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Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon George Younger TD MP  
Secretary of State  
Scottish Office  
Dover House  
Whitehall  
LONDON  
SW1A 2AU

6 March 1984

*Dear Secretary of State,*

THE SCOTTISH BLOCK

With the Prime Minister's approval I am taking a fresh look, in the interval between annual Surveys, at a number of areas of public expenditure which lend themselves to indepth review. One area where I see a good case for this is the block budgeting regime for Scotland, Wales and Northern Ireland.

This regime has I need not remind you now been operational for about five years, the Scottish block itself being the first to be introduced, in 1978. The attractive simplicity of the block/formula arrangements has saved us all a great deal of time and trouble, and there could be no benefit to anybody in a return to the programme-by-programme horse-trade which preceded them. Nonetheless, given the inexorable pressure we face on all public expenditure programmes, I have felt the time has come to take stock of the public expenditure consequences of this largely automatic system. That can only mean relating expenditure to some assessment of need.

The Treasury has carried out an internal study which attempts to relate expenditure to need for the three territorial blocks. The Prime Minister has seen the results. This is an inherently difficult topic, because no way of measuring need can ever be perfect or free from controversy. There was indeed some dispute over the results of the Needs Assessment Study (NAS) published in 1979, and of its 1980 update, even though the methodology had been broadly agreed by those concerned to be the best that could be devised with the time and resources available. For present purposes, we have seen no alternative but to attempt a further update based on that agreed methodology, in full awareness of its pitfalls and of the necessary limitations of the data available within the Treasury.

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Those qualifications granted, I would make two claims for the NAS approach:

- i. While its detail is arguable, it can be used with some confidence to point up areas where there is an important divergence between expenditure and need - need, for these purposes, being assessed relative to need in England.
- ii. It is a valid indicator of the broad trend, over time, of that relationship between expenditure and need.

The results suggest at first sight that the Scottish block is now running at a level significantly in excess of relative need, and that the gap has widened in the last few years. Absolute precision is not claimed for the figure of £900m, which is the sum total (rounded) of the excesses identified for 1983-84 in those results. But I do believe such a large figure must point to some imbalance in the geographical distribution of public expenditure resources - even when allowance is made for the special needs of Scotland (which, to judge by the indicators, have declined in recent years relative to those of the rest of the country). For some kinds of expenditure this is supported by statistical and anecdotal evidence of rather high relative standards of provision.

How has this situation arisen? Not, the study suggests, through the working of the territorial formula, whose effect tends to be broadly neutral over time, and in any event, very marginal. The excess seems to have grown by around £275m since 1978-79 (as assessed in the earlier study) after inflation is allowed for. Over half of this increase is evidently due to a rise in Scottish expenditure provision relative to England, much of which seems to have been implicit in the forward plans already in existence when the block was established (which looked forward to 1982-83). The rest appears due to reduced relative need in Scotland.

As to the implications, I recognise very clearly the constraints imposed by the political dimension, not least because of major changes that have been taking place in the structure of Scottish industry. I recognise that you might face very great difficulty over any proposal to make large changes to the block expenditure totals already published in the Public Expenditure White Paper. And any fundamental change to the block/formula regime itself would, I am sure, hold as little attraction for the informed public in Scotland as it does for either of us.

But I do believe that, unless we can be shown to have got the problem out of proportion, it has to be tackled. Before coming to any firm view on how to do so, I should like to have a talk with you about it. But what I have in mind is a different approach to the setting of baseline provision for your block for the new final year in each survey round, starting with this year's Survey. The usual procedure is to apply a flat percentage increase to the previous year's provision. Instead I believe we should detach the Scottish block and negotiate each year on the level of the new baseline provision. To make any impact on the problem this would obviously have to be on the understanding that we were looking for an outcome lower than the flat percentage increase would give you. Then the provision would gradually, over time, move more into line with relative need.

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I recognise that you will want to think carefully about this, before embarking on any wide-ranging study. So I am not copying this letter widely, and I am sure the first step should be a meeting between the two of us. But I would hope it might be possible to agree that officials should jointly look into the results of the Treasury study and seek to reach some kind of agreed view on them. I have acknowledged that the results are necessarily based on incomplete information, and it may be that your officials will want to propose corrections. But I think it essential that we aim to make some initial impact on this problem in the 1984 Survey.

I attach to this letter, though I am reluctant to inflict them on you, annexes on the methodology and figures.

I am sending the Prime Minister a copy of this letter.

Yours Sincerely,  
Paul Rees

P PETER REES

(Approved by the Chief  
Secretary and signed  
in his absence)

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