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PRIME MINISTER

THE COMMUNITY CHARGE

A further discussion on the community charge has been arranged for next Tuesday, after you return from Dublin. The meeting will be attended by the Lord President, the Chief Whip, the Chancellor, the Chief Secretary, Mr. Patten, Mr. Portillo and the Solicitor General.

There will be three papers for consideration:

- the minute from the Solicitor General giving his considered advice on the scope for using existing capping legislation more extensively than previously thought possible; and the practicalities of taking new legislation for an enhanced capping regime;
- a paper from Mr. Patten setting out likely levels of spending and community charges under the Solicitor General's proposed approach using existing powers to cap extensively;
- a report on the negotiations between the Chief Secretary and Mr. Patten on TSS and levels of AEF.

Background

The major development since the last meeting has been the Solicitor General's minute of 19 June. In essence, he has advised that, under existing legislation, the Government can impose cash limits (technically income limits) on virtually all local authorities.

That advice could be undermined by the Appeal Court decision on the existing capping powers early next week. Or the Solicitor General may qualify his advice - there are some references to "in principle" in his minute. But my understanding is he is likely to stand by the approach set out in his minute.

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If the Solicitor General sticks to his advice, then the proposals would enable strict cash limits to be applied to all (except a handful of well-behaved local authorities). Such a regime is potentially tougher than the enhanced capping system Ministers were working on previously - which, of course, required new legislation.

The Solicitor General's approach would work by the Secretary of State for the Environment promulgating a policy on permitted year on year increases in local authority (LA) budgets by category of LA. His specific proposals involve limits for 1991-92 for three categories:

- those LAs spending at or below SSA would face no restriction on the increase allowed in their budgets; however, this covers only a handful of well-behaved, small, largely Conservative-controlled shire districts;
- for those spending between SSA and SSA+5%, an increase only sufficient to cover inflation and any new burdens would be allowed;
- for those spending more than SSA+5%, real cuts would be required - perhaps on a progressive scale according to the degree of overspend.

Such an approach limits LA spending through two mechanisms:

- (a) a deterrent effect: local authorities would know that if they exceeded the limits, they could expect to be capped back to them; in those circumstances many will not exceed them;
- (b) a direct capping effect: if they ignore the limits, then the Secretary of State would be able to cap them.

It follows that the number of authorities to be capped would not be clear till LA budgets were set. Most local authorities seem

likely to respond to the deterrent effect and seek to avoid being capped, provided the limits themselves are set in a reasonable way.

Views of other Ministers

Given advice from the Solicitor General that tough extensive capping powers are available under present legislation, it must be assumed that the "neutrals" on the Ministerial group such as the Lord President, the Chief Whip and the Solicitor General will support the new approach. The key is therefore the stance of Treasury Ministers and DOE Ministers.

My understanding is that Treasury Ministers will support you fully on the need to ensure that extra grant goes into keeping down community charges not adding to local authority spending. Treasury Ministers will not move off the previous proposal for new legislation to introduce an enhanced capping regime, unless and until DOE Ministers sign up in full to the Solicitor General's approach; and Ministers are satisfied that the Solicitor General's approach can be successfully implemented for 1991/92.

Messrs. Patten and Portillo are therefore now in difficulty. They are offered a way out of undertaking new legislation - which they have, of course, been anxious to avoid. But that way does involve using (or strictly threatening to use) very tough capping powers. They may try to resist such potentially extensive use of those powers: they may cite worries about the lack of local accountability; about cuts in local services; and about the resource implications for the Department on undertaking large numbers of caps.

But this does not look to be a sustainable position: no-one has denied at previous meetings that a way needed to be found to ensure that extra grant went to keeping down community charges not adding to local authority spending. Now that the Solicitor General has found such a way Ministers must surely take it up. In practice, DOE will then argue about what constitutes a reasonable year on year increase for different categories of LA.

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Strategy

At this stage you might adopt a twin-track strategy.

If the Solicitor General so qualifies or retracts his earlier advice that his proposed approach no longer looks tenable, then you, in conjunction with Treasury Ministers, must press for new legislation to be introduced next session to create an enhanced capping regime.

If, as is more likely, the Solicitor General remains sufficiently robust, then the objective might be to seek colleagues' approval for a package as follows:

- (x) an increase of fx million in AEF: this would be sufficient to provide for holding down LA expenditure and keeping community charges broadly constant in real terms;
- (y) measures on transitional relief, mixed hereditaments, standard charges, etc., to provide more support for those particularly badly affected by the introduction of the community charge; and critically
- (z) a statement that the Government is determined to ensure this extra grant goes to keeping down community charges not increasing local authority spending; accordingly, the Government would announce in July the criteria (as above) which were likely to be adopted in selecting local authorities for capping next year. (Legally, the Secretary of State must be careful not to fetter his discretion by what is said.)

Mr. Patten must be committed to this approach, before any decision is made on the addition to AEF.

But it is also necessary to consider what happens if there were a successful legal challenge to the extensive use of the capping powers now proposed by the Solicitor General. Such a challenge could arise at any time after the July announcement: but it is

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most likely that local authorities will challenge actual capping decisions next spring.

The Government would have three options if a legal challenge were successful in the courts.

- (i) It could accept that decision. Provided the deterrent effect had worked satisfactorily and relatively few local authorities were being capped, the Government might be prepared not to pursue them further. The other arm of the capping powers (i.e. an excessive level of spending rather than excessive increases) would still be available on the basis used this year. However, I would not recommend this course: in effect the Government's position on holding year on year increases in local authority spending would have been undermined and would not be available in future years.

- (ii) The Government could take legislation to restore the legal position as previously interpreted when the statement had been made in July. An emergency bill could then be introduced - the scope, length and timing of the measures would need to be looked at further. It would be a different prospect for the Government (and backbenchers) to introduce in-year legislation to restore the previously-assumed position, than undertake new legislation to introduce enhanced capping. But timing is a worry - for wider reasons.

- (iii) The Government could take the enhanced capping regime into legislation instead. If experience over the next year had suggested that existing powers had not had a significant deterrent effect, the Government might judge that the enhanced regime - with the important referendum provision to sustain accountability - is to be preferred. Timing is again awkward.

No decision on the precise form or timing of legislation can sensibly be taken yet. But it is vital that Mr. Patten and

Mr. Portillo are signed up now on the willingness to legislate,
if there were a successful challenge to the caps next year.

Conclusion

The aim at next Tuesday's meeting must be to agree on the extensive use of capping powers. If, on further reflection and investigation the Solicitor General's approach proves insufficiently robust, then colleagues should, in logic, be willing to introduce the enhanced capping regime discussed earlier.

If, however, colleagues are satisfied that the Solicitor General's approach is workable in practice, then the meeting might conclude that:

- (i) an announcement on the lines of (x)(y)(z) above should be made at the end of July by Mr. Patten;
- (ii) Mr. Patten must be committed to taking appropriate legislation if there were to be a successful challenge next spring - though the timing of that is clearly affected by other considerations.

The numbers are not yet available on what the Solicitor General's approach might make possible on expenditure and community charges. I will submit further advice on the numbers in time for the meeting on Tuesday.

BHP

BARRY H. POTTER

22 June 1990

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