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SUBJECT

CCMASTER

10 DOWNING STREET
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5 October 1987

From the Private Secretary

Dear Jill,

PROSPECTS FOR THE 1987 PUBLIC EXPENDITURE SURVEY

The Prime Minister held a meeting this morning to discuss the prospects for the 1987 Public Expenditure Survey. There were present the Lord President, the Chancellor of the Exchequer, the Chief Secretary and Mr. Richard Wilson (Cabinet Office).

The Chancellor of the Exchequer briefly described the overall picture along the lines set out in the note attached to Alex Allan's letter to me of 2 October. The Prime Minister congratulated the Chief Secretary on his achievements so far in the Public Expenditure Survey. The meeting then discussed in turn major programmes where agreement had not yet been reached.

The Chief Secretary explained the options for defence. One would be to settle a firm figure this year within which the Long Term Costing exercise would take place. Alternatively, an interim settlement could be reached now with a view to taking final decisions next year after the Long Term Costing had been completed. It would however be very difficult to reach agreement on a one stage option. A two stage option seemed more achievable, perhaps with some form of assurance on the financing of pay increases for the armed services. This might be along the lines that the defence programme would absorb first year costs but the Treasury would take later year costs into account in the Public Expenditure Survey. It would be important in that event for MOD to give suitably firm evidence to the AFPRB. However, even with a two stage settlement, the defence programme might well need to go to the Star Chamber: the figure for the first year would need to be tough in order to set a firm framework for the Long Term Costing exercise, and Mr Younger would resist this.

The Prime Minister agreed that the defence programme should be taken to the Star Chamber if necessary. The choice between the options would have to be for the Chief Secretary's judgment. However he should bear in mind the need for the Secretary of State for Defence to achieve a settlement which would give assurance to the armed services. The wasteful procurement policies of the MOD and the slowness with which

action was being taken on R&D showed the scope for better use of resources.

The Chief Secretary explained that education was the most likely candidate for the Star Chamber, though it was possible that Mr. Baker would settle beforehand. The Prime Minister urged the need to be very tough.

The Prime Minister said she had some sympathy with the bids for extra resources for health which had been entered by the Secretary of State for Social Services. All the signs were that a more fundamental examination of the provision of health care would be needed before too long. After discussion it was agreed that the possibility of withdrawing exemption from prescription charges for people between retirement age and the age of 80 should not be pursued, even though other exemptions on the grounds of low income and the like would still apply to them: this was not a proposal which would be readily accepted by Cabinet or by Government supporters in the House. It was further agreed that the choice of health bids to go to the Star Chamber should be considered with great care by the Lord President and the Chief Secretary. The Prime Minister asked to be kept closely in touch.

On the aid programme, the Prime Minister drew attention to a recent report from the European Court of Auditors which had agreed that aid resources were not reaching those for whom the aid was intended. There was no strong case for an increase in the aid programme and indeed the Foreign Secretary could find resources from the diplomatic wing if he wished to make such an increase. Any increase should be resisted.

The Chief Secretary explained that the Secretary of State for Scotland might accept a move from regional development grant to selective regional assistance if he felt that he could then have an easier settlement on Scottish block expenditure. The formula consequentials for Scotland this year were likely to be quite tough so this might well be an acceptable deal. The Secretary of State for Wales might accept the principle of the change but dispute the quantum of selective assistance.

It was agreed that the members of the Star Chamber, should be the Chief Secretary, the Secretary of State for Energy, the Lord Privy Seal, the Minister for Agriculture (if as expected his programme was soon settled) and probably the Secretary of State for Employment. The Chancellor of the Duchy of Lancaster would be an alternative to the Secretary of State for Employment. However, he could not easily be a member if Wales or Scotland were going to the Star Chamber over regional aid. If the Chancellor of the Duchy of Lancaster were not in the end to be a member, the Lord President should explain the reasons to him.

The Chief Secretary explained the position on the remaining major programmes. On electricity, the Prime Minister said that substantial increases in electricity prices would need to be justified by reference to the heavy programme

of investment both in new power stations and in de-sulphurisation equipment, with the environmental benefits that would bring. It would cause difficulties for the Secretary of State for Employment, if, having accepted a tight settlement, others were now seen to fare better.

I am copying this letter to Mike Eland (Lord President's Office), Alex Allan (H. M. Treasury) and Richard Wilson (Cabinet Office).

y
Jms,
David.

D. R. Norgrove

Ms. Jill Rutter,
HM Treasury.