community charge payers of authority X (though the authority might have an action against their auditor). Under option (1), the incidence of cost between them and the shareholders of the counter-parties would depend on the Court's view of the authority's vires, and, assuming the activities were found to be largely ultra vires, on the outcome of litigation to enforce the agreements or to recover, e.g., damages in negligence. The Chief Secretary and I are agreed that no action should be taken which results in the costs being borne by Central Government.

(1) Doing nothing

12. There are advantages in leaving matters to take their course. Those who have acted beyond the authority's powers would be left to bear the consequences of their action; that would be salutary for both councillors and officers generally. To the extent that the financial institutions had to bear losses there would be a salutary effect generally: we have repeatedly said that the Government will not step in to help financial institutions which participate in creative accounting and other questionable business with local authorities, and we should not be seen to be coming too readily to their assistance unless it is absolutely necessary. There is no reason why the authority's rate/community charge payers should be obliged by the Government, as distinct from the Courts, to bear any of the costs resulting from the actions of the authority's Director of Finance and possibly a handful of members.

13. The disadvantages of doing nothing are chiefly the effects on the market. If the prospect of losses arose from ordinary credit risks, there would be no reason to shelter the arguably institutions. But they have not been imprudent in assessing risk and are not in a position to check the vires of the other party, even in circumstances in which that party can repudiate an agreement entered ultra vires. Extensive litigation would take time to resolve. Meanwhile, there would be the risk of disruption to the swap and swap option market, possibly to related markets, to other borrowing by authority X, and possibly to borrowing by other local authorities and the UK public sector generally. The effects on the authority and its ratepayers are uncertain: on the one hand, they could sustain greater losses because they would be unable to manage the liabilities in the market and because litigation might actually increase what they ultimately have to pay; or on the other hand they could be better off if some of the liabilities are found to be unenforceable.

(2) Section 19 Sanction

14. Section 19 of the Local Government Finance Act 1982, allows the Secretary of State for the Environment to sanction any item of account. The effect is to prevent the auditor from applying to the court for a declaration that an item is

contrary to law and for orders requiring any person responsible for incurring unlawful expenditure to repay it in part or whole, and disqualify any member responsible for the unlawful item if it exceeds £2,000. (Section 20 provides inter alia, and without the possibility of sanction, for similar consequences where a loss has been incurred or a deficiency has been caused by wilful misconduct.)

15. Sanction under S.19 has normally been used to deal with minor errors by members and officers where the unlawful action has been in ignorance or inadvertent. Each case must be considered on its merits, but the Secretary of State's general approach has been to use the power retrospectively only after the item of account has been entered and only where there are exceptional and extenuating circumstances. It would in principle be possible to indicate that, if the courts decided that the existing agreements were illegal, the Secretary of State would be minded to use the power to sanction further payments under authority X's existing agreements. The power could not be used to sanction in advance payments flowing from new ultra vires agreements, so the authority could not minimise its losses by entering new hedging agreements. Such sanctions would be likely to be issued payment by payment.

L persons
16. However the sanction only shelters the authority and responsible *L* from action by the auditor. Aggrieved persons could seek judicial review and under s. 20 of the 1982 Act it would still be possible too for the auditor, , to initiate action in respect of losses incurred as a result of wilful misconduct, or for an aggrieved *L* to bring about the circumstances in which the auditor is obliged to initiate such action.

L person
17. The use of s. 19 sanction in this way and in these circumstances (i.e. when a court had found the agreements unlawful) would be a major change of approach: the Department is under constant pressure to widen its use of this power of sanction and such widening is in general undesirable because it is important that authorities should take care to act only within their powers.

(3) Legislation

18. It would be possible by new legislation, in effect, to give special and prospective cover to the authority which would enable it to honour its obligations under existing ~~the~~ agreements even though there were no powers to enter them and they may be void. The Government's intention to legislate would be announced straightaway, before or at the same time as authority X makes its public interest report, and would be accompanied by a statement of policy making it clear the authorities ought to make use of interest rate swaps and options only in very restricted circumstances. The legislation could include statutory restrictions to that effect in advance of any declaration of the Court as to the existing state of the law.

19. Such legislation (if the authority took advantage of it) would have the effect of guaranteeing that the rate/community charge payers of authority X had to bear the financial consequences of the actions of the Director of Finance and possibly of leading members of the authority (except to the extent that anything was recovered from the auditor). In the next financial year, the implication might be up to 50p extra on the rate (at present 246 p). There could well be local electoral consequences. Moreover, legislation could be shaped so as not to shelter the Director of Finance and others from the consequences of their personal responsibility for the present situation.

(4) Delaying action

20. In the view of the Secretary of State for the Environment special and immediate retrospective legislation as in (3) would be extremely difficult to take through Parliament. It would not be easy to persuade Parliament that the rate/community charge payers should be obliged to bear the full consequences of unauthorised actions by officers and leading members when the Courts, if they had the opportunity, might decide the various matters in ways which would imply a lesser financial burden for the authority's ratepayers - though the financial burden from letting events take their course could alternatively be more expensive eventually for the ratepayers.

21. In the view of the Secretary of State it would be preferable not to take immediate action but to allow the Court to decide upon the lawfulness or otherwise of local authority involvement in interest rate swaps and options and, if authority X were then to renew its request for help to consider helping them at that stage either by way of sanction under s.19 of the 1982 Act or by legislation which would be retrospective in effect, or possibly even by some blend of the two. Authority X can be expected to suspend payments under its existing agreements while the matter of vires is before the Court and there would be some temporary disruption to markets. That would however be salutary for the future dealings of financial institutions and brokers with local authorities. If following the court's decision on the matter of law, the Government helped by way of sanction or legislation, the institutions would be able to receive the sums due to them without the need for lengthy litigation. The choice both as to principle and method could however be left until the Court had reached a decision.

Conclusion

22. The Secretary of State attaches great importance to action to reinforce the frequent statements to the City that the Government cannot be expected to stand behind imprudent or reckless local authorities. He does not favour immediate action by way either of s. 19 or legislation. He is strongly against the latter. His preference is for the fourth option.

L.C. - Relaters' P136

21.11