

*purp*FROM: A J C EDWARDS  
DATE: 28 June 1988

CHIEF SECRETARY

*Ch*  
*Could discuss*  
*last CST in margins*  
*A Prange or NHTS*  
*meeting*cc Chancellor  
Sir P Middleton  
Mr Anson  
Mr Phillips  
Mr Potter  
Mr Fellgett*AA**cc M Tyrie*

RSG, 1989-90 AND LA CAPITAL RECEIPTS

You are due to see Mr Ridley at 11.30 tomorrow morning. The main developments since yesterday's discussion with the Chancellor are:

- (i) Mr Ridley did not accept the Treasury's terms for publication of the consultative paper on the new capital control system (that he should commit himself firmly to taking action to control use of capital receipts in 1989-90, and if possible in the current year as well): the consultative paper is not, therefore, being issued today;
- (ii) we understand that Mr Ridley, while supporting the objective of reaching agreement with you first, is anxious not to delay much longer before taking the RSG close-down issue to the Prime Minister. As he sees it, time is running out;
- (iii) Mr Ridley, or his officials on his behalf, is apparently wary about taking up the Treasury's challenge of saying what grant figures in the 1989-90 RSG settlement he would be prepared to consider under options 1 and 2 for the close-down, respectively;
- (iv) we have reached broad agreement with DOE on the attached paper setting out the pros and cons of options 1 and 2 and the position on capital receipts;

- (v) DOE have consulted outside Counsel, Mr Paul Walker, about possible legal challenges to option 1 close-down legislation, with generally reassuring results. Counsel's preliminary opinion will be available in writing tomorrow evening.

Objectives

2. We suggest that your objectives should be:

- (i) to reach agreement, if possible, on the choice between options 1 and 2, with an understanding at least on the relative amounts of Aggregate Exchequer Grant on offer as between the two options; and
- (ii) to reach agreement on how to proceed with the consultative document on the capital control system.

RSG close-down

NB ||| 3. You are thoroughly familiar with the arguments, both from earlier papers and from yesterday's discussion with the Chancellor. The only point I would like to add is that DOE told us today that their impression was that in many cases local authorities probably did not forfeit grant in order to build up special funds. To that extent the early closedown option would be rather less brutal than we suggested yesterday.

4. The difficult question is the grant figures which might be associated with either option. You will wish to ask Mr Ridley what his proposals would be. Your own position, we suggest, might be as follows:-

- if we are going for option 2, you should stick rigidly by your existing offer of an increase in AEG in line with inflation: that is to say, an increase of

£520 million over last year as set out in option B of the recent E(LA) paper. You would wish to make it clear that you regard this increase as being conditional on (i) taking action as at option C2 of the paper to limit the use of capital receipts for repairs and maintenance for 1989-90; and (ii) full account being taken of the likely use of special funds in the settlement spending assumption for 1989-90. This means an allowance of around £900 million as against the £567 million allowed for in the DOE's existing E(LA) arithmetic;

- if option 1 is preferred, we suggest you should argue that, if a surge in local authority spending is to be avoided, we must have a tough overall grant settlement in order to make up for the much weakened incentive at the margin to keep spending under control. Under option 1 the amount of any extra LA spending at the margin which falls on the domestic ratepayer would fall from 70% at present to as little as 45% before rising to 100% under the Community Charge system. Perhaps for this reason, and also because the authorities would not lose grant through underclaim, Mr Ridley acknowledged at your meeting in the House that with option 1 a tougher grant settlement would be needed. He may now change his line on this. We suggest that you should endorse his earlier line and press for a grant increase of between £520 million and zero, preferably closer to the latter.

5. We estimate that the loss of grant underclaim under option 1 would mean that we would have to pay perhaps £450 million more grant than otherwise (or more or less, depending on the settlement decisions and the actual level of budgets established). But this additional grant should be rather more than offset by the fact that we should no longer be liable to additional claims for grant arising from the manipulation of accounts. The main dangers from manipulation are:

- retrospective capitalisation of repairs in 1987-88 and 1988-89 (up to £350m grant);
- manipulation of special funds in those years (up to £200m);
- and delaying expenditure from March to April 1990 (up to £150m-300m).

In practice not all these dangers should materialise by July 1989. Our best guess is that, for any given level of grant at settlement, the total amount of grant we would have actually to pay out (in respect of all years) would be perhaps £100-200 million less under option 1 than under option 2. The case for a lower settlement under option 1 therefore rests critically on the need to make up for the weakening of restraints at the margin on overall spending.

#### Capital controls consultation paper

6. As noted above, DOE last night rejected the suggestion that they should agree firmly to restrict the use of capital receipts in 1989-90 as a condition for our agreeing that the consultative paper should issue. They continue to maintain that action affecting 1988-89 is not practicable without retrospection, but they admit that action on 1989-90 could have some effect. Paragraph 17 of the paper explains why they think that the problem maybe less acute than we suggest. As the figures in paragraph 18 show, however, the amounts of expenditure at risk are substantial.

7. If you have agreed separately on grant option 2, stopping this loophole will be doubly important. If, as is more likely, you reach agreement on a tough variant on option 1, I think you could soften your position to the extent of insisting on

a presumption in favour of dealing with this problem by one means or another (possibly less Allocations or restricting the use of capital receipts for repairs or maintenance) early next year.

8. In the meantime, we think it important that the consultative paper should now issue as soon as possible. The longer it is delayed, the greater the danger that the legislation for a more effective control system to take effect from April 1990 will slip. We do not think that action to deal with the capital receipts problem in 1989-90 requires any change in the consultative paper text.

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A J C EDWARDS

CHANGES TO THE LOCAL GOVERNMENT FINANCE SYSTEM  
IMPLICATIONS FOR GRANT AND EXPENDITURE

1. The 1989/90 Rate Support Grant (RSG) Settlement is the last under the present system prior to the introduction of the community charge in 1990. The central feature of the present system is that a local authority's grant entitlement varies with its expenditure. For almost all authorities higher expenditure means lower grant. From 1990 onwards, however, grant entitlement will be fixed at the beginning of the year and will not vary with expenditure; strong downward pressure on expenditure will, however, continue to exist since all additional expenditure will fall to be met by community charge payers.

2. The change to the new grant arrangements gives local authorities an opportunity to reduce reported expenditure in the last years of the present system and thereby increase grant entitlements. In 1990 the capital control system will also be revised. This too will provide opportunities to local authorities to manipulate total expenditure to increase grant. Some reductions in expenditure will be genuine and rightly should lead to higher grant receipts. Others will be bookkeeping adjustments - such as use of special funds - that we have accepted over the years should reasonably lead to additional grant. But some adjustments will be more dubious simply taking advantage of this unique opportunity to increase grant.

3. While authorities may be using these opportunities to reduce their "total" expenditure (total expenditure is the term of art for the measure of expenditure on which RSG is paid) and gain grants, they may alternatively increase their real underlying level of expenditure without foregoing grant, or strike some balance between the two. This note considers the risks of higher grant claims or higher expenditure and discusses options for reducing them.

ASSESSMENT OF RISK

(1) GRANT

4. Since 1987/88 the amount of RSG available to local authorities has been "open ended" i.e. dependent only on authorities' own expenditure decisions - the less they spend, the more grant is paid. The expectation, however, has been that the actual payments would be lower than allowed for in the RSG Settlements. In practice local authorities have indeed spent higher than allowed for in the RSG Settlements and have forfeited grant. On present information in 1987/88 authorities overspent by £811m and consequently lost £298m grant, while in 1988/89 authorities have budgeted to spend £1035m more than allowed for in the settlement and have lost £521m grant.

5. In the normal cycle of events we update our information after the year end to take account of first "unaudited" and subsequently "audited" out-turn and revise grant claims accordingly. Final calculations of grant are not made until at least two years after the end of the relevant financial year.

6. The particular grant risk to the Exchequer arises now because of the opportunity for local authorities to use accounting adjustments either to reduce reported total expenditure or to switch reported total expenditure from years in which it would reduce their grant entitlements to years where it has less impact on grant.

7. Throughout the 1980s local authorities have used a number of devices for reducing reported total expenditure in order to maximise grant. Common methods have been through the use of special funds, and by classifying expenditure on repairs and renewals as capital rather than revenue. Many rate capped authorities have indulged in a wider range of creative accounting arrangements.

8. We already know that many local authorities are wondering how best to take advantage of the opportunity presented by the change of system; and we believe that experts in the City are working up schemes to sell to local

authorities. Amongst the arrangements being considered are factoring - which involves "selling" future expected capital receipts - use of special funds, capitalising repair and maintenance, and reducing debt servicing costs.

9. We can anticipate the use of some of these schemes and take account of them in fixing the assumptions for the 1989/90 Settlement. In particular we can allow for use of special funds to reduce expenditure in 1989/90 and partly for further capitalisation of repairs and maintenance. We may also be able to prevent some abuses - such as factoring - using existing powers. But we cannot allow for other unwelcome accounting practices in the 1989/90 Settlement without effectively condoning them and thereby encouraging authorities to indulge them. Nor can we now change the assumptions for 1987/88 or 1988/89 which are the other years at risk of grant manipulation. Moreover it is always possible there may turn out to be other devices available to authorities to manipulate grant which we have not yet identified.

10. We cannot quantify precisely the extent to which Exchequer grant may be at risk. As an outer limit we note that in recent years rate capped authorities have understated true expenditure by around 12%. If all authorities were to understate expenditure to this extent the grant claim would rise by around £1700m in 1989/90. This certainly exaggerates greatly the extent to which grant might be manipulated. But we can expect manipulation even from authorities that would normally avoid such arrangements. In particular we can expect a herd instinct to develop as it becomes clear that many authorities are manipulating the system particularly as these accounting arrangements are all within the law. The risk to the Exchequer is at least £350m in respect of 1987/88 and 1988/89. For 1989/90 an expected grant underclaim of several hundred million pounds could become a grant overclaim. Moreover the proposed changes to the capital control system, which requires at least half of cash-backed capital receipts to be applied to redemption of debt in 1990, may encourage local authorities to make maximum use of capital receipts to reduce revenue expenditure, and hence gain grant, in the years up to 1989/90. Annex A sets out our present assessment of the maximum scope for manipulation by those means we have been able to identify.



(2) EXPENDITURE

11. Another risk is that the period of transition to the new control system will see a surge in overall spending by local authorities. There are three main ways in which this might come about.

12. First, the more grant the authorities succeed in obtaining from the Government, the more possible it will be for them to finance extra expenditure without additional calls on the domestic ratepayer. However, to the extent that authorities raise revenue spending in 1989/90 they will, under present rules, forego grant gains.

13. Second, the action which the Government takes to prevent local authorities from obtaining large extra amounts of grant on the strength of creative accounting could have the effect of reducing the marginal impact of extra spending on domestic ratepayers to a level far below that under the existing control system or the Community Charge system. This would reinforce the temptation which authorities may anyway perceive to spend more during the next 18 months when they will be able for the last time to raise extra sums from non-domestic ratepayers.

14. Third, some authorities may be prompted to undertake extra expenditure as a result of publication of details of the transition to the new capital control system. Although most capital expenditure by local authorities is "prescribed expenditure" and thus subject to control under Part VIII of the Local Government, Planning and Land Act 1980, there is also a considerable amount of "non-prescribed" expenditure. The largest element of such expenditure (about £500m a year) is capitalised repair and maintenance of buildings, roads, and structures. The amount of capitalisation has increased in recent years, largely in response to pressures to maximise grant and keep rates down. The 1980 Act limits the rate at which local authorities may use their capital receipts to finance prescribed expenditure and, at present, there are approximately £6½ billion of cash-backed capital receipts (of which £0.4bn are held by counties, £0.6bn by metropolitan districts, £1.2bn by London authorities, and £4.2bn by shire districts).

15. Under the new capital control system, local authorities will be required to apply a proportion of their cash-backed capital receipts to debt redemption. (The proportions at present envisaged are 75% for the proceeds of council house sales and 50% for other receipts). In terms of their ability to use capital receipts to finance capital expenditure, they will "lose" this amount and the Treasury's first concern is that this may provide an incentive to them to "use" their capital receipts in the interim to undertake extra capitalised repair and maintenance expenditure.

16. Quite apart from this, and leaving aside the question of RSG incentives to capitalisation, the Treasury's second concern is that the prospect of the new system may also provide an additional incentive to local authorities to transfer expenditure that they would otherwise have incurred on repair and maintenance from revenue to capital account. That would not represent additional expenditure, and would probably be accomplished by ex post facto bookkeeping adjustments, but would have the effect of converting a corresponding amount of capital receipts into revenue balances, which would be available to finance further expenditure rather than be applied (in part) to debt redemption.

17. There are a number of constraints or disincentives which will in practice limit the use of capital receipts (either to finance extra expenditure or to transfer expenditure out of reserve account) :-

- i) Not all repair and maintenance expenditure can properly be capitalised. (works which will lengthen the lives of assets or save expenditure in several future accounting periods may qualify - day-to-day repairs do not);
- ii) There is a marked "mismatch" between the distribution of capital receipts (primarily in shire districts) and the distribution of the sort of structural maintenance that can properly be capitalised. (Some of the authorities who have latterly made extensive use of capitalisation have now used up their capital receipts);

iii) To the extent that capital receipts are spent before the new capital control system comes into effect, the amount of capital spending power which local authorities will derive in the new system from capital receipts will be reduced. (For any given level of capital receipts, the new system will, by comparison with the present system, give local authorities greater freedom to spend a smaller overall amount. But it will permit a larger proportion to be spent in any given year). Thus to use capital receipts for extra maintenance will make it more difficult to undertake future large projects.

iv) In so far as additional repairs are carried out using capital receipts, councillors will not perceive any benefit to rate/community charge levels, since the savings on future maintenance will be offset by loss of interest on the cash balances or by the debt charges on debt not redeemed.

v) Depending on the choice made between options G1 and G2 below, the present strong grant incentive to capitalisation may be removed.

18. DoE's assessment is that the amount of additional repair and expenditure which might be undertaken as a result of knowledge of the proposals for the new capital control system would not exceed £200m in 1989/90. (This figure is an upper bound, not an estimate). The overall scope for capitalisation by bookkeeping adjustments might be as much as £1000m over the 3 years 1987-88, 1988-89 and 1989-90.

#### OPTIONS FOR REDUCING RISK

19. This section considers what action might be taken to reduce these risks. There are 2 grant options (G1 and G2) and one option on capital receipts (C1 and C2). Doing nothing is also an option in both cases.

20. In considering what might be done we have taken account of the situation regarding determination of grant for the forthcoming year, in the next RSG Settlement, the present year (1988/89) and, past years. Grant entitlements for 1988/89 and all outstanding earlier years are due to be

revised in Supplementary Reports later this year. These reports will take account of outturn expenditure for 1985/86 and 1986/87, of revised budgets for 1987/88 and budgets for 1988/89. Full sets of expenditure data for these Supplementary Reports are being put together now. This therefore provides a good opportunity for changing the present system to reduce the risk to the Exchequer. The next such opportunity when we will have full sets of expenditure data for all outstanding years is July 1989.

21. We have identified two main options for reducing the opportunities to manipulate the system to increase grant claims. The first requires legislation in the next session to change the basis on which grant will be distributed in 1989/90, and to limit grant claims in respect of earlier years. The second option is to delay action until summer 1989 and then legislate to close down the present system.

OPTION G1 : Immediate closedown of the present RSG system

22. The main features of this proposal are: -

(a) grant entitlements for 1989/90 would be fixed in the forthcoming settlement and would not be linked to actual expenditure. This means that there would be no grant underclaim as in 1987/88 and 1988/89, but nor would there be any risk of grant overclaim.

(b) Final grant entitlements for 1988/89 and all outstanding earlier years would be determined on the basis of reported expenditure available on the date of the announcement in July of this year (possibly with a small adjustment reflecting the normal average reduction in expenditure from budget to outturn). These grant changes would be made through supplementary reports at around the end of this year: these would be the last reports under the present system.

23. Fixing grant in this way would remove the risks to the Exchequer on the grant side. But it would also reduce pressure on local authority expenditure since higher expenditure would no longer lead to lower grant. We do not know what effect there would be on expenditure in this transitional period before

the discipline of the community charge system is introduced. But every 1% increase in expenditure is equivalent to £300m. Account would have to be taken of such grant and expenditure implications when determining the 1989/90 RSG Settlement.

24. If this option is pursued an early announcement is desirable to minimise both the risk to the Exchequer and the possibility of authorities getting wind of the proposal and adjusting the accounts before we act. A short Money Bill would be required in the autumn to achieve Royal assent by March in order to pay grant in 1989/90 on the correct basis. Apart from this the 1989/90 Settlement and the series of supplementary reports planned for the autumn would proceed as planned other than that no account would be taken of expenditure data reported to us after the date of announcement.

**Option G2: Delay closing down until 1989.**

25. Under this option the existing grant related restraints on expenditure would continue. For most individual authorities, higher expenditure would continue to mean absolute reductions in grant. The option consists of three elements:

(a) run the system for another year and announce close-down arrangements in July 1989. At that time we would have information on expenditure for all outstanding years of the present system. The legislation would simply state that for the purposes of calculating grant entitlements no account would be taken of later information expenditure in respect of any year. If at that time the scope for manipulation seems much reduced, it might even be possible to give authorities advance notice of closedown in respect of certain financial arrangements.

This element alone would carry a significant risk of grant manipulation in 1989/90. It would therefore also be necessary:

(b) to draw up a "tough" 1989/90 RSG Settlement to allow as far as possible for potential manipulation in deciding upon the spending assumptions and the grant total; and

(c) to take separate action to block off other manipulations of the system to the greatest possible extent. Action on capitalisation of repairs, etc. (Option C2 below) would certainly be necessary. Other action, to prevent the use of other devices that come to light, would have to be taken as soon as their significance or potential significance came to light.

26. The option on capital receipts is:-

OPTION C1 and C2 : Bring Capitalisation of Repairs under control.

The use of receipts to finance capitalised repair and maintenance expenditure is theoretically under the control of the Secretary of State, though that control has for many years now been waived by means of the issue of general consents and block borrowing approvals. Under the option, these contents would be modified so as

- (i) to preclude the use of capital receipts for this purpose; or
- (ii) to require specific consents to be obtained; or
- (iii) to permit the use of receipts only for specified classes of expenditure.

There are limitations on the scope for changing the rules during a financial year, and in particular for changing them with immediate effect. This is because (a) changes cannot be made retrospectively in the absence of primary legislation and (b) it is only at the end of year, when the accounts are drawn up, that particular sources of finance are imputed to the particular items of expenditure. So to the extent that permission to use receipts for any given class of transactions is withdrawn during the year, the local authority could when drawing up their accounts impute receipts to all transactions in that class before the relevant date and other sources of finance to transactions after that date.

27. In DOE's view, it is not practicable to think of altering the rules for 1988-89 so as to impose restrictions on the use of receipts to finance actual repair and maintenance during that year. It would, however, be possible to prevent local authorities from entering into advance maintenance deals (on the

lines of the advanced purchase deals for capital expenditure which were brought into control by the Local Government Act 1987). This is because there is no evidence that authorities have yet started to enter into such deals. The immediate prohibition of advance maintenance deals in Option C1.

28. It would in DOE's view be practicable to impose a more rigorous control for 1989-90. It would be necessary for consultation to be undertaken and for the consents to be modified before the end of 1988-89 so that the modification took effect from 1 April 1989 and so that authorities could allow for this when setting rates. The modification would have to be accompanied (if this had not already been done) by action in relation to advance maintenance deals. This is Option C2.

29. Option C2 would be controversial and would be represented as being inconsistent with undertakings that Ministers have given about the ability of authorities to use capital receipts to finance repair and maintenance work and the encouragement that authorities have been given to do this in the field of housing. It would have to be justified on the basis that action was needed to prevent excessive expenditure in this area financed by capital receipts or the use of receipts to liberate revenue spending power. Option C1 would be much less controversial.

#### ASSESSMENT OF OPTIONS

30. Option G1 provides the greater certainty on grant as Treasury would know exactly how much grant has to be paid out under the present system in July. The change could be presented as an orderly transition to the new system where grant will also be fixed in the Settlement. By acting swiftly we minimise the risk to the Exchequer. Local authorities would also know precisely how much grant they would be entitled to and could concentrate on setting up the new system rather than expending energy trying to manipulate the present system.

31. The first option has four main disadvantages. The first is that there would be less downward pressure on local authorities' total expenditure following the July announcement. This could lead to higher local authority expenditure in the period to March 1990. A 1% increase, as noted earlier, is £300 million. DOE doubt whether the reduced disincentive to spend more at the

margin would greatly affect the overall level of expenditure. In the Treasury's view these marginal effects do influence behaviour. Under Option 1, an average authority would have to finance some 45% of any increase in expenditure from the domestic rate-payer, as against some 73% under option 2 and 100% under the community charge.

32. A second, related disadvantage is the loss of grant underclaim in 1989-90. This needs to be set against the savings in grant from closing off the possibilities for manipulating accounts so as to increase grant entitlement.

33. A third disadvantage is that the Government would have to expect strident criticism from local authorities for changing the rules. Authorities who genuinely reduce their expenditure below present reported levels for 1987/88 and 1988/89, and below the 1989/90 settlement spending assumption would receive no reward. Further, authorities who have legally built up special funds would resent action by the Government to remove the grant entitlements which they assumed they would have on drawing down those funds. The Government would come under pressure during passage of the Bill to concede that authorities may enjoy the grant advantages of special funds: no significant concession would be possible, however, without destroying the whole approach.

34. Finally, option 1 would require a short but highly contentious money Bill in the 1988-89 Parliamentary session, where the pressures on time already promise to be intense.

35. Option G2 would have the advantages of retaining the grant-related restraints on total expenditure in 1989-90, at least until the authorities have set their budgets. There would also still be a grant underclaim in 1989-90 associated with decisions by local authorities to spend in excess of the settlement spending assumptions. And this option avoids legislation in the 1988-89 session and the opportunity that would provide for complaint and concessions.

36. This option also has several disadvantages. The main one is that between now and next summer the Government would have to be ready to meet large claims for extra grant in respect of 1987/88 and 1988/89, and in respect



of 1989/90 to the extent that the settlement did not allow for all opportunities to reduce expenditure and increase grant.

37. The second disadvantage is that at any time local authorities might bring forward new schemes to increase grant entitlements. We would either have to live with the grant consequences or stand ready to block such loopholes through further legislation. Most likely these would entail "midnight tonight" elements.

38. Thirdly we would expect a rolling barrage of criticism both about the flow of administrative and legislative changes necessary to block off loopholes, and about the implied very tough RSG Settlement. On the Settlement we would face particular criticism over assumptions that effectively required authorities to indulge in "creative accounting" arrangements such as capitalisation of which many would heartily disapprove.

39. Finally Option G2 would require a Money Bill in the 1989/90 legislative session, where pressures on time are also likely to be considerable.

40. It should also be noted that although this option would allow authorities with special funds to gain the grant benefits other authorities would receive correspondingly less grant within a given grant pool. The grant distribution in 1989/90 might therefore be very skewed leaving some authorities well placed for the introduction of the community charge but others poorly placed.

41. Options C2 will prevent exploitation of the freedom to capitalise repairs and renewals in 1989/90. It is likely to be badly received by local government (see para 28 above) even if the approach is modified e.g. to allow capitalisation on the level of recent years. Furthermore, authorities have to know what is proposed before they set their rates for 1989/90, but this fore-knowledge will give them an opportunity to maximise capitalisation in 1987/88 and 1988/89. This option cannot therefore be wholly effective. Option C1 would be less controversial and would operate successfully on one aspects of the problem. Neither of these options would require legislation.

42. Either Option G1 or G2 can be combined with Option C1, or Option C2. Option G1 (RSG Closedown in July 1988) would remove the grant incentives to undertake capitalisation and to that extent, but to that extent only, would make Options C1 and C2 less necessary. A combination of Option C2 and Option G2 would be an effective approach to 1989/90 provided allowance was made for potential manipulation in framing the 1989/90 Settlement, but this combination of a pre-emptive Settlement and the announcement of Option C2 might well lead authorities to maximise the opportunities still open to them in 1987/88 and 1988/89. Option C1 would, however, shut off one avenue of manipulation completely.

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ANNEX A

Scope for Manipulating Total Expenditure In Order To Gain Grant

N.B. These figures are estimates of the maximum potential use of the various devices. We have no evidence that they will be used on this scale.

	Maximum grant at risk £m.
Special Funds : £1.1bn of special funds available at April 1989. Use of up to £900m could be allowed for in 1989/90 settlement. Remaining £200m could be used in earlier years to increase grant claims by around £200m	200
Capitalisation of repairs and renewals: LAs have around £7bn of cash backed capital receipts that could in principle be used to finance repairs and renewals. In practice the scope is much lower as around £5bn receipts are held by shire districts. But as much as £1bn could be used between 1987/88 and 1989/90 to reduce total expenditure thereby increasing grant claims by £500m.	500
Factoring : This scheme is specifically designed to reduce total expenditure and increase grant. It involves "selling future capital receipts" for a lump sum which is then invested. The resultant interest receipts count as a reduction to total expenditure and hence increase grant. The future capital receipts are "repurchased" post March 1990. One London Borough is already planning to increase RSG entitlements by £½m in both 1988/89 and 1989/90 through this arrangement. The total RSG at risk in 1988/89 is probably small but in 1989/90 could in principle be up to £100m. Consideration is being given to ways of stopping this abuse of the system.	100
Debt Servicing: LAs could reduce repayments of outstanding debt from the revenue account by shifting the profile of repayments or by early repayment of outstanding debt from capital receipts. At risk here is up to £200m of expenditure and hence around £100m of grant for the period up to March 1990.	100

Short term delaying of expenditure :

There is scope for authorities to holdback expenditure from the early part of 1990 and have a surge of expenditure in April 1990. We have seen evidence of this when targets and holdback were abolished in 1986. Perhaps 2% of expenditure might be so delayed. This would increase grant claims by around £300m.

300

Interest rate swaps :

This involves swapping a low interest loan for a higher interest loan with an outside body for an up front premium. This premium is then invested and the interest receipts used to reduce total expenditure. Although the amounts swapped are large the effect on total expenditure is relatively small.

Other schemes : We know of a number of other small scale schemes for reducing total expenditure. We cannot rule out however that new large scale schemes may be devised.

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