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E(81) 16th Meeting

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CABINET
MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

MINUTES of a Meeting held at
10 Downing Street on
WEDNESDAY 13 MAY 1981 at 3.00 pm

PRESENT

The Rt Hon Margaret Thatcher MP
Prime Minister

The Rt Hon William Whitelaw MP
Secretary of State for the
Home Department
(Item 1)

The Rt Hon Lord Carrington
Secretary of State for Foreign
and Commonwealth Affairs
(Item 1)

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
(Item 1)

The Rt Hon Sir Keith Joseph MP
Secretary of State for Industry

The Rt Hon Lord Soames
Lord President of the Council

The Rt Hon James Prior MP
Secretary of State for Employment

The Rt Hon Peter Walker MP
Minister of Agriculture,
Fisheries and Food

The Rt Hon Michael Heseltine MP
Secretary of State for the
Environment

The Rt Hon John Biffen MP
Secretary of State for Trade

The Rt Hon David Howell MP
Secretary of State for Energy

The Rt Hon Leon Brittan QC MP
Chief Secretary, Treasury

THE FOLLOWING WERE ALSO PRESENT

The Rt Hon George Younger MP
Secretary of State for Scotland

The Rt Hon Nicholas Edwards MP
Secretary of State for Wales

The Rt Hon Mark Carlisle QC MP
Secretary of State for Education
and Science
(Item 2)

The Rt Hon Norman Fowler MP
Secretary of State for Transport
(Item 2)

The Rt Hon Tom King MP
Minister of State, Department of the
Environment (Minister for Local
Government and Environmental Services)
(Item 2)

Sir George Young MP
Parliamentary Under-Secretary of
State, Department of Health and
Social Security
(Item 2)

Mr J R Ibbs
Central Policy Review Staff

SECRETARIAT

Sir Robert Armstrong
Mr P Le Cheminant
Mr D J L Moore

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1. NATIONAL COAL BOARD FINANCES 1981-82

The Committee considered memoranda by the Secretary of State for Energy (E(81) 57) and by the Chief Secretary, Treasury, (E(81) 58) on the finances of the National Coal Board in 1981-82.

Their discussion and conclusions reached are recorded separately.

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2. LOCAL GOVERNMENT EXPENDITURE

The Committee considered memoranda by the Secretary of State for the Environment on local government expenditure in England in 1981-82 (E(81) 52), the future of the rating system (E(81) 53), and the proposed Accounts Commission for local government (E(81) 54); and a memorandum by the Secretary of State for Wales (E(81) 56) on local government expenditure in Wales in 1981-82.

THE SECRETARY OF STATE FOR THE ENVIRONMENT said that in January 1981 he had issued to each English authority specific volume targets for 1981-82 of 5.6 per cent below their 1978-79 levels. The authorities' April returns showed that in total they were planning to overspend by £1,350 million in 1981-82; with allowance for shortfall, this excess might be reduced to £950 million. It had been announced in the Public Expenditure White Paper that the Government expected local authority current expenditure in Great Britain to fall by a further 1 per cent in 1982-83 and $\frac{1}{2}$ -1 per cent in 1983-84. Unless the Government were to abandon its public expenditure targets for local authority current expenditure, it was now necessary to take action to deal with the prospective excess in 1981-82. He recommended that he should announce on 2 June, in Parliament and at the Consultative Council on Local Government Finance, that the English local authorities should each submit revised budgets to him by mid-July and warn that, if necessary, he was willing to hold back up to £900 million grant in 1981-82. Grant would not be withheld from any authority which kept

its budget within the target set, but would be withheld on a sliding scale, related to the amount of planned overspend, from other authorities. Decisions on the detailed application of this policy could be taken by the Committee in July in the light of the revised budgets. He judged that to threaten to hold back any lesser amount of grant, say £500 million, would be ineffective. He recognised that this action could lead to substantial rate increases, and that the Government would be blamed for this. It was, therefore, necessary to announce at the same time the Government's intention to introduce medium-term measures for improving the rating system and increasing the discipline on the local authorities, as he had proposed in E(81) 53 and 54, and by announcing a longer term study into the alternatives to the rates.

In a preliminary discussion of these proposals the following were the main points made -

a. While it would be necessary to take some corrective action, the Committee would need to consider very carefully the impact both on services, particularly education, and on the rates, of withholding as much as £900 million of grants. Labour-controlled local authorities would make the most of the opportunity to blame the Government for supplementary rates, some of which they would have levied anyway. Sixty per cent of the burden would fall on the non-domestic rate payer and could add to unemployment; the options put forward by the Secretary of State for the Environment in E(81) 53 for reducing the burden on the non-domestic rate payer would need careful consideration.

b. The proposed system of penalties was unfair. All but two of the shire counties, for example, were above their volume targets, but 17 of them were spending below their Grant Related Expenditures. Further consideration should be given to exempting such authorities from penalties. Since the Inner London Education Authority (ILEA) had virtually no more grant to lose, the effect of not withholding grant generally would be to transfer the penalty

for ILEA's overspending to the shire counties. Expenditure in 1978-79 had been chosen as a basis for the volume targets since that was a year in which many authorities, irrespective of political control, had spent heavily, but the basis was to some extent arbitrary and had the effect of penalising some shire counties with a good record of making expenditure savings.

THE PRIME MINISTER, summing up the discussion, said that the Committee had not had time to discuss in substance the major and complicated issues in the memoranda before them. They would resume their discussion in two meetings which would be arranged in the week beginning 18 May.

The Committee -

Agreed to resume discussion of Local Government Expenditure at further meetings on Tuesday 19 May and Thursday 21 May.

Cabinet Office

15 May 1981

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CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

LIMITED CIRCULATION ANNEX

E(81) 16th Meeting Minutes, Item 1
WEDNESDAY 13 MAY 1981 at 3.00 pm

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1. NATIONAL COAL BOARD FINANCES 1981-82

The Committee considered memoranda by the Secretary of State for Energy (E(81) 57) and by the Chief Secretary, Treasury (E(81) 58) on the finances of the National Coal Board (NCB) in 1981-82.

THE SECRETARY OF STATE FOR ENERGY said that the NCB's External Financing Limit (EFL) for 1981-82 was £886 million. This was inadequate, mainly because of the increasing costs of financing stocks while production continued to exceed sales and because of the need to meet the commitments made in February in the tripartite discussions between the Government, the NCB and the National Union of Mineworkers (NUM). The cost of these commitments, and in particular the withdrawal of the accelerated closure programme and the measures to reduce imports, had been publicly stated by the NCB, with the Government's knowledge, at £100-200 million in the current year. The Board now proposed a revised EFL of £1,406 million and capital investment of £924 million; that is, the same investment in real terms as in 1980-81. In considering these proposals, it was necessary to balance the need to fulfil the undertakings given in the tripartite discussions and to avoid confrontation with the NUM against the need to avoid making further costly concessions. He recommended that the Board should now be set a revised EFL of £1,200 million, with capital investment approval for £825 million. These figures were substantially below those recommended by the Board and thus already entailed an element of risk. In his judgement, any lower figures would carry too great a risk of provoking industrial action by the NUM. The reduction in the Board's bid for capital investment could be defended on the

grounds that £825 million was a small increase in money terms over their expenditure of £805 million in 1980-81. The EFL could be kept down to £1,200 million if there were a lower assumption for wages than the 13 per cent assumed by the Board, and some reductions in production at existing mines to enable a reduction in the rate of stock-building. He further recommended that there should be legislation to provide for a new single revenue support grant to be paid before profit and loss were struck in the Board's accounts. This new grant should be at a level to enable the Board to achieve break-even by extra effort. On present estimates this pointed to a level of £450-500 million in 1981-82 in addition to social grants of £100 million; these grants would be found from within the EFL. He further recommended that full use should be made of existing powers for making deferred interest loans to the NCB. These measures were designed to deal with the Board's immediate and short-term problems, and he would bring forward further proposals later in the year for the size and shape of the industry in the longer term.

THE CHIEF SECRETARY, TREASURY, said that he recommended an EFL of £1,100 million. The increase of £214 million over the present provision would be a charge on the Contingency Reserve and would be in line with the top of the range of £100-200 million which the NCB had publicly given as their estimate of the costs of meeting the undertakings given at the tripartite discussions. It would be for the NCB to decide how to keep within this EFL, but the reduction might come from capital investment, increases in export sales, higher reductions in production at the continuing pits, and improvements in efficiency and cost savings. Provision for capital expenditure should be kept at £765 million which was the level of the existing approval for 1980-81 representing 85 per cent of the total envisaged a year ago. To maintain investment at this level represented a substantial concession, since there was no justification in investing in new capacity when production of coal was expected to out-run demand up to 1990 and when the industry was unwilling to accept closures of old high cost capacity. He agreed that there should be a single new grant to replace specific operating and deficit grants, provided that this was paid after the Board had struck profit and loss in their accounts otherwise the reality of the Board's heavy losses would be obscured and a false impression given of the state of their finances. Subject to further examination of the details, he agreed with the proposal for deferment of repayments

of loan principal as well as of interest, provided that the Board's EFL were reduced to take account of the payments of interest deferred; otherwise there would in effect be an increase in their EFL and in public expenditure.

In discussion the following were the main points made -

- a. In looking at the size of the EFL of £1,100 million, care should be taken to avoid unrealistic assumptions for pay in order to make apparent room for increased investment; that could lead to further pressures to increase the EFL later in the year, when the pay settlement was made.
- b. The NUM attached importance to increasing capital investment in mining in order to preserve and create jobs. A cut would be provocative, and could encourage militancy in areas which at present stood to benefit from new investment. The considered view of the Board was that investment should be of £924 million; they were unlikely to support proposals for anything less, and they would argue that this would reduce the possibilities for reinstating the closure programme and for securing a satisfactory pay settlement. The outcome of seeking to cut investment too far below that figure could thus be further confrontation with the NUM and higher costs than if the proposals put forward by the Secretary of State for Energy were to be accepted.
- c. An EFL which was pitched to minimise the possibility of confrontation would be too costly; and, if it were to be readily accepted by the industry, there would be less opportunity to increase public understanding of the financial situation of the NCB and of the need to act on it. The right course was for the Government to deploy its case in discussion with the NCB and to negotiate an EFL which was reasonable and defensible but not so low as to lead inevitably to major and costly confrontation. This pointed to opening the discussions somewhere below the £1,100 million proposed by the Chief Secretary, Treasury, but with freedom to move to that figure if necessary. An EFL of £1,100 million could be represented as a substantial concession to the industry, by comparison with the present figure of £886 million, and consistent with the undertakings

given at the tripartite discussions. The fact that investment was lower than had been envisaged before the tripartite discussions could be justified on the grounds that the closure programme had been withdrawn. Credit could be taken for the very generous redundancy terms now offered which had led to a trebling of the previous rate of voluntary redundancies.

d. There was in principle a good case for running down high stocks by encouraging more exports of coal. When opportunities had been presented to them, however, the NCB had been slow to respond and had failed to quote competitively. The disadvantage of letting them drop their prices with the objective of clearing stocks was that this would effectively lead to subsidies of electricity used by the overseas competitors to British industries.

THE PRIME MINISTER, summing up the discussion, said that the Committee agreed that the NCB's EFL for 1981-82 should not exceed £1,100 million, and that, although he had authority to move up to that figure, the Secretary of State for Energy should open his negotiations with the NCB by putting the argument for a lower figure. It would be for the NCB to decide what were their priorities in limiting their financing requirement to £1,100 million, or less; but it was important that they should not seek to make room for additional investment by making unrealistic pay assumptions which could then lead to demands for a further increase in their EFL following the miners' November pay settlement. The Committee were generally sympathetic to the arguments against increasing the capital investment approval beyond the present £765 million, but the Secretary of State for Energy should reach agreement with the Chief Secretary to the Treasury, on the precise figure to be approved. The Committee agreed that there should be a single new grant, to replace the present specific operating and deficit grants, and that this should be paid after the Board had struck their profit and loss account. They further agreed that any payments of interest deferred should count against the Board's EFL which should be reduced accordingly. The Committee took note that the Secretary of State for Energy judged that there was a significant risk that these proposals could lead to a costly confrontation with the NUM and that he accepted them very reluctantly. If necessary, and in the light of developments in his further negotiations, he should report further to the Committee.

The Committee -

1. Agreed that the National Coal Board's External Financing Limit for 1981-82 should be revised to no more than £1,100 million.
2. Invited the Secretary of State for Energy -
 - i. To be guided by the Prime Minister's summing up of their discussion in his further negotiations with the National Coal Board.
 - ii. To agree with the Chief Secretary, Treasury, what should be the approved level of capital investment in 1981-82.
3. Agreed that there should be a single new grant, to replace specific operating and deficit grants, and that this should be paid after striking profit and loss in the Board's accounts.
4. Agreed that the Board should be allowed deferred interest loans but that payments of interest deferred should count against their External Financing Limit which would be reduced accordingly.

Cabinet Office

15 May 1981