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Secretary of State

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The Rt Hon John Major MP
Chief Secretary
Treasury Chambers
Parliament Street
LONDON
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25 May 1989

Dear John.

PUBLIC EXPENDITURE SURVEY 1989

ATTACHMENT IN FOLIO

In this year's Public Expenditure Survey I aim to build on the developments of the last 12 months, in particular the launch of Employment Training and Training and Enterprise Councils. These initiatives address two of the major problems in today's labour market. First, the need to reduce the pressure on wages by increasing the supply of labour; this is particularly effective if those helped to take jobs would otherwise be receiving state benefits. Second, to increase the volume of employer funded skills training, particularly higher level transferable skills.

I judge that the momentum can be maintained without a significant increase in the baseline of our major programmes. But it is important that we make no further reductions below baseline. Last year's reductions of £300 million in YTS and ET in 1990-91 and £400 million in 1991-92 have still to work through and we should not add to them. Training is becoming an increasingly important political issue and the period in which we set up TECs is not the time to make bigger cuts than we have already agreed to the programmes for which they will have responsibility. I suggest our strategy should be to hold public expenditure broadly constant while using TECs to secure the large increase in training expenditure by employers which we are seeking. It is also vitally important that, through the stricter benefit regime, we keep up the pressure to minimise the unemployment count, especially given the risk that a slowdown in economic activity may cause the count to rise slightly. My objectives are at annex 1 and are reflected in the structure of my detailed bids at annex 2.



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As part of the Inner Cities Initiative I announced two pilot schemes, the Job Interview Guarantee Scheme and the Inner City Development Fund, which offer incentives to the long-term unemployed and other disadvantaged groups. I believe the pilots will form the successful basis for a programme which will encourage long term unemployed inner city residents to establish a bigger stake in their local economy. Therefore I am bidding £12 million, £22 million and £22 million for the programme to be implemented in full.

Many disabled people need help to keep and find work. Technological developments now offer cost-effective ways of helping a wider range of people with disabilities to find work. At the same time there are more people with health problems and disabilities in the community. We have the opportunity offered by the tightening labour market to get more of these people into jobs. I anticipate additional gross expenditure of £21 million, £28 million and £37 million to provide equipment and adaptation for the disabled in mainstream employment, sheltered placements and to restructure Remploy.

Turning to my second theme, encouraging employer funded training, only one of my initiatives requires new money. The others will be met from ET and YTS and EAS. These and other bids also to be met from existing resources are at annex 2. However, Business Growth Training is an important development. At this early stage I am not seeking a general increase to what is a fairly modest baseline, but I have identified the need for special support to enable TECs to establish Local Training Advisory Centres which would have an important role to play alongside the BGT initiative. TECs would contract with agents to set up and run the centres, which would provide professional advice and assistance, particularly to smaller firms, about new training developments, practical demonstrations of new training technology and information about training provision. I anticipate I will need an extra £8 million, £12 million and £13 million.

I have been very encouraged by the results being achieved in the first Compacts I established. Evidence from the first 30 Compacts shows the value of pump priming to fund development work and initial operations. I am bidding for additional funds of £6 million in each PES year to establish partnership activities in all TEC areas by the end of the PES period. This will provide greater business involvement in schools and better coherence between education, training and work.

I have several proposals involving capital expenditure. In particular, rationalisation of the ES local office network and Information Technology for both the ES and TA. Business cases are well advanced for these projects. My bid for additional non running cost expenditure in total, mainly capital, is £40 million, £49 million and £28 million. The full analysis is at annex 3.



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Last year we negotiated a three year agreement on running costs. Even though its assumptions on pay and prices have proved overly optimistic given, particularly, the nature of the long-term pay agreements made by the Treasury and the large increase in rents and other charges coming through from PSA, I intend to stand by that agreement. However, it will prove particularly difficult to maintain those of my programmes for the unemployed run directly by the Employment Service, because these costs are included in the running cost limit.

There are three items outside the agreement. First, the extra up-front running costs associated with relocation, on which there has been a separate submission at official level. Delay in starting the relocation programme engendered by the delay in getting approval for the additional running costs and for improvements in the package of relocation terms, also under discussion with Treasury at official level, now leads me to rephrase those running cost requirements slightly. I also take the opportunity to add in some additional, relatively small running cost requirements recently identified and quantified, the most notable of which is a bid in respect of HSE, who have now come forward with a proposal to relocate some more staff to Bootle. My bid for additional running costs for relocation as a whole is £8 million, £5 million and £3 million. Second, we have asked that the TEC management fee should be treated as programme expenditure, in the same way as we have been doing for fees to Managing Agents of our training programmes - and indeed as we do generally for payments to grant aided bodies which cover, inter alia, their administrative expenses. I have written separately on this as an early decision is needed so we can plan expenditure across the Group for next year. Third, I would like the administration by HSE of the Food and Environment Protection Act to move on to net running cost control from 1 April 1990. This would require a technical adjustment to the gross provision. Also from 1 April 1990 the Nuclear Installations Inspectorate net running cost ring fence should be extended to cover Nuclear Safety Research work transferred from the Department of Energy. I would be grateful for confirmation that you are content for discussions to proceed on this basis.

I now turn to the running cost bid I am making for 1992-93. My decision not to reopen the running cost agreement for the first two new PES years will mean not only that the ED Group will have to achieve efficiency gains of more than the 1.5 per cent a year stipulated in the Management Plans but also that some work will be stopped or deferred. Projects requiring expenditure now to save money later must be postponed, in particular work on the Employment Service's Information Technology strategy. I propose to spend £26 million in 1992-93 to go some way to redressing earlier delays. Also by 1992-93 known large increases in accommodation costs will have fully worked through. First, the



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addition of about £10 million VAT to rents, which has been imposed on us. Second, the steep rise in commercial rents as leases come up for renewal. Third, some routine maintenance due over the first two PES years may have to be postponed. I anticipate accommodation costs in 1992-93 in total will be £31 million above baseline. Similarly, we may have to delay training and other human resource development work throughout the Group, with consequent additional commitment in later years.

The HSE require £4 million in 1992-93, largely for new work generated by the harmonisation of European Health and Safety regulations and in response to increased public concern about workplace hazards. As mentioned above, I have not included a bid in relation to pesticides work (FEPA) - which would otherwise have required an additional £0.7 million in that year - which I am assuming will have moved on to a net running cost basis by the beginning of the PES period.

Finally I need some cover for the recent pay settlements entered into by Treasury. I intend to absorb the 1989-90 settlement but larger increases are already in the pipeline and there is a limit as to how long I can go on absorbing them without endangering the core activity of the Group. I have assumed pay increases of the order of 5.5 per cent in 1992-93, and I will need at least an extra £58 million for pay in that year. The several items discussed above produce an additional requirement in 1992-93 totalling £119 million. There will of course be any number of additional small requirements for new activities but I would propose to absorb them by a continuation of increased efficiencies beyond those identified in Management Plans and reduced activities elsewhere. One major saving I can, however, now identify and offer up as an offsetting saving. The privatisation of the Skills Training Agency should release £24 million running cost provision in that year. My retention of the likely running costs savings from the STA baseline provision in Years 1 and 2, as I am entitled to do under the fixed three year settlement, provides at least a partial offset in those years for the increased costs, thus making my task in standing by the agreement that much more manageable. In total, therefore, my requirement for gross running costs in 1992-93 is £95 million above the baseline, as revalued by 2.5 per cent. The details are at annex 4.

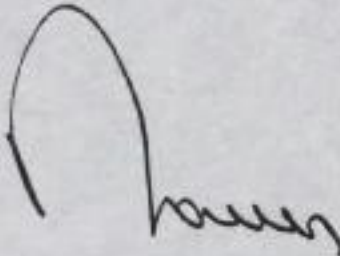
In addition to the above items I am seeking extra cover of £4 million, £4 million, and £6 million for the Redundancy Fund. This need arises because in PES 88 we overestimated the reduction in requirement as the economy improved.

Finally, I attach at annex 5 details of output and performance indicators to support my baseline and bids for programme expenditure. My Management Plans are being reassessed, to take account of my decision to stand by the three year running cost agreement. Your officials are aware of the position and the new deadlines agreed.



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I am copying this letter to the Prime Minister and also the Secretary of State for Wales and the Secretary of State for Scotland with whom I intend to meet shortly on this.

Yours, ever


NORMAN FOWLER