



FROM: CHIEF SECRETARY

DATE: 22 August 1985

10A

PRIME MINISTER

1985 SURVEY : SCOTLAND AND NORTHERN IRELAND (NI)

I have been considering what could be done in the current Survey to tackle over-provision in the Scottish and Northern Ireland blocks.

2. You will recall that I last year identified, on the strength of internal work in the Treasury, over-provision roughly of the order of £900m in the Scottish block, and of £200m in the NI block. (I discounted a further £200m of over-provision in Northern Ireland, attributable to law and order.) The decision reached was that I should pursue only "invisible" savings on the Scottish block: these have so far yielded savings of £5-20m pa, with something similar in prospect this year.

3. Potentially, though, Scotland and NI have an important contribution to make to solving our wider problem on public expenditure. The inequity of Scottish over-provision in particular is attracting growing notice: Keith Joseph drew attention to its consequences for education at the Chequers Cabinet, and there has been critical comment in both Parliament and the press.

4. George Younger has never denied that over-provision exists. You were yourself, I know, struck by the ease with which he found offsets from his block for rates relief this spring; he has now told us that he is ready to do so again in future. This seems to me to undermine his earlier claim that the political and presentational problems of restraining his block totals were insuperable.

5. NI for its part now has the prospect of additional US funds as an "extra" to the deal we are negotiating with the Irish Republic, on top of the over-provision that already exists.

6. In all this we have to bear in mind that over-provision, in both territories, is enshrined in a purely automatic block budgeting system, involving no Treasury scrutiny whatever, which we inherited from the Labour Administration. Even our predecessors never saw it as any more than a stopgap arrangement on the road to political devolution, certainly not as the permanency it has now become. Be that as it may, the block system is now publicly construed, in the territories, as a political entitlement to public expenditure. The longer we let it run, the harder it becomes to challenge that perception, and the greater the risk of political repercussion when we do.

7. In the context of this year's difficult Survey I concluded that I could not disregard the possibility of savings from this quarter. I therefore wrote to George Younger and Douglas Hurd asking for reductions in the Scottish and Northern Irish provision for all years of the Survey. I thought however it might be helpful if I told you, before the bilateral discussions begin in September, how I intend to tackle the problem.

8. I have asked initially for reductions in the three Survey years, of £100m, £150m and £200m for Scotland, and £25m, £50m and £75m for NI. The outcome I am aiming for, which I think has some presentational advantage, is to secure reductions equivalent in effect to suspending the operation of the formula on block programmes (other than local authority current - this is explained in more detail in Annex A). Our best estimate is that this would mean asking for something of the order of £100m a year from the two territories together. The key presentational advantage is that while this would mean denying the Scottish and NI programmes the increases implied by the operation of the formula there would not be cash cuts in the block.

9. Inevitably, George Younger and Douglas Hurd will be concerned about my proposals and are likely to oppose them strongly. I thought I should therefore let you know how I am proceeding before the September bilaterals. I would of course be very ready to discuss if you wish.

10. As background, Annex B sets out some examples you have seen before of high standards of provision in Scotland and NI; and Annex C reminds you of the relatively prosperous state of the Scottish economy.

PRS

for PETER REES

[Approved by the Chief Secretary]

1985 SURVEY : SCOTLAND AND NORTHERN IRELAND

The "fallback" approach to securing savings is to suspend the operation of the comparability formulae for the Scottish and Northern Ireland blocks - though not for Wales, where over-provision is not suspected. An explanation follows.

The block system

2. The arrangements for determining territorial block provision are entirely automatic. They are designed to ensure that block programmes overall move broadly in line with comparable English programmes - although on the basis of an overall allocation of national resources which in general allows the territories a higher per capita level of spending, in recognition of their special needs.

3. Baseline provision is fixed as for the rest of public expenditure, ie provision for the new final year in each Survey is constructed by applying the normal uplift factor to the previous year's provision.

4. Marginal changes to the territorial blocks, up and down, are fixed by a population-based formula, as an automatic consequence of changes to comparable English programmes. For Scotland, the formula is 10/85, and for Wales 5/85; for NI, it is 2.75% of the resulting GB figure.

5. Within the block totals so determined, each territorial Secretary of State has a wide measure of discretion as to how he allocates resources to meet local needs.

Suspending the formulae

6. Thus in a Survey such as 1985 where net additions are expected to comparable English programmes, suspending the formulae has the same effect as applying cuts to territorial block provision. It is proposed to exclude from this process

that half of the blocks which corresponds (in Scotland anyway) to local authority current expenditure.

7. A very rough prediction of what such savings in 1985 might amount to, based on a best guess of the outcome of the Survey for English programmes, is as follows:

	£m		
	<u>1986-87</u>	<u>1987-88</u>	<u>1988-89</u>
Scotland	70	70	90
Northern Ireland	20	20	30

Presentational advantages

8. This approach - suspending the formulae - has modest presentational advantages over the alternative method of cutting baselines. Increases foregone sound better than cuts. And the basis for the extent of the savings achieved can be explained publicly.

EXAMPLES OF HIGH STANDARDS OF PROVISION - SCOTLAND

	<u>Scotland</u>	<u>England</u>
<u>Health:</u>		
NHS spends:	£5 per head	£4 per head
Hospital beds per 1,000 people	11.3	7.5
General practitioners per 1,000 people	6.6	5.3
<u>Education:</u>		
Pupil/teacher ratio	17.3 (excluding Highlands & Islands)	18.5
Teacher training	Surplus capacity	
<u>Roads:</u>		
Schemes with negative NPV	28%	14%
Urban motorways	Glasgow said to have highest per capita mileage in Europe	
<u>Housing:</u>		
Dwellings lacking basic amenities	2.8%	5%
Dwellings statutorily unfit	4.5%	5%
Average weekly rents	£9.84	£14.05

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EXAMPLES OF HIGH STANDARDS OF PROVISION - NORTHERN IRELAND

	<u>NI</u>	<u>England</u>
<u>Health:</u>		
Hospital beds per 1000 people	10.9	7.5
General practitioners per 1000 people	5.7	5.3
Staff in health authorities relative to population	35% above England	
Home helps per 1000 people over 65	19.4 (expenditure having risen by 91% in 5 years)	6.5 (GB)
<u>Housing:</u>		
Age of stock	Half is either less than 10 years old, or has been improved in last 10 years	
Crude surplus of dwellings over households	12.3% (highest in UK)	8.7%
Proportion of house- holds in private rented accommodation (usually worst maintained)	8% (lowest in UK)	12%

SCOTTISH ECONOMY

Blessed by oil, and excessive public expenditure (£2054 per capita on the latest figures; national average, £1706), Scotland's position has over a decade improved markedly relative to the rest of the UK. On GDP per capita it now, at 96% of the national average, ranks behind only the SE and East Anglia of UK economic planning regions; on personal disposable income per capita it scores 95% of the national average, and on average earnings for male manuals 2% above the national average. On seasonally adjusted unemployment it has, at 14.7%, narrowed the gap with the UK average at 13%.

2. There is optimism in the manufacturing sector with end-1984 output up 6% on a year earlier, employment up, and orders (especially for export) increasing. Manufacturing productivity has risen above the trend of the UK as a whole, while pay settlements have kept in line, so competitiveness relative to the rest of the UK is strong. Prospects for electronics (where Scotland has been notably successful in attracting new firms) are said to be bright. There is also an upturn in oil-related work, which now (directly or indirectly) employs about 100,000. The number of new businesses is increasing. Outside manufacturing, there is buoyancy in distribution, particularly retailing, and strong growth in lending by the financial sector, although construction remains depressed.

3. Scotland's industrial structure is no longer a handicap, and now more closely resembles the national average. Its manufacturing sector now accounts for only some 25% of all employment, although Scotland still has an above average share of employment in the declining industries of textiles, clothing, and shipbuilding. Service employment accounts for 63%, but the earlier, unhealthily fast growth in public sector employment has slowed.

COMMUNICATION

