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1. MR POTTER (LG1) BH 20/6
2. CHIEF SECRETARY

FROM : A P HUDSON (LG1)
Ext 4945
20 June 1989

cc Chancellor
Sir P Middleton
Mr Anson
Mr Monck
Mr Phillips
Mr A J C Edwards
Mrs Lomax
Mr MacAuslan
Mr G C White
Mr Rutnam
Mrs Chaplin

LOCAL AUTHORITY CURRENT : BRIEFING FOR E(LF), 22 JUNE

I attach a series of briefs prepared in LG1 for Thursday's meeting of E(LF). The top page lists the briefs.

Issues for the meeting

2. There are two key issues for the meeting:

- a. the main decisions on AEF and total standard spending (TSS);
- b. the form of the safety net.

3. In due course, E(LF) will have to consider other aspects of the settlement. The briefing provides background information on these just in case.

Objectives

4. The first objective is clear: to secure the Committee's agreement to the proposals on the TSS and AEF which have been agreed between you and Mr Ridley, and endorsed by the Prime Minister. Whether you can do so, in the light of the additional options now on the table on the safety net, and the scope this gives for further work to be commissioned, is doubtful.

5. On the question of the safety net, as you know, the position has become more complicated. Mr Ridley's main E(LF) paper proposes the form of safety net you agreed with him: the first £25 of losses borne; and protection above that to be financed by allowing

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through only the first £20 of gains, plus 25 per cent above that threshold. However, Mr Ridley is now proposing to circulate an addendum, setting out three further options for the safety net:

- a. the original formulation, with a maximum contribution from the gainers of £39 (assuming £25 of losses);
- b. allowing through 43 per cent of all gains, with no flat-rate allowance; and
- c. a variant of his previous top-slicing approach, under which everyone pays a flat-rate contribution of £26 - so big losers bear the first £26 of their losses, modest losers have their loss increased to £26, modest gainers become modest losers, and those gaining above £26 get their gains in full, less ~~from~~ the £26 contribution.

What is driving this, as before, is the desire to bring down the very high contributions to the safety net from Westminster, and parts of the Home Counties.

6. You may wish to discuss these revised proposals with us tomorrow. Annex I provides briefing.

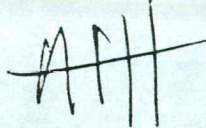
Tactics

7. You may also want to discuss the tactics for the meeting. As we see it, the key issues to decide are:

- What line to take on Mr Ridley's proposals on AEF and TSS? The present speaking note suggests that these proposals go too far. You would then allow yourself to be argued up.
- You would clearly have to explain this approach to Mr Ridley in advance. You might also want to talk to him about the safety net.
- Would it be worth either you or Mr Ridley talking to other members of E(LF) in advance? The one with the biggest interest is Mr Baker, through his paper on the bottom-up approach to total standard spending, and his interest in the new needs assessment package and in the ILEA specific grant.

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8. The Cabinet Office have scheduled further meetings of E(LF) for 6 July and, if necessary, for 13 July. Given the extra options on the safety net, it may be that the second meeting will look at a specified range of options on that. The best that can be hoped for is that the quantum of AEF is firmly settled on Thursday. If it is, there is probably no harm in taking the safety net at the second meeting.



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BRIEFS FOR E(LF)

- A. Speaking note
- B. Key points

"Needs"

- C. Terminology
- D. Total standard spending
- E. New needs assessment package
- F. Mr Baker's E(LF) paper

Grant

- G. Specific grants
- H. ILEA

Safety net

- I. Safety net ← NB.
- J. Distribution of CCs: what can be done
- K. Demand note * ~~(to follow)~~
- L. NNDR

Other issues (background only)

- M. RPI
- N. Scottish experience
- O. Years 2 and 3
- P. Use of reserves ~~(to follow)~~
- Q. General public expenditure pressures
- R. Pay pressures ~~(to follow)~~
- S. Figures.

Overtaken
- CST can explain
line he proposes to take.

ANNEX A

SPEAKING NOTE

1. Agree with Nick that this is a very important settlement, and very difficult.
2. Need to strike balance between:
 - (a) successful introduction of CC;
 - (b) maintaining ten-year policy of getting down LA overspending, which CC is designed to achieve.
3. Two levers for influencing LA behaviour: grant, ie AEF; and figure for total standard spending (TSS).

Grant

4. Nick proposes 7 per cent increase in AEF, nearly £1 billion over baseline. Very substantial increase, in what is a very difficult public expenditure round.
5. Understand reasons for this. But must be clear: cannot buy lower community charges with more grant.
6. Last year, very generous grant settlement - up 9 per cent. Intended to minimise level of rates preparatory to CC this year. Frankly didn't work. Expenditure rose in real terms by around 4 per cent - second largest overspend in ten years. And in Scotland, authorities increased spending by 11½ per cent, and increased CC by 14 per cent over domestic rates.
7. All this confirmed previous suspicions: extra grant tends to lead to extra spending, not lower rates or CCs.

8. Not surprising, since two-thirds of authorities not controlled by our supporters. Their instinct, given more cash, is to spend it, not reduce burden on taxpayer. Doubly true in first year of CC.

- Authorities will try to blame Government for high charges.

- Hard for chargepayer to compare this year's bill with last year's.

- And accountability blurred by safety net.

9. Aim therefore a settlement which enables reasonable LAs, including own supporters, to set reasonable charges. Not persuaded this requires as much grant as Nick proposes. Most of extra will simply go in higher spending, as we have seen before.

TSS

10. Also think Nick ^{may have gone} ~~goes~~ too far in setting TSS.

11. TSS intended to be prescriptive, not a forecast. Equivalent in old system is GREs, not provision, and still less budgets, which Nick bases his figure on. That builds in every penny piece of the £1.2 billion overspend Nick refers to.

12. Nick's proposals represent a 10½ per cent increase on GRE's, on top of a 4 per cent real increase last year. And these GREs not unrealistic - our own supporters, on average, stay within them.

13. TSS sends a signal to LAs about how much they need to spend to deliver standard level of services. Danger of levering up spending if TSS rises too far. Evidence in Scotland suggests that moderate spenders increased spending to equivalent benchmark, but that accountability has yet to have full impact on overspenders. Result: substantial increase overall.

14. Nick's proposals therefore go too far. And Kenneth Baker's proposal of £34.1 billion, 8 per cent up on last year's budgets, would frankly signal the end of any attempt to control local authority spending. Simply don't think this approach is a valid way of setting TSS: starts from budgets, thus validating overspending, and does not take proper account of scope for efficiency savings and benefits from compulsory competitive tendering. Thus bound to produce gross over-estimate.

Safety Net

15. Seen all of Nick's proposals on the safety net. Clearly very complicated, and a lot of difficult political judgements to make. Suggest we agree figures for AEF and TSS, and principles on which safety net should operate, and ask officials to look at further exemplifications. Suggest key questions are:

- how much of losses should feed through in first year;
- that decided, how do we finance that degree of protection from the gainers -by a maximum contribution, or a percentage, or a flat rate, or some combination of these approaches?

Personally, still see some attraction in Nick's proposal in the main paper. As he says, "gives protection only where it is most needed and finances it only from those who stand to make the larger gains in the long term" (paragraph 19).

16. But key thing is to decide AEF and TSS, so officials know the framework, and ask for more exemplifications. Not closing off any options, because legislation provides that safety net has to be self-financing. So more or less grant would not affect distributional questions, but simply mean higher or lower community charges across the board.

KEY POINTSAggregate Exchequer Finance (AEF)

The DOE E(LF) paper proposes a figure for AEF of £23.0 billion in 1990-91. This is broken down as follows:

	£ billion
NNDR	10.5
Grants	12.5

2. The grants figure includes Revenue Support Grant (RSG) and specific grants. Our estimate of the likely Survey outcome is that specific grants will total £3.1 billion and RSG £9.4 billion (see Annex G).

Total Standard Spending

3. The DOE paper proposes standard spending of £32.8 billion in 1990-91, an increase of 10 per cent on 1989-90.

4. This recognises upward pressures but continues to signal that further restraint on spending is needed (see Annex D).

Community charge for standard spending (CCSS)

5. The CCSS is a central government responsibility: it must be realistic, achievable and credible.

6. A figure of £275 is a figure that well-run authorities can be expected to deliver - most Conservative authorities should be able to set their charges below the CCSS.

7. In the E(LF) paper the figure of £275 for 1990-91 is compared to £227 for 1989-90. The £227 figure is however artificial - it is based on adjusted figures that reflect a number of functional changes. It has not been published and is irrelevant because the Government would have taken different decisions with different functions and NNDR in place. The important point is that the CCSS is credible and valid for the new system - comparisons with notional figures for earlier years are irrelevant.

CONFIDENTIALActual spending

8. The E(LF) paper assumes local authorities actually spend £33.9 billion in 1990-91 - 1989-90 budgets plus 7 per cent. This represents a real increase of 3 per cent (based on the GDP deflator of 4 per cent).

9. Actual spending could well be higher - particularly in the light of the Scottish experience (see Annex N). But it is no use putting in more grant, this will only encourage higher spending.

Actual community charges

10. The paper assumes average actual community charges of £301. This is based on 1989-90 budgets plus 7 per cent. But community charges could be lower because of the use of reserves (see Annex P) and the increased use of fees and charges. This is particularly relevant if others argue that community charges will be much higher than £301.

11. It is important to remember that £301 is an average figure: with this AEF settlement, many community charges will be below £300; whatever the settlement some are bound to be higher.

Ready reckoner

12. For any given level of AEF, every extra £100 million of spending adds £3 to the community charge (ie assumes 36 million chargepayers).

13. Similarly, for any level of spending, an extra £100 million on AEF reduces the community charge by £3. (Note: Do not accept the argument that extra grant reduces community charges - it finances higher spending.)

Import

TERMINOLOGY: KEY TERMS

Mr Ridley is proposing several changes in the terminology that has so far been used in discussing the new system of local government finance. These changes are:

- Standard Spending Assessment, (SSA) in place of assessed need to spend, ie the amount we assess each individual authority needs to spend if it is to provide a standard level of service.
- Total Standard Spending, (TSS) for aggregate assessed need to spend, ie the total amount we think authorities in aggregate should be spending to provide a standard level of service (equals the sum of standard spending assessments).
- Community Charge for Standard Spending, in place of Community Charge for Spending at Need (CCSN), ie the community charge which would be set in all areas if all authorities spent at the level of their SSA (ignoring any safety net adjustments).

2. The aim in all these changes is to remove the objectionable phrase "need to spend". We have long been concerned about this terminology, and DoE have now accepted that it risks introducing pressure for authorities spending below the level at which we think they would have to spend to provide a standard level of service, to spend up to that level. These changes are therefore to be welcomed.

3. Mr Ridley has, however, stuck to the term Needs Grant instead of Revenue Support Grant. This is a recent innovation (unlike the phrases he has now dropped), and is much favoured by Mr Gummer. The term is dangerous, and we recommend you to press Mr Ridley hard to change it back to Revenue Support Grant.

Line to take

- welcome changes in terminology proposed in E(LF) paper
- but very unhappy about use of term 'Needs Grant', instead of Revenue Support Grant.

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- absurd to replace references elsewhere to spending necessary to meet 'needs' with spending for 'standard level of service' but retain concept in 'Needs Grant'.

- term 'Needs Grant' has no standing; correct term in legislation Revenue Support Grant; would oppose any change in legislation to introduce the term.

- very concerned about political pressure to which we will be exposing ourselves if we use term 'Needs Grant'; will raise profile of whole issue of Government's support for local authorities, advantages for ourselves; can see no sense in creating unnecessary difficulties.

Total standard spending

1. The DOE E(LF) paper proposes a figure of total standard spending (previously called "need to spend") of £32.8 billion for 1990-91.

2. This represents an increase of over 10 per cent on GREs (needs) in 1989-90.

3. Compared to 1989-90 budgets it represents an increase of about 3½ per cent. But it is important to distinguish between budgets (actual spending) and needs (standard spending). The appropriate comparison is with GREs (needs) for the following reasons:

(a) using budgets would validate local authority overspending;

(b) if needs were set in relation to budgets it would be an admission that local authorities (particularly Labour) had not been overspending in the past;

(c) budgets in 1989-90 are inflated by one-off spending of up to £1 billion from special funds/reserves (see Annex P);

(d) a distinction between needs/standard spending and actual spending is an important distinction to maintain. It provides a signal about the Government's desire to reduce overspending.

4. Arguments why £32.8 billion is appropriate:

(a) Existing levels of GREs by no means unrealistic - after all, taken together, all conservative authorities spend below GREs.

(b) Nothing in new system which implies a step change is justified.

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(c) An increase of 10 per cent is ample recognition of the pressures on pay and additional burdens. (For pay pressures, see Annex R.)

(d) Community charge is about getting spending down, anything higher gives the wrong signals.

(e) A higher figure will lever up actual spending by encouraging authorities that spend below standard spending to spend up.

(f) Still considerable scope for efficiency savings and contracting out more work. Need to maintain pressure for further savings, hence figure should not show large increase on budgets.

5. The DOE paper points out that the total of £32.8 billion includes financing items - loan charges, interest receipts, etc - and argues that if these go up then the current element (the amount left to be spent on services) will be squeezed. This could be seized on by departments as a reason for increasing the total. But it is tantamount to a "bottom-up" approach and there is no reason to specifically look at financing items. In fact they could go down as well as up and spending on services would benefit. However this is all for discussion in the autumn, as part of the discussions on the service distribution, and it would not be appropriate to get involved in detailed discussions now.

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Total standard spending - new assessment package

1. DOE officials have been discussing proposals for new needs assessment packages with the Local Authority Associations over the last 6 months. The aim is to introduce a simpler, fairer system for distributing Revenue Support Grant. Mr Ridley circulated a paper showing the effects of a number of packages to colleagues on 25 May 1989. He asked for comments so that he could construct a suitable package for use in E(LF) discussions.

2. The package that has been chosen for the E(LF) discussions reflects comments by colleagues and should not cause any great difficulties. However it only partly reflects Mr Baker's concerns on education in London - it increases Education needs in London from about £620 million to £750 million in 1989-90, compared to Mr Baker's request for £800 million. DOE believe that £800 million goes too far and leaves unacceptably low education figures for the rest of the country.

3. The main impact of the package is as follows:

(a) it moves grant away from the Shire counties;

(b) it moves grant into inner London (mainly as a result of the education change);

(c) it moves grant away from the Metropolitan districts but into the Shire districts.

4. This should not be controversial and there is little direct Treasury interest. The package chosen for E(LF) is for illustration purposes only and further changes can still be introduced. Final decisions will be taken in the autumn.

5. The new assessment package will provide the long term mechanism for distributing Revenue Support Grant. In the short term, any redistributive effects of the new assessment package are overridden by the safety net.

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Service departments' assessment of "Need to Spend"

1. The paper to be presented by Mr Baker proposes an aggregate "need to spend" figure of £34.1 billion in 1990-91.
2. You are aware that Mr Clarke has refused to endorse the Department of Health (DH) figures and these have been withdrawn from the paper. Thus instead of an aggregate of £34.5 billion, as previously expected, the total has been reduced because for DH the paper simply repeats 1989-90 budgets.
3. Mr Baker's paper reflects the "bottom-up" approach and can be criticised on the following grounds:
 - (a) It starts from the wrong base - actual spending rather than needs (see Annex D on why this is inappropriate).
 - (b) It proposes a 15 per cent increase on 1989-90 in needs (even without any increase for DH).
 - (c) A 15 per cent cash increase is more than twice the increase in any one year in the 1980s except one. (The highest increase was in 1986-87 - 7.8 per cent).
 - (d) It represents a real increase of more than 10 per cent in one single year - more than the total real increase over the last 10 years.
 - (e) Why does 1990-91 warrant special treatment? - it will give all the wrong signals to authorities.
 - (f) It is not a proper "bottom-up" approach. It does not look at unit costs and more efficient ways of providing services (it fails to take proper account of the spread of best practice). For example difficult to believe that there are no efficiency savings to come from over £500 million spending on OAL.

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(g) It does not take proper account of the savings identified by the Audit Commission - paper only identifies savings of £200 million compared to over £500 million that could be realistically expected from Audit Commission work. (Audit Commission have identified potential savings of some £2 billion. Individual auditors said that by March 1988 they had identified annual savings of £750 million but that authorities had only achieved savings of £250 million. So plenty of scope for more, certainly £500 million is not unreasonable.)

(h) Must therefore query whether whole approach is valid. Unlikely that departments have genuinely tried to assess costs of providing services on a consistent basis.

(i) The withdrawal of DH from the exercise only goes to emphasise the lack of consistency in the methodology.

(j) Even if the aggregate is of little value, the exercise might have had some marginal benefit in establishing relative service priorities. ^cWould have been useful to help establish service distribution in the Autumn. But the service distribution for 1990-91 is exactly the same as the 1989-90 distribution. This must again throw doubts on whether this has been a genuine exercise. X

4. Mr Baker's proposal is even higher than DOE's forecast of actual spending of £33.9 billion (1989-90 budgets plus 7 per cent). Mr Baker may argue that this is unrealistic. He will almost certainly query the inflation assumption of 4 per cent. However we can argue that 7 per cent on budgets still represents a large increase on 1989-90 and even if the inflation assumption were to increase this should still represent a real increase. It is, of course, possible that actual spending could be higher than 7 per cent above budgets but it is unlikely to be in our interests to put this forward at E(LF).

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ANNEX G

E(LF) BRIEFING : SPECIFIC GRANTS

The attached table summarises the bids for specific grants within AEF for 1990-91, along with Treasury divisions' forecast of the outcome.

2. As you will see, in the majority of cases the bids are very small. But there are significant bids for the Personal Social Services grants (items 10 and 11), and, of course, the Home Office grants (items 12-16).

3. As you will recall, the original aim was to settle specific grants within the AEF envelope before final decisions were taken on the quantum of AEF in E(LF). You agreed this with Mr Ridley and other colleagues earlier in the year, to get round the danger that Mr Ridley would seek to reopen the AEF decision in the autumn if substantial increases were agreed in specific grants, which left less room for Revenue Support Grant than he had envisaged at the time of the settlement.

4. However, it now looks as though a firm decision on AEF may be reached on Thursday, before we have been able to settle the specific grants. Neither Mr Ridley nor his officials have asked about the likely outcome on specific grants, and we have not taken this up with them.

5. We propose to continue to try to settle these specific grants this month, wherever possible. The question is whether you should tell Mr Ridley of the likely outcome, and if so, when.

6. The risk in telling Mr Ridley is that he will think the amount of room left for RSG within AEF is too low, and will seek to reopen the deal. But the argument for speaking to him is that it is better to sort this out now, rather than to risk him coming back at a later stage.

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7. The figures are as follows:

Breakdown of AEF

	£ billion		
	DOE baseline (1989-90)	E(LF), with SGs up 4% + ILEA	E(LF), with SGs at HMT forecast
AEF	21.4	23.0	23.0
Of which:			
RSG	9.1	9.5	9.4
SGs	2.8	3.0	3.1
NNDR	9.5	10.5	10.5

8. Our advice would be to say nothing on the subject until after Thursday's meeting if possible. But subject to the outcome of that meeting, you might take the opportunity to tell Mr Ridley the position, perhaps along the lines of:

- specific grants within AEF look like increasing by around £300 million over the equivalent 1989-90 figures;
- one-third of the increase is down to the new ILEA grant, and most of the rest to higher police grant;
- these grants will be settled soon, as agreed, so there will be no shocks in the autumn;
- and the increase in unhypothecated finance (RSG and NNDR) should be around 7 per cent, the same as the increase in specific grants excluding ILEA.

9. If asked about specific grants at the meeting, we suggest the line to take might be:

- still in early stages of assessing and discussing bids;
- and clearly some substantial bids, which will need careful consideration;
- but would expect increase in specific grants ^(excluding ILEA) over 1989-90 equivalent to be broadly in line with the increase in AEF as a whole, (excluding ILEA grant.)

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Version of: ²⁰ June 1989

1989 SURVEY: SPECIFIC GRANTS WITHIN AEF (ENGLAND)

GRANT	1990-91 fm					
	Baseline	Dept. position	Forecast outcome	HMT position	Grant rate %	Forecast addition to GGE (f
1. LEA TGS*	127.2	-0.2	-1.5	-1.5	65/50	0
2. Educ support*	84	0	-1	-1	60/50	0
3. Travellers' children	0	5	4	3	75	0
4. JLEA	0	100	100	100	100	0
5. Careers service	19.7	0	0	0	0	0
6. Shelter employment	17.8	3.9	0	0	50	0
7. National Parks SG	9.3	0.7	0.3	0.3	75/95	0.5
8. Urban Programme	55.9	0	0	0	75	0
9. Housing benefit admin.	93.8	0.7	0.7	0.7	50	1.4
10. AIDS and HIV	0	9.8	9.8	7	70	3
11. Soc services tra	0	26.4	19.4	13.1	70	6.5
12. Magistrates' courts	159.8	16.4	15.2		80	19
13. Probation	178.3	13.5	12.4		80	15.5
14. Police	1904.8	208.5	193.2		91	177.9
15. Civil defence	17.9	0.5	0.5		75/100	1.5
16. CWwealth immigrants	117.6	2.3	0		75	0.5
TOTAL	2784.6	387.5	353	121.6		427.9

* already settled

ILEA specific grant

1. ILEA currently spends about £1 billion on education compared to a needs assessment of about £600 million. Under the new needs assessment this is likely to increase to about £750 million.

2. To help finance the additional burden that is to be placed on the inner London boroughs it is proposed that a specific grant be introduced.

3. The specific grant would be phased out over a number of years. Mr Ridley has suggested 3 or 4 years. It would recognise that savings cannot be achieved immediately and would be designed to allow boroughs to achieve savings over this period. The level of grant would start at £100 million in 1990-91.

4. Mr Baker may argue that the grant needs to be phased out over a longer period. The longer the period of grant the less incentive there is for an authority to find the necessary savings. To maintain the pressure for efficiency gains the grant should only cover a 3-4 year period. This would also be consistent with the number of years proposed for the safety net.

5. The specific grant can be introduced in two ways:

(a) distribute the specific grant and then apply the safety net;

(b) apply the safety net and then distribute the grant.

The effects of the two are very different.

6. Under (a) the safety net dominates and, in the first year the main authorities which benefit are contributors to the safety net (City of London, Kensington and Chelsea, and Westminster). The high spending London boroughs are protected by the safety net and this overrides the effect of the specific grant. The grant

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therefore provides little help to the 'losers' in the system, ie those who benefit from the safety net.

7. Under (b) all inner London boroughs gain. It has the effect of reducing CCs in high spending boroughs to relatively low levels. First they benefit from the safety net and then they benefit from the specific grant. Under (b) the grant reduces CCs by a further £50-60. It will mean low CCs in the first year but, as both grant and the safety net are phased out, there will be large increases in CCs.

8. The DOE E(LF) paper argues that all inner London boroughs need extra support and proposes (b).

9. The grant can be distributed to each authority in a number of ways. It can be based on:

- (i) number of charge payers;
- (ii) number of children;
- (iii) education service assessment;
- (iv) actual spending on education.

10. The E(LF) paper is based on (ii). Actual spending makes more sense because the inherited overspend will be greatest in those authorities spending most. DOE recognise this but have not yet been able to calculate the figures. A change to (iv) would benefit those authorities with more schools (ie Westminster would probably lose out) but it is unlikely to change community charges by more than £5-6. The exact details of the method of paying grant needs further exploration and need not be considered in detail in the first E(LF) meeting.

11. The number of community charge payers in Inner London is about 1.8 million. Thus an increase/decrease in the specific grant of £10 million will cut/raise community charges by £5-6.

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ANNEX I

SAFETY NETBackground

You are familiar from earlier briefing with the basic principles of the safety net. It is:

- intended to protect authorities from the effects of major changes in the distribution of income, following the introduction of the new system;
- a zero-sum game: it must be self-financing under the existing powers, with protection for losers on the transition to the new system offset by contribution from the gainers.

2. In public we have said the safety net will:

- protect all losers fully, apart from a few £s per head;
- be funded by taking all the gains away from gainers, subject to a maximum contribution of £75.

Summary of Options

3. When you met Mr Ridley last week, you agreed with him on the precise formulation of the safety net that should be put forward to E(LF) as a central option. This was, in short,

- (i) Losses of up to £25 to feed through at once. Losses above £25 to be protected by safety net.
- (ii) Financed by allowing through all gains up to £20, but then taking in 75 per cent of all gains above £20.

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4. Mr Ridley has however now circulated an addendum to the E(LF) paper. This contains no fewer than 5 further options for the formulation of the safety net. In all there will therefore be 6 options on the table at E(LF) tomorrow. These are summarised in the attached table, which follows the order in Mr Ridley's new paper. (Also attached is a list of authorities, from largest losers to largest gainers, which should be consistent with the DOE exemplifications.)

5. The original E(LF) proposal is option 3. The 5 new options are:

(1) allow through no losses in the first year, and finance the safety net by taking in all gains as contributions, subject to a maximum contribution of £34 (column 3 in table 4 attached to Mr Ridley's note);

(2) allow through up to £25 of losses, and finance by taking in all gains up to maximum contribution of £39 (column 4);

(4) allow no losses to feed through, and finance by taking in a percentage of all gains, and allowing the rest (19%) to feed through (column 6);

(5) allow up to £25 of losses to feed through, and finance by taking in a percentage of all gains, and allowing the rest (43%) to feed through (column 7);

(6) raise the flat rate contribution (of £26) from everybody (including the losers).

6. The easiest way to assess these options is probably in two stages:

- first, decide how much of the losses should feed through;

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- and second, decide how the protection for losers should be paid for.

7. Mr Ridley's options have two different levels of losses. Options 1 and 4 allow no losses through. The rest allow £25-26 of losses.

8. He then has four different ways of paying for this protection.

- A maximum contribution, with no losses (option 1) or £25 losses (option 4).
- A percentage of the gain, with no losses (option 2) or £25 losses (option 5).
- The first E(LF) proposal, of allowing the first £20 of gains plus 25 per cent of the rest (option 3).
- A levy on everybody but the big losers of £26. This is the same as the amount of losses coming through, so would be presented as a contribution of £26 from everybody.

Assessment

Losers

9. The first question, therefore, is how much, if any, of the losses should feed through.

10. The arguments for introducing some losses are that:

- the safety net is a transitional arrangement, and it is not usual to begin a transition by actually freezing the bills of those protected;

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- the losses of many authorities are small, and it hardly seems worth operating a safety net that would protect against losses of a few pounds;
- a safety net that protected all authorities in full would be very expensive (£950m or so); a very large amount of gains would need to be deferred to achieve this; and much of this money would be used simply to defer small losses for a large number of authorities.

11. The arguments against introducing losses are two-fold:

- a high level of losses in the first year would add to the difficulties that areas like Pendle and Calderdale will already be facing as a consequence of the change to the new system;
- there would be a serious danger that Mr Ridley or colleagues would subsequently resile from an agreement to introduce a high level of losses, and expect the Exchequer (not gainers) to finance additional protection.

12. On balance, however, we do not feel that the arguments against introducing losses point to allowing no losses to feed through at all. A modest level of losses in the first year should not hurt areas in the North excessively; it should also not raise too great a danger that Mr Ridley or others will subsequently resile from the agreement. Introducing no losses, on the other hand, would be expensive in terms of contributions required - and you are well aware of the political pressure that Mr Ridley feels he is under to get gains through.

13. We think the arguments about losers point to allowing through a modest level of losses - such as £25.

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Gainers

14. You are aware that Mr Ridley feels he is under great pressure to get gains through, and not to delay them with the safety net. He is particularly keen to get the biggest gains through, for areas like South Bucks (£245) and Westminster (£247). John Mills (No.10 Policy Unit) has also drawn attention to the large gains in politically sensitive parts of the West Midlands (Birmingham, £88; Sandwell, £68; Solihull, £110; Wolverhampton, £110).

15. Our main interests are:

- to ensure that it is gainers who contribute to the safety net, not the Exchequer;
- to ensure that we come under no further pressure to put money into the safety net.

16. Apart from these interests, we do not think that there is a major Treasury interest in how the contributions should be distributed among the gainers. There is, however, clearly a political judgment to be taken here on how much big gainers should be made to pay relative to small gainers, and vice versa.

Details of Options

17. The effects of each option, and the pros and cons, are set out on the attached sheets.

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Option 1 Original formulation, no losses, maximum contribution £74 (Column 3 in table 4 of Mr Ridley's paper).

Contributions made: All gains contributed up to £74 maximum contribution

- Pros:
- full protection for losers
 - big gainers pay less than under:
 - Option 3 (option in first E(LF) paper).
 - Option 5 (£25 loss, contribution as percentage of all gains).

but more than under:

- Option 2 (£25 loss, maximum contribution £39
- Option 6 (£26 levy)

- Cons:
- large proportion of contributions go to protect small losers;
 - small and medium gainers lose all gains; only big gainers (above £74) see gains come through

- Assessment:
- Mr Ridley unlikely to pursue this option, as maximum contribution too high;
 - probably we should be prepared see some losses come through;
 - public expenditure risk: as safety net unwinds, gains realised by authorities may go into higher spending not lower charges; this risk is greater if we require larger contributions in the first year.

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Option 2 Original formulation, £25 losses, maximum contribution £39 (Column 4 in table 4 of Mr Ridley's paper)

Losses suffered: up to £25

Contribution made: all gains contributed, up to £39 maximum contribution

Pros: - big and medium gainers pay less than under all options except option 6

Cons: - small gainers lose all gains; only big and medium gainers (above £39) see gains come through

- losses feed through; hurts areas in North etc.

Assessment: - level of losses moderate, probably acceptable

- big and medium gainers should clearly perceive benefit, though unfair on small gainers;

- Mr Ridley will prefer this option to option 1; we should be content to go along with it if he presses;

- public expenditure risk probably less than option 1: more chance large gains will go to reducing community charges in year 1, rather than raising spendingⁱⁿ later years.

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Option 3 First E(LF) paper; £25 losses; contribution as 75% of all gains over £20 (column 5 in Table 4 of Mr Ridley's paper).

Losses suffered: up to £25

Contribution made: 75% of all gains above £20; gains up to £20 feed through immediately

Pros:

- small gains feed through in full;
- symmetrical: protection for big losers paid for by big gainers;

Cons;

- big gainers pay heavily; more than under options 2, 5, 6, though less than under options 1 and 4;
- complicated.

Assessment:

- Mr Ridley objects to high level of contributions from big gainers
- this option broadly meets Treasury interests: level of losses probably acceptable and low risk of being required to provide Exchequer money for more protection
- but perhaps slightly greater public expenditure risks than under option 2: as safety net unwinds more of gains may feed into high expenditure rather than low charges.

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Option 4: no losses; financed by taking percentage of all gains
(column 6 in Mr Ridley's paper)

Losses suffered: 0

Contributions made: 81% of all gains; remaining 19% feed through

Pros: - full protection for losers;

Cons: - big gainers pay very heavily; more than under any other option;

- complexity of taking proportion of numerous small gains.

Assessment: - probably not a runner, as hits big gainers so heavily;

- unlikely to be worthwhile taking contributions from large number of small gainers.

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Option 5: £25 losses; financed by taking percentage of all gains. (column 7 of Mr Ridley's paper)

Losses suffered: up to £25.

Contributions made: 57% of all gains; remaining 43% of gains feed through.

Pros: - better for big gainers than option 3 (which also has £25 of losses), and option 4 (which has no losses).

Cons: - worse for big gainers than option 2 and 6;
- complexity of taking proportions of numerous small gains.

Assessment: - to be considered alongside options 2, 3, 6, all of which involve £25 of losses;
- level of losses probably acceptable;
- but unlikely to be worthwhile taking contributions from large number of small gainers;
- some public expenditure risk, as option 3.

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Option 6: £26 losses; financed by taking £26 flat rate levy from everybody else. (column 8 of Mr Ridley's paper)

Losses suffered: £26 by all losers.

Contributions made: £26 by all gainers.

Pros:

- best deal for big gainers;
- according to Mr Ridley, 'simple to understand and present';
- some contribution from all gainers, equal to loss suffered by losers.

Cons:

- after year 1, contribution from gainers and losses actually suffered by losers no longer equal;
- turns small losers into £26 losers, after safety-net applied;
- turns gainers into losers, after safety-net applied;
- major public expenditure risks; risk £26 levy will be seen as surcharge on CC; pressure for Exchequer grant to cut levy, or reduce CCSS to compensate.

Assessment:

- variant of top-slicing;
- should be rejected as against Treasury interests;
- will attract public attention to safety net; may be in Exchequer's interest to make safety net less not more transparent;
- a silly scheme which makes small gainers into losers, and small losers into £26 losers.

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CONCLUSIONS

18. We doubt if Mr Ridley and colleagues will want to pursue the "no losses" options (1 and 4), simply because too much of the gains has to be deferred.

19. As indicated above, we think that £25 of losses is probably acceptable.

20. If you agree, the difference between the options is simply the way in which the remaining protection for losers is financed.

21. On the financing of protection, we see no overriding interest for the Treasury in choosing between options 2 (maximum contribution of £39), 3 (allow gains of £20 plus 25%) and 5 (allow 43% of gains). Options 3 and 5 may pose slightly greater risks for public expenditure than option 2, as they afford more scope for gains to be translated into higher expenditure rather than lower charges as the safety net unwinds. But this is a fine judgment, which should not drive your thinking. Basically the choice turns on a political judgment as to whether more or less of the contributions should come from small gainers or big gainers.

22. We do however see strong Treasury objections to option 6 (the £26 levy). This option leaves us most exposed to pressure for higher grant as a consequence of the safety net. We recommend you to oppose this option.

Line to take

23. General approach to adopt at meeting:

- safety net raises complex and important questions about how we distribute the amount of grant we have to decide on;
- a wide range of options just circulated by Nick Ridley: impossible to consider fully in time available;

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- should not therefore take any final decisions now, in particular on appropriate level of losses that should feed through (if any), and on precise mechanism for financing safety net.

[24. Remind meeting of major considerations at stake:

- should be cautious in introducing losses for losers, many are areas in North where position already difficult;
- these areas already face serious problems in adapting to new system;
- should not be deliberately exacerbated by decision on our part;
- that said, recognise Nick's concern that we should not be seen to penalise South to pay North; but safety net has to be a self-financing mechanism - one half of equation has to balance other half.]

25. Reaction to Nick Ridley's latest proposals:

- little time to study them;
- but initial reaction is that idea of taking in all gains as contributions, subject to a maximum contribution of £39 or £74 would not pose difficulty for us; but level of maximum contribution would of course depend on whether any losses introduced in first year;

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- but idea of percentage applied to all gains, or flat rate contribution unattractive. Percentage applied to all gains would involve collecting some very small sums. Flat rate contribution would appear to be a levy on all community charges: turns gainers into losers; and can see serious presentational disadvantages and risk of political pressure to provide extra grant to compensate;

- need further thought on all these points.

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	1	2	3	4	5	6
DESCRIPTION	Original formulation	Original formulation, £25 losses	First E(LF) paper	No losses, percentage of gain	£25 losses, percentage of gain	£26 levy
LOSSES SUFFERED	0	First £25	First £25	0	First £25	First £26 (and see below)
GAINS ALLOWED	All gains over £75 "maximum contribution"	All gains over £39 "maximum contribution"	First £20 of all gains, plus 25% of remainder	19% of all gains	43% of all gains	All gains less £26 levy
PROS	<ul style="list-style-type: none"> - Full protection for losers - Helps big gainers 	<ul style="list-style-type: none"> - Further help for big gainers 	<ul style="list-style-type: none"> - Small gains through in full - Protection for big losers, paid for by big gainers 	<ul style="list-style-type: none"> - Full protection for losers - Financed proportional to gain 	<ul style="list-style-type: none"> - Financed proportional to gain - More help for big gainers 	<ul style="list-style-type: none"> - Best deal for big gainers - NR: ° simple to understand and present - Same contribution from a
CONS	<ul style="list-style-type: none"> - Lots of gainers see no gain at all 	<ul style="list-style-type: none"> - Many gainers see no gain at all - Small losses feed through 	<ul style="list-style-type: none"> - Hits big gainers - Complicated - Small losses feed through 	<ul style="list-style-type: none"> - Restricts all gains - Hits big gainers 	<ul style="list-style-type: none"> - Restricts all gains - Still hits big gainers - Small losses feed through 	<ul style="list-style-type: none"> - Turns gainers into losers, and small losers into £26 losers. - Hard to present?
SELECTED CHARGES, pending at £32.8 bn						
BIG LOSERS:						
- Pandle	169	194	194	169	194	195
- Wandsworth	150	175	175	150	175	176
MALL LOSER:						
- Kingston-upon-Thames	324	328	328	324	328	351
MALL GAINER:						
- Peterborough	274	274	256	270	265	282
BIG GAINERS:						
- Huntingdonshire	250	246	224	242	230	234
- Westminster	414	379	480	505	448	367
						229

DOE CALCULATIONS

GAINS AND LOSSES ON FULL TRANSITION
TO NEW SYSTEM

(i.e. before safety net applied)

AUTHORITY	RBPA +4%	DOE CC1 @ANTS	LOSS GAIN
Greenwich	285	579	-294
Isles of Scilly	214	505	-291
Hammersmith and Fulham	373	563	-190
Southwark	281	439	-158
Lewisham	275	423	-148
Wandsworth	202	350	-148
Barnsley	221	367	-146
Calderdale	236	379	-143
Barrow in Furness	198	321	-123
Barking and Dagenham	244	365	-121
Bolsover	225	342	-117
Tower Hamlets	282	397	-115
Doncaster	258	372	-114
Wansbeck	238	348	-110
Kirklees	217	326	-109
Wear Valley	205	313	-108
Wakefield	237	344	-107
Sheffield	278	384	-106
Copeland	191	293	-102
Pendle	169	270	-101
Rotherham	249	349	-100
Sedgefield	225	324	-99
Kingston Upon Hull	233	330	-97
Derwentside	209	301	-92
Boothferry	220	309	-89
Easington	200	288	-88
Scunthorpe	284	371	-87
Allerdale	197	282	-85
Westfield	258	342	-84
Burnley	176	259	-83
Hyndburn	176	256	-80
Rochdale	262	342	-80
Rossendale	199	277	-78
E. Yorks	242	318	-76
Gateshead	248	324	-76
Blyth Valley	271	345	-74
Wigan	269	343	-74
Hillingdon	328	402	-74
High Peak	254	328	-74
Great Grimsby	251	322	-71
N.E. Derbs	276	347	-71
Cleethorpes	264	332	-68
Amber Valley	249	316	-67
Scarborough	204	269	-65
S. Tyneside	236	300	-64
Berwick-upon-Tweed	231	295	-64
York	187	248	-61
Erewash	265	325	-60
Sunderland	217	275	-58
Bradford	218	276	-58
Leicester	232	289	-57
Selby	205	262	-57
Newcastle upon Tyne	279	335	-56
North East Lincolnshire	227	282	-55
Merseyside	247	301	-54
Alnwick	242	296	-54
Durham	226	280	-54
Mansfield	225	279	-54

LOSERS

Middlesbrough	277	330	-53
St. Helens	262	313	-51
Ashfield	206	257	-51
Blackburn	183	234	-51
Blackpool	239	290	-51
Tameside	253	303	-50
Thamesdown	253	302	-49
Eden	208	256	-48
Bradford	298	345	-47
Bexley	247	294	-47
Torridge	169	216	-47
Richmondshire	187	231	-44
Stoke-on-Trent	210	254	-44
Chester-le-Street	237	280	-43
Bath	255	298	-43
Lancaster	211	253	-42
Craven	197	238	-41
Teesdale	183	223	-40
Havering	257	297	-40
Darlington	248	285	-37
Ryedale	211	248	-37
Torbay	258	293	-35
N. Devon	185	220	-35
Haringey	532	566	-34
N. Tyneside	313	345	-32
Bassetlaw	228	259	-31
S. Lakeland	249	280	-31
Leeds	223	253	-30
Weymouth and Portlan	203	233	-30
Tynedale	257	287	-30
N. Wilts	226	256	-30
Ribble Valley	215	245	-30
Langbaugh-on-Tees	308	337	-29
W. Wilts	232	260	-28
Glanford	259	286	-27
S. Derbs	281	308	-27
Holderness	262	288	-26
Kerrier	193	219	-26
Mid Devon	194	219	-25
Forest of Dean	203	228	-25
Lincoln	199	224	-25
Exeter	216	238	-22
Oldham	237	259	-22
S. Ribble	228	249	-21
Great Yarmouth	222	242	-20
Oswestry	202	222	-20
S. Holland	204	224	-20
Merton	285	304	-19
Lambeth	316	334	-18
Derbyshire Dales	297	314	-17
Boston	208	225	-17
King's Lynn and W. N	203	220	-17
Nottingham	234	250	-16
Dartford	218	234	-16
Newcastle-under-Lyme	238	253	-15
Penwith	205	219	-14
Portsmouth	205	219	-14
Brighton	335	348	-13
W. Dorset	231	244	-13
Harrogate	260	272	-12
Restormel	205	217	-12
Redbridge	231	242	-11
Cannock Chase	244	255	-11

Hambleton	226	236	-10
Wyr...	239	249	-10
Ch...	228	238	-10
Wansdyke	278	288	-10
Staffs Moorlands	233	242	-9
Nuneaton and Bedwort	308	317	-9
Sedgemoor	259	267	-8
Taunton Deane	255	263	-8
Ha...	259	266	-7
Plymouth	217	223	-6
W. Devon	205	211	-6
Fenland	223	229	-6
S. Somerset	259	264	-5
Bromley	255	260	-5
Medina	245	250	-5
Swale	198	203	-5
Gloucester	228	232	-4
Teignbridge	225	229	-4
Norwich	256	260	-4
Kingston-upon-Thames	324	328	-4
Stockton-on-Tees	298	301	-3
Forest Heath	226	229	-3
Warrington	266	269	-3
Ipswich	283	286	-3
W. Lindsey	200	203	-3
E. Lindsey	204	207	-3
Broxtowe	258	260	-2
Newark and Sherwood	248	250	-2
N. Shropshire	200	201	-1
Bolton	242	243	-1
Kingswood	264	264	0
Bury	308	308	0
Derby	311	311	0
Cr...	269	269	0
N. Warwickshire	307	306	1
East Staffs	230	229	1
Mendip	250	249	1
Carrick	229	228	1
Kettering	246	244	2
Caradon	220	218	2
N. Kesteven	205	203	2
Sutton	309	306	3
Salford	286	283	3
Bournemouth	254	251	3
S. Wight	269	265	4
Babergh	253	249	4
Tonbridge and Mallin	228	223	5
N. Cornwall	220	215	5
Camden	446	441	5
W. Somerset	271	263	8
Harlow	425	417	8
Breckland	223	214	9
Ealing	321	312	9
N.W. Leics	259	249	10
Stroud	251	240	11
Wrekin	267	256	11
S. Kesteven	222	211	11
Dover	198	187	11
He...	185	173	12
N. Norfolk	228	215	13
Mid Suffolk	241	228	13
Preston	233	220	13
Northampton	296	282	14

NEUTRAL

GAINERS

Wellingborough	244	230	14
Ker	241	227	14
Val Royal	267	252	15
Beverley	317	302	15
Castle Morpeth	304	288	16
St. Edmundsbury	230	214	16
Peterborough	274	256	18
East Northants	233	215	18
Se	288	270	18
E. Devon	242	223	19
S. Norfolk	251	232	19
W. Dorset	222	203	19
Gedling	274	254	20
Woodspring	305	285	20
Tamworth	264	244	20
Islington	445	425	20
S. Shropshire	208	187	21
Tandridge	302	280	22
Fylde	272	250	22
N. Dorset	216	193	23
Hounslow	373	350	23
Brentwood	408	385	23
Northavon	184	275	24
Congleton	280	256	24
E. Cambs	235	211	24
Hinckley and Boswort	257	232	25
Cheltenham	280	255	25
Gillingham	211	186	25
Thanet	234	209	25
Canterbury	224	199	25
Ellesmere Port and N	292	267	25
Corby	274	248	26
Stafford	252	226	26
Liverpool	302	276	26
Wyre Forest	242	215	27
Melton	258	231	27
S. Hams	257	228	29
Newsbury and Atcha	251	222	29
try	311	281	30
	491	461	30
beck	227	197	30
Wirral	381	350	31
Hastings	269	238	31
Worthing	248	217	31
Rutland	243	212	31
Rugby	313	281	32
Leominster	179	147	32
Crewe and Nantwich	308	276	32
Southampton	221	189	32
Manchester	322	288	34
Broadland	253	218	35
W. Lancs	275	239	36
Newham	356	319	37
Oadby and Wigston	281	243	38
Salisbury	262	224	38
Cherwell	269	231	38
Gravesham	232	193	39
Rushcliffe	289	249	40
Bl	266	226	40
Brigg	228	187	41
S. Herefordshire	189	148	41
Huntingdonshire	250	208	42
Enfield	316	274	42

Rochester upon Medwa	205	163	42
Ashted	241	198	43
Adur	281	238	43
Worcester	259	216	43
Stockport	313	269	44
Chester	302	258	44
Runnymede	294	247	47
Suffolk Coastal	287	238	49
Sharnbury	278	229	49
Reading	274	224	50
Walsall	305	255	50
Waltham Forest	325	275	50
Richmond-upon-Thames	356	305	51
Charnwood	265	213	52
Thurrock	365	313	52
Trafford	287	235	52
Maidstone	231	179	52
W. Oxon	272	220	52
Dudley	302	249	53
Knowsley	300	247	53
Tunbridge Wells	245	190	55
Stevenage	386	331	55
Redditch	270	214	56
Tewkesbury	271	215	56
Cotswold	279	223	56
Daventry	303	247	56
Watford	340	283	57
Poole	292	235	57
Gosport	245	188	57
Rushmoor	231	174	57
Christchurch	305	247	58
Spelthorne	293	234	59
Arun	270	209	61
Colchester	291	230	61
E. Herts	336	274	62
Broxbourne	326	264	62
Harrow	327	264	63
Harborough	307	244	63
Lichfield	294	230	64
Wealden	289	224	65
Tendring	310	245	65
Sevenoaks	257	192	65
Bracknell	305	239	66
Hove	290	223	67
S. Staffs	291	224	67
Sandwell	279	211	68
Chichester	262	191	71
Mid Beds	316	244	72
North Beds	310	238	72
Malvern Hills	258	185	73
Eastbourne	343	269	74
Oxford	294	220	74
Braintree	302	228	74
New Forest	264	189	75
Mole Valley	336	261	75
Cambridge	323	248	75
Epsom and Ewell	398	323	75
Warwick	361	283	78
Mid Sussex	287	209	78
Welwyn Hatfield	417	337	80
Woking	368	288	80
Basildon	434	353	81
Horsham	261	179	82

Lewes	309	227	82
Vale of White Horse	302	220	82
Basingstoke and Dean	245	162	83
Reigate and Banstead	358	275	83
E. Dorset	317	234	83
S. Northants	293	209	84
Birmingham	281	193	88
Wychavon	281	191	90
Billingham	264	174	90
S. Oxfordshire	321	230	91
South Beds	364	273	91
Eastleigh	282	187	95
Test Valley	262	164	98
Stratford on Avon	369	268	101
Aylesbury Vale	288	186	102
Croydon	267	164	103
Southend-on-Sea	357	254	103
Maldon	327	224	103
Rother	325	221	104
Macclesfield	357	252	105
Fareham	287	182	105
S. Cambs	297	192	105
Havant	280	175	105
Castle Point	339	233	106
Hertsmere	405	297	108
Windsor and Maidenhe	348	240	108
Guildford	333	224	109
Wolverhampton	306	196	110
Solihull	318	208	110
N. Herts	374	264	110
Surrey Heath	352	240	112
Hackney	351	239	112
Milton Keynes	331	217	114
E. Hants	287	173	114
Slough	265	150	115
Barnet	361	246	115
Winchester	294	176	118
Newbury	299	178	121
Waverley	362	240	122
Dacorum	375	252	123
Rochford	366	242	124
Hait	314	190	124
Luton	361	233	128
Three Rivers	406	276	130
St. Albans	389	259	130
Uttlesford	363	226	137
Wokingham	340	201	139
Chelmsford	371	229	142
Elmbridge	445	303	142
Epping Forest	415	267	148
Wycombe	386	223	163
Kensington and Chels	393	204	189
City of London	541	325	216
Chiltern	463	231	232
S. Bucks	458	213	245
Westminster	587	340	247

DISTRIBUTION OF COMMUNITY CHARGES: WHAT CAN BE DONE

1. Actual community charges are up to individual local authorities not central government.
 2. Central government does determine the CCSS (Community Charge for Standard Spending) and the safety net; accordingly for 1990-1991 it determines the pattern of safety netted CCSSs across all LAs.
 3. For any given standard spending assumption and level of AEF, these safety netted CCSS figures are a product of three factors
 - i) the new needs assessment
 - ii) the precise form of safety net
 - iii) any specific grants paid after the safety net
- i) The new needs assessments determines the long term pattern of community charges: the proposals involve switching grant away from the shire districts and into London and to a lesser extent the metropolitan districts
 - ii) The safety net is expenditure neutral; it must be self-financing under existing powers. Therefore changing the pattern of the safety net can only reduce safety netted CCSS figures in the north (ie the eventual losing authorities) at the cost of putting up safety netted CCSS in the south (ie the eventual gainers). Moreover putting more grant in is ineffective: for any given safety net this merely takes away a common sum per adult off community charges everywhere. Should Mr Ridley pursue his top-slicing RSG, ^{provision} the main arguments against it are:

- pushes up the CCSS
- appears to require controversial legislation
- room would have to be found within AEF.

iii) Within a given quantum of AEF, new specific grants also change the pattern of safety-netted CCSS figures. The proposed ILEA grant - applied after the safety net - will reduce CCSS in all inner London boroughs.

- [If appropriate]: a specific grants for areas of low rateable value would reduce community charges in the north; proposal to be investigated further.

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ANNEX K

COMMUNITY CHARGE DEMAND NOTE

A copy of the demand note as currently drafted is attached.

2. As you will see, it includes a line for contributions to/receipts from the safety-net. You expressed doubts in correspondence last Autumn about the inclusion of this line, and suggested that we should look at this point further at the time decisions on the safety net more generally were taken. In the interim, the local authority associations have been told that the Government plans to introduce the type of demand note attached.

3. The arguments against including the safety net adjustment on the demand note are that:

- it will raise the profile of the safety-net, and prompt complaints in the contributing authorities that they are having to pay towards overspending in other areas;
- it risks provoking pressure for the Exchequer rather than gainers to pay for the safety net.

4. The arguments for including this adjustment are that:

- it is necessary to show contributions to/receipts from the safety-net if accountability is to work in the first few years of the new system;
- there is a risk that gaining authorities will use their gains to finance extra spending, rather than reduce the community charge, as the safety-net unwinds; this risk will be minimised if it is clear that contributions to the safety-net have fallen compared to previous years.

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K

5. On balance, we feel that the arguments point to including the adjustment in the demand note, because of the importance of accountability, and of the risks to public expenditure posed by the safety-net. We think that technically it should be possible to exclude the adjustment line, but would recommend that it should appear provided we are content that the form of safety net chosen does not expose the Exchequer to a serious risk that we shall have to provide extra grant.

Line to Take

6. Content in principle for the safety-net adjustment to appear, provided preferences on form of safety net satisfied.

NAME OF CHARGING AUTHORITY

COMMUNITY CHARGE BILL FOR THE PERIOD
1st April 1990 - 31st MARCH 1991

NAME
AND
ADDRESS

DATE OF ISSUE

ADDRESS OF PROPERTY GIVING RISE TO CHARGE
(IF DIFFERENT)

Ref No.

You are shown in the Community Charges Register as liable to pay a Community Charge as set out below. The Community Charge helps to pay for spending on local services. Some of this spending is also paid for by the Government and from rates paid by businesses. The Governments grant system is designed to allow (before transitional "safety net" contributions) a standard level of service to be provided for a community charge of £

YOUR BILL

THE READY RECKONER

	AMOUNT NEEDED BY YOUR SPENDING BODIES TO PAY FOR THE SPENDING THEY PROPOSE (If Per head)	AMOUNT NEEDED TO PAY FOR THE STANDARD LEVEL OF SERVICE (If Per head)
NAME OF PRECEPTING BODY 1		
NAME OF PRECEPTING BODY 2		
NAME OF PRECEPTING BODY 3		
NAME OF PRECEPTING BODY 4		
NAME OF PRECEPTING BODY 5		
LESS GOVERNMENT GRANTS BUSINESS RATES		
CONTRIBUTIONS TO OR FROM SAFETY NET (SEE NOTES)		
AMOUNT NEEDED		
ADJUSTMENT (SEE NOTES)		
COMMUNITY CHARGE		
TOTAL AMOUNT OF PERSONAL COMMUNITY CHARGE DUE FOR THE PERIOD DD/MM/YY - DD/MM/YY		
LESS REBATE ENTITLEMENT		
AMOUNT PAYABLE BY YOU		

This Community Charge account is payable in 10 monthly instalments.

First payment of £ due DD/MM/YY
followed by
9 payments of £ due on the nth day of each month

YOU MUST INFORM ME IF YOU CHANGE
YOUR PLACE OF RESIDENCE DO THIS
BY FILLING IN THE FORM OVERLEAF

Payment documents to follow

FOR DETAILS OF HOW TO PAY SEE OVER
TELEPHONE ENQUIRIES TO 123 456 7890

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ANNEX 3 L

NNDR: DECISIONS AND TIMING

Background

1. There will be two sets of decisions for Ministers on the NNDR:

(a) in June/July, final decisions on the transitional arrangements;

(b) in September/October, deciding the yield of NNDR and the starting poundage.

Transitional Arrangements

2. As you know, Mr Ridley has already put forward revised proposals here.

(a) He proposes doubling the threshold for special protection for small businesses from new rateable value of £7,500 to £15,000 in London, and from £5000 to £10,000 elsewhere.

(b) And he wants to drop the present proposal to limit gains to 10 per cent of the old rate bill, in real terms. Protection for losers would be financed instead by a premium on the NNDR poundage, coupled with a 20 per cent cap on gains in the first year only. Mr Ridley's objective is to allow the gains to come through much earlier.

As you will recall, you minuted the Prime Minister opposing both these proposals. She has said that the matter should be discussed at the next E(LF) meeting.

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L

3. It is therefore unlikely that this issue will come up on Thursday. In case it does, the key points are:

- (a) on small businesses,
- doubling limit risks letting in branches of multiples, eg off-licences, even small building society branches;
 - propose instead increase from £7,500 to £10,000 in London, and from £5000 to £7,500 elsewhere, covering 70 per cent of properties;
- (b) on the premium on the poundage,
- turns gainers into losers on a substantial scale;
 - benefits those with big gains to come, at the expense of those who just about break even;
 - means starting NNDR poundage would be perhaps one-eighth higher than it should be - tantamount to breach of faith with business community about level of business rates under new system.

Generally, you could welcome the chance to discuss this. It may be better to do this in a small meeting, rather than in E(LF).

Yield

4. The yield of the NNDR will be determined broadly as follows:
- 1989-90 yield from private sector and nationalised industries uprated by September RPI;
 - plus Crown contribution in lieu of rates (revalued and uprated);
 - plus allowance for buoyancy;
 - less mandatory reliefs for charities, deduction for effect of appeals etc.

5. This is largely a matter of arithmetic, and setting the initial poundage follows from the decisions on the yield. Mr Ridley may argue, in the autumn, that the burden on business ratepayers is too high, and that the uprating should be rather less than the September RPI, particularly if that turns out high. But indications so far are that he is reasonably robust on this point.

6. The E(LF) paper incorporates DOE's estimate of the NNDR yield for 1990-91, of £10.5 billion. We think this may be on the high side - it assumes a September RPI of 8 per cent, and buoyancy of 2 per cent. But it was agreed at the Prime Minister's 25 May meeting that it was right for this to feed through to local authorities, and for it to be fully offset within AEF by lower RSG. In any case, you could resist arguments that RSG looks low on the grounds that

- what matters, to local authorities and for public expenditure, is the quantum of AEF;
- the NNDR estimate may be on the high side; though this is offset by a low estimate of specific grants (see separate brief), so that the RSG figure may be broadly right.

THE COMMUNITY CHARGE AND THE RPI

There are two effects on the RPI when the community charge is introduced in 1990-91.

- a. A one-off effect when the community charge is introduced. This arises because the general RPI does not cover those households likely to benefit most from the new system (ie high earners and pensioners). The RPI Advisory Committee Report argued that as those households covered by the RPI will have to meet a larger share of the cost of local authority services, then this should be reflected in the RPI as a price increase. It will add between 0.1 and 0.2 percentage points to the RPI.
- b. The second effect is the extent to which increases in community charges feed through into the RPI. A 1 per cent increase in the community charge will add about 0.05 percentage points to the RPI.

2. The impact on the RPI of the community charges implied by the DOE proposal (spending at £33.9 billion and AEF at £23 billion) is as follows:

One-off effect	0.1 to 0.2
Increase in community charges (£301 in 1990-91 compared to a rate bill per adult of £274 in 1989-90 is an increase of 10 per cent)	<u>0.5</u>
	<u>0.6 to 0.7</u>

3. Changes to the RPI have a direct effect on public expenditure. A change in the RPI of one percentage point has the following effects:

- a. social security benefits £280 million⁽¹⁾
- b. inflation-proofed public service
pensions £ 20 million.

(1) Assuming no corresponding increase in RPI less housing.

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4. In addition, changes in community charges affect community charge rebates. A change of £10 on the community charge adds or reduces rebates by about £40-50 million.

5. So in total, from a base of £274, each extra £5 on the community charge adds 0.1 percentage points to the RPI and about £50 million to public expenditure.

Line to take (defensive)

[If others argue that AEF should be increased so as to reduce CCs and hence the RPI.]

6. Increasing AEF would not necessarily shield the RPI at all. It all depends on whether LAs would respond by reducing their CCs or (as is all too likely) by increasing their expenditure. In the latter case there would be no RPI effect.

7. Even if extra AEF did reduce CCs £ for £ (highly unlikely), then £200 million on to AEF would reduce community charges by £5-6. This would reduce the RPI by 0.1 percentage points and result in public expenditure savings of about £50 million (though mostly not until 1991-92).

8. The eventual public expenditure impact of increased grant remains considerable (about 75 per cent of the initial increase). The cost of extra grant far outweighs any public expenditure savings on CC rebates, social security benefits and public service pensions.

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ANNEX N

Scottish experience

The community charge was introduced in Scotland on 1 April 1989. The average personal community charge is £280, which when added to the average water community charge of £21, gives an overall average community charge bill of £301.

2. This represents a substantial increase of 14 per cent over the average domestic rate bill per adult in 1988-89.

3. Scottish local authorities have plans to increase spending in 1989-90 by 11½ per cent over 1988-89 and, in addition, to build up balances (ie most of the 14 per cent increase in income will be reflected in higher spending but some will feed through into increased balances).

4. This represents a real increase in spending of some 6 per cent, although Mr Rifkind will argue that the volume increase is not so high - perhaps 3½ to 4 per cent (and that is too high).

5. Local authorities plan to increase overspending relative to need by nearly 100 per cent in 1989-90 (ie from 4½ per cent above need in 1988-89 to 8½ per cent above need in 1989-90).

6. Twelve authorities will spend more than 15 per cent above needs in 1989-90 (highest is Glasgow at 45 per cent). All of these authorities have increased spending by large amounts in 1989-90 - they range from increases of 11 per cent to 35 per cent. In other words, they could have set community charges lower - they have taken the opportunity to blame the high level of community charges on the Government.

Conclusion

7. Evidence from Scotland suggests that the introduction of the community charge will encourage local authorities to increase spending. A generous grant settlement will only fuel any tendency for them to do so - it is therefore important for the grant settlement to give the appropriate signals and indicate the Government's intention to continue to exert downward pressure on local authority spending.

ANNEX
N

YEARS 2 AND 3Background

1. Mr Ridley's paper suggests that the next meeting of E(LF) should consider how to take the year 1 proposals forward into future Survey years.
2. In the Autumn Statement, we shall have to provide figures for years 2 and 3 for:
 - a. projected NNDR payments;
 - b. Revenue Support Grant;
 - c. specific grants;
 - d. projected local authority self-financed expenditure.

Specific grants will be shown as part of departmental programmes. There is no commitment to show figures for the aggregate of AEF for years 2 and 3 - we can decide whether it is to our advantage to do so, though it would be difficult to refuse to publish the figures if asked.

Assessment

3. These four items can and should be handled in different ways.
4. Local authority self-financed expenditure is important for its impact on GGE. Decisions on that will be taken towards the end of the Survey, by Treasury Ministers, consulting DOE only so far as it is necessary. No decisions should be taken now, and it would be best to void any discussion of the issue.
5. Grant and NNDR payments will need to be agreed with colleagues, probably in E(LF). But given the uncertainties surrounding the overall Survey prospects, decisions are probably best left until the autumn, when we will be better able to assess how hard we need to apply downward pressure on these items in the interest of securing an acceptable outcome overall.

6. We shall need to consider the approach to years 2 and 3 with you in more detail nearer the time. But we are likely to be arguing for much lower figures than colleagues will want to see.

- It would help most with the Public Expenditure aggregates to have the lowest plausible figures - at the extreme, even to have a stylised presentation, showing RSG and NNDR flat in cash terms.

- If colleagues found that unacceptable (which they almost certainly would), a natural next step would be to show AEF, including specific grants, flat in real terms; or at least to show RSG and NNDR flat in real terms.

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- Spending Ministers, however, will argue that the figures should be realistic (as intended within the new planning total and the new system of local government finance), and that increasing real needs should be reflected in increasing real grant.

- I understand that DOE have yet to give this much thought. They are likely to argue for realistic figures. But they might take the point that substantial real increases would give the wrong signal about spending to local authorities.

7. As far as specific grants for years 2 and 3 are concerned, divisions will begin discussions in the normal way, though without committing themselves to publishing realistic figures, in case it is decided to go for a stylised presentation of AEF across the board.

8. We suggest the main aim at Thursday's meeting should be to keep options open. It would be best to discuss this privately with Mr Ridley before any substantive discussion in E(LF).

Line to take

9. Look forward to considering proposals on years 2 and 3 in due course. No need to decide now. [In the past, has in fact been settled in the Autumn.]

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ANNEX P

USE OF RESERVES

1. Local authorities have budgeted to draw £945 million from reserves (balances and special funds) in 1989-90. This is a very substantial amount, though drawings in previous years have certainly run into hundreds of millions.

2. Nonetheless, they still have substantial reserves left. Mr Ridley's 13 June letter says that, at 31 March 1989, local authorities had rate fund balances of £1.6 billion, and special fund balances of £2.5 billion. The pattern varies widely, of course, from authority to authority.

3. The use of balances in 1989-90, and the potential for further use in 1990-91, do not directly affect the decisions on total standard spending (TSS) and the CCSS. You accepted early in discussions the DOE view that these decisions must assume no use of reserves. But use of reserves does affect the debates about likely actual spending, and hence actual CCs.

4. You could make a number of points, arguing that actual spending and actual CCs are likely to be lower than the DOE estimates:

- (anecdotal evidence suggests that) much of the spending financed out of balances this year was of a one-off nature - special purchases of school books etc;
- *manpower figures show slight decrease - also suggests substantial one-off spending*
- it will not all therefore be carried forward into 1990-91;
- even if it is, local authorities are able to fund it again out of reserves;

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- either way, charges will be lower than in the DOE estimates, which assume spending carrying on, with no use of reserves.

5. On the other hand, DOE are likely to argue that:

most of the spending out of reserves in 1989-90 is not one-off, but continuing spending, financed from reserves because of unexpectedly high inflation, and the desire to keep rates down and spending up with elections in the counties;

- LAs will therefore want to rebuild reserves next year, particularly since the blame for higher CCs will fall on the Government;
- and with rate fund balances down to £1.6 billion, it is unrealistic to expect, under any circumstances, that anything like £945 million will be drawn down again.

6. Our own view is that DOE may well be right that LAs will look to rebuild their balances this year. It looks as though some Scottish LAs did this this year. So this ground is best avoided. But if pressed on upward pressures and likely actual CCs, you could make the points:

- LAs still have over £4 billion in ^{total} reserves;
h
- these have been built up, over the years, from rates, to provide a cushion against unforeseen upward pressures and contingencies;
- reasonable therefore to expect LAs to draw on them if necessary, to avoid adding ^{to} burden _h on taxpayer or ratepayer/chargepayer.

GENERAL POINTS TO MAKE ON PUBLIC EXPENDITURE

- Public expenditure restraint crucial part of strategy: for medium term aim of reducing tax burden; to reassure markets of soundness of financial policy and determination to defeat inflation; if Government not prepared to restrain its spending, squeeze on rest of economy must be that much greater.
- Facing very difficult Survey. Huge bids entered; significant proportion reflects commitments already made or other non-discretionary changes [some £4 billion]; little prospect of further savings of sort achieved last year (£5 billion from benefits to unemployed, housing receipts, nationalised industries performance, and agricultural market support).
- Must look hard at priorities. Every £50 million more made available to local authorities is £50 million less for hospitals or roads or science.
- Size of PSDR not a reason to spend up. Surplus reflects Chancellor's Budget judgement. Nothing that has happened since suggests judgement too tight. Quite the reverse. While demand and inflationary pressures remain strong, must be cautious. [Much of surplus will disappear naturally as economic growth moderates. Rest must be available for reducing tax burden].
- Inflationary pressures are a reason for restraint in spending, not for pumping more money into local authorities.

TRENDS IN EXPENDITURE, TAX AND BORROWING

(% of GDP)

	<u>GGE</u> <u>ex priv proc</u>	<u>Tax burden</u> <u>(non-oil)*</u>	<u>PSBR</u>
1978-79	43½	34½	5½
1979-80	43½	35	4½
1980-81	46	36½	5½
1981-82	46½	38½	3½
1982-83	46½	38½	3½
1983-84	45½	37½	3½
1984-85	46½	37½	3
1985-86	44½	37½	1½
1986-87	43½	37½	1
1987-88	41½	37½	-¾
1988-89	39½	37½	-3
1989-90	39½	37½	-2½
1990-91	39	36½	-1½
1991-92	38½	36	-1
1992-93	38	35½	-½

(Source: FSBR)

* Non-oil taxes and NICs as % of non-oil GDP

AVERAGE ANNUAL REAL EXPENDITURE GROWTH

(%)	Planning total (old)	Planning total ex priv proc	GGE	GGE ex priv proc	Debt interest
<u>FSBR</u>					
1968-69 to 1978-79	2.8	2.8	2.9	2.9	3.5
1978-79 to 1988-89	0.4	0.9	0.9	1.3	1.2
1984-85 to 1988-89	-1.4	-0.7	-0.8	-0.2	-1.8
1984-85 to 1989-90	-0.1	0.1	-0.1	0.2	-3.8
1988-89 to 1991-92	4.1	3.4	2.2	1.7	-10.7

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ANNEX R

PAY PRESSURES

The main pressures on the pay of LA employees come from the following groups:

(a) Administration, technical and clerical (722,000 GB). Claim for 12% from July 1989. Latest offer from employers 7%. NALGO balloting on rejection of offer and industrial action (succession of 1, 2, 3 day strikes). Other unions (NUPE, TGWU) balloting on rejection of offer, but may be possible to settle around 8%. Could be lower from July 1990, say 5%-6%.

(b) Teachers (455,000 E & W) 6.3% settlement from April 1989. May be possible to settle around inflation rate for settlement from April 1990. Therefore likely be 6%-7%.

(c) Police (146,000 GB) 8.5% settlement from September 1988. Settlement based on average earnings in 12 month period to May. Therefore likely to be around 9% from September 1989. Assume similar increase, 7%-9%, from September 1990.

(d) Manuals (1 million) 5.6% settlement from September 1988; may well be higher from September 1989, c.6-8%. Assume lower increase from September 1990, say 6%.

2. As you know, DOE have projected LA spending in 1990-91 as 7% above 1989-90 budgets. On that basis, most of the cost of the rises assumed above could be regarded as included within the DOE projection if we argue that forecast rises in 1989-90 should

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already be reflected in 1989-90 budgets. On that basis, the 1990-91 rises projected above would put only limited additional pressure on LA spending in 1990-91, at most £100 million.

3. Colleagues may dispute this, particularly if there is uncertainty over the 1990 inflation rate. You will however wish to reject any suggestion that Total Standard Spending, or AEF, should be increased to reflect any extra pressures on pay.

Line to Take

4. - difficult to project pay trends beyond current year, but good chance many LA settlements next year will be lower than ⁱⁿ ~~this~~ ^{year};
- DOE projection of actual spending already assumes spending up 7% in 1990-91 compared to 1989-90; some 1990 pay settlements may in fact be below this, though there is of course always ^{pressure} on police pay; expected 1989-90 increases ^{for all groups} should already be reflected in 1989-90 budgets;
- reject any suggestion Total Standard Spending or AEF, should be increased to accommodate possible extra pressures on pay; best way in which we can hope to contain pay settlements is to hold down AEF and TSS.

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	<u>1989-90 adjusted figures</u>	<u>E(LF) proposal</u>	<u>Cash increase</u>	<u>% increase</u>
<u>Total Standard Spending</u> fbn	29.7	32.8	3.1	10.4%
<u>AEF</u> fbn	21.4	23.0	1.6	7.5%
Of which:				
RSG fbn	9.1	9.4*	0.3	3.3%
SGs fbn	2.8	3.1	0.3	10.7%
NNDR fbn	9.5	10.5	1.0	10.5%
<u>CCSS</u> £	227	275	48	21.1%
<u>DOE projected actual spending</u> fbn	31.7	33.9	2.2	6.9%
Actual CC	258	301	43	16.7%

* HMT forecast outcome, including ILEA specific grant

<u>Increases on baseline</u>	fbn
RSG	0
SGs	+0.2
NNDR	+0.7
AEF	+0.9