

CHIEF SECRETARY

FROM A J C EDWARDS
DATE 29 JUNE 1988

cc Chancellor—
Sir P Middleton
Mr Anson
Mr Potter
Mr Fellgett

RATE SUPPORT GRANT, 1989-90 AND CAPITAL RECEIPTS

Following your meeting with Mr Ridley this morning, we have reached agreement with DOE on:

- (i) the estimated consequentialials for rates next year of increases in aggregate Exchequer grant of between £350 million and £850 million (annex A);
- (ii) what would best be done (if it were agreed to do something) to limit manipulations of capital receipts next year (annex B); and
- (iii) small revisions to the joint paper by officials which I submitted last night.

Estimated rates consequentialials of particular levels of grant

2. The gratifying results presented in DOE's note at Annex A confirm the figures which Mr Fellgett quoted this morning. DOE now accept that, for an increase of 3 per cent in real terms in overall spending by Local Authorities, and assuming that they draw down balances and special funds by £570 million, the range of increases in grant which you discussed this morning would produce the following average increases in rates:

Increase in grant £m	Average rate increase (per cent)
350	6.6
450	6.1
600 550	5.6 5.3
650	5.0
750	4.5
850	4.0

These increases compare with a 7½% average increase in rates this year.

3. If local authorities decided to draw more heavily on special funds and balances, the increases in rates could of course be significantly lower. The amount of special funds outstanding is some £1.1 billion, and balances outstanding are believed to be similar in magnitude. Each £200 million drawing on special funds or balances would reduce the rates increase by 1 percentage point.

4. The DOE figures seem to us powerfully to reinforce the case which you have argued on overall expenditure control grounds for a low grant increase. There was, I think, widespread support in E(LA) for the thesis that the Government had little interest in making rates popular in their last year. Even the lowest grant increase illustrated above (+£350 million) would, on these calculations, entail a lower increase in rates than this year.

Capital receipts

[To Follow] 5. The note at annex B, ^{prepared} ~~proposed~~ by us after discussion with DOE, sets out what would best be done on capital receipts if Ministers agree that they cannot be indifferent to a possible surge of up to £550 million in authorities' spending potential next year. DOE have calculated that they could spend £200 million on extra repairs and maintenance and substitute up to £350 million of capital receipts for revenue financing of repairs and maintenance expenditure, thus liberating an equivalent sum of revenue for spending elsewhere.

6. In our view there is no question that action must be taken to preclude advance maintenance deals (option C1). The experts now think, however, that this should not be announced on 7 July since drawing attention to the possibilities for manipulating

capital receipts would encourage local authorities to increase repairs and maintenance expenditure and/or explore the possibilities for substituting capital receipts for revenue financing.

7. DOE remain opposed to taking any action to limit possible use of capital receipts by local authorities to enhance expenditure or balances in 1989-90 (option C2). They agree, however, that the two realistic options for dealing with this problem, in descending order of efficacy, are:

- (i) amend the consent in Circular 5/87 so as to limit the use of capital receipts to finance repairs and maintenance to this year's level of around £500 million: for the reasons explained in annex B, this would best be announced in November;
- (ii) achieve offsetting savings in capital expenditure, if possible, by increasing the assumed level of non-prescribed capital and reducing the capital allocations agreed in the survey (say by £350 million).

Clearly approach (i) is far superior to approach (ii) from the Treasury's point of view. It would be extremely difficult to persuade Messrs Baker, Channon and Moore in the survey, not to mention Mr Ridley himself, to accept capital allocations several hundred million ^{pounds} lower than they would otherwise have been.

8. We suggest that you should continue to argue for approach (i) in the previous paragraph, to be announced in November alongside option C1, up to and including the Prime Minister's meeting.

Simultaneous announcement of grant and closedown

9. Assuming that Ministers decide on option 1, Mr Ridley

envisages a timetable whereby Cabinet would confirm the decision next Thursday morning (7 July) and he would make the announcement that afternoon. It seems to us important that he should announce the amount of Government grant as well as the closedown proposals. There are two reasons for this:

- First, the Government would come under great pressure between 7 July and the end of the month to provide a generous grant settlement if the initial announcement had not covered this.
- Second, it would anyway be difficult presentationally to announce a fixed grant for 1989-90 without indicating the level at which it would be fixed.

The decisions on rate capping and expenditure provision would then be announced later in July, in accordance with the normal timetable.

10. You may like to check with Mr Ridley tomorrow that he too envisages announcing the level of grant on 7 July as part of the fixed grant/closedown announcement..

Consultation with other Ministers

11. Mr Ridley seemed to envisage this morning that a small group of Ministers comprising the Prime Minister, the Chancellor, Mr Parkinson, Mr Wakeham, himself and yourself would decide on closedown and the level of grant for 1989-90.

12. Before you and Mr Ridley joined the meeting, we considered the logistics of consultations with the colleagues. Our provisional conclusion was that the best approach might be:

- (i) to cancel next week's E(LA) meeting and deal with rate-capping in correspondence;
- (ii) Mr Ridley to minute the Prime Minister on Friday,

in preparation for a meeting of those in paragraph 11 above on Tuesday next (5 July);

- (iii) to have an E(LA) meeting immediately before Cabinet on Thursday (7 July), so as to bring E(LA) Ministers more fully into the picture; and
- (iv) to arrange E(LA) meetings as necessary between 7 July and the end of the month in preparation for the usual announcement at the end of the month covering rate-capping and expenditure provision.

13. We have to consider also the problems of Wales and Scotland. Although Mr Walker *might* contest the point, we think that the only sustainable solution is for fixed grant and closedown to apply in Wales just as in England. It would be much best for Mr Ridley to cast his 7 July announcement in terms of England and Wales. Mr Walker will however need to be consulted. We think therefore that Mr Ridley should copy to Mr Walker his minute to the Prime Minister and that a Welsh Office minister should attend the Prime Minister's meeting: Mr Walker himself will, we understand, be abroad next week.

14. The Scots have a different RSG system and are due anyway to introduce the Community Charge next year. We do not think, therefore, that any closedown option will be needed there. A possible way ahead would be for Mr Ridley to copy to Mr Rifkind his minute to the Prime Minister but note that his announcement will not affect Scottish local authorities.

15. It would be useful to discuss these issues with Mr Ridley tomorrow. Miss Rutter might also like to check whether DOE have booked a slot in the Prime Minister's diary for next Tuesday.

Objectives for July and November packages

16. If you agree with the above, your objective might be to

end up with an announcement on 7 July covering both England and Wales and comprising:

- (i) a fixed grant of between £350 million and £630 million (England) for 1989-90;
- (ii) immediate closedown of grant claims in respect of all earlier years; and
- (iii) issue of the consultative paper on the new capital control system.

17. This would be followed at the end of July by an announcement on rate-capping and expenditure provision, and in November by an announcement on advance maintenance deals and limitation on the use of capital receipts for repairs and maintenance.

Checklist of points for meeting

18. It maybe helpful to summarise the points on which you will wish if possible to reach agreement with Mr Ridley:

- (i) option 1 on fixed grant/closedown
- (ii) amount of grant (preferably £350 million given the new rates figures and certainly not more than £630 million);
- (iii) on capital receipts, options C1 and C2 (consent variant), to be announced in November;
- (iv) 7 July statement to cover fixed grant and closedown, including level of grant for next year, and consultative paper on new capital control system;
- (v) statement to cover Wales as well as England, but not Scotland;
- (vi) Mr Ridley to minute the Prime Minister, Chancellor,

Mr Parkinson, Mr Wakeham, Mr Walker, Mr Rifkind and yourself on Friday;

- (vii) Prime Minister's meeting on Tuesday next;
- (viii) cancel E(LA) now planned for next week but fix a meeting immediately before Thursday Cabinet if possible;
- (ix) Thursday Cabinet to confirm decisions prior to afternoon announcement.

AJCE
A J C EDWARDS

RATE IMPLICATIONS OF GRANT OPTIONS FOR 1989/90 RATE SUPPORT GRANT SETTLEMENT

	AEG £13,325m (+ £350m)	AEG £13,425m (+ £450m)	AEG £13,525m (+ £550m)	AEG £13,625m (+ £650m)	AEG £13,725m (+ £750m)	AEG £13,825m (+ £850m)
Non-rate limited	8.1	7.5	6.9	6.3	5.7	5.2
All authorities	6.6	6.1	5.6	5.0	4.5	4.0
% increase in AEG at settlement	2.7	3.5	4.2	5.0	5.8	6.5
<i>% increase in AEG at outturn</i>	<i>6.7</i>	<i>7.5</i>	<i>8.2</i>	<i>9.0</i>	<i>9.8</i>	<i>10.5</i>

NOTES

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1. Based on closedown Option G1: so no grant underclaim.
 2. Assumes local authorities use £570m of reserves (special funds and balances) in 1989/90 to hold down rates.
 3. Assumes that authorities spend at 3% above inflation plus community charge preparation costs ie 7.5% above this year's budgets.
 4. % increase in AEG at settlement calculated from AEG at 1988/89 settlement adjusted for transfer of polytechnics.

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FROM: A J C EDWARDS
DATE: 30 June 1988

PS/CHIEF SECRETARY

cc PS/Chancellor
Sir P Middleton
Mr Anson
Mr Potter
Mr Fellgett

RATE SUPPORT GRANT FOR 1989-90 AND CAPITAL RECEIPTS

Here, with apologies for the delay, is Annex B to my submission of last night.

AJCE

A J C EDWARDS

POSSIBLE MEASURES ON CAPITAL RECEIPTS**C1 Stop Advance Maintenance Deals**

This would best be done by amending the consent in Circular 5/87 so as to stop advance maintenance deals unless the Secretary of State gives specific consent for them (which he would not do). Best to announce later than July but before actual deals would be contracted. Early announcement would run the risk of drawing to authorities' attention the advantages of increasing repairs and maintenance expenditure between now and April 1990.

C2 Stop or limit capitalisation of repairs and maintenance in 1989-90

This too would best be done by amendment of Circular 5/87. The consent in this Circular would be amended to stop the use of capital receipts for repairs and maintenance without the specific consent of the Secretary of State. A consequential amendment to the consent to borrow would also be needed. DOE could then, if so desired, maintain capitalisation at broadly the current level by issuing some £500 million of such consents, corresponding to the amount of repairs and maintenance currently financed from capital receipts and borrowing. DOE regional offices would distribute these consents between local authorities. Announcement would best be made in December. This would allow just enough time for the necessary consultation with local authorities and for them to finalise their 1989-90 budgets. Earlier announcement would give them more time to increase their repairs and maintenance expenditure this year.