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E(81) 17th Meeting

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CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

MINUTES of a Meeting held at
10 Downing Street on
TUESDAY 19 MAY 1981 at 11.00 am

PRESENT

The Rt Hon Margaret Thatcher MP
Prime Minister

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer

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 Patrick Jenkin
Secretary of State for
Social Services

The Rt Hon Mark Carlisle MP
Secretary of State for
Education and Science

The Rt Hon Norman Fowler MP
Secretary of State for Transport

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

Mr Patrick Mayhew QC MP
Minister of State
Home Office

Mr J R Ibbs
Central Policy Review Staff

SECRETARIAT

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

SUBJECT

LOCAL GOVERNMENT EXPENDITURE

CONFIDENTIAL

LOCAL GOVERNMENT EXPENDITURE

Previous Reference: E(81) 16th Meeting, Item 2

The Committee considered memoranda by the Secretary of State for the Environment on local government expenditure in England in 1981-82 (E(81) 52) on the future rating system (E(81) 53) and on proposals for an Accounts Commission for local government (E(81) 54), and a memorandum by the Chief Secretary, Treasury, (E(81) 59) on the Accounts Commission.

THE SECRETARY OF STATE FOR THE ENVIRONMENT said that the English local authorities had submitted budgets for their current expenditure in 1981-82 which showed that they were planning to exceed their volume targets by 5.8 per cent, or £1,350 million in cash terms; with allowance for short-fall, this excess might be reduced to £950 million. To deal with this, he recommended that he should announce in the week beginning 1 June, in Parliament and at the Consultative Council on Local Government Finance, that the authorities should each submit revised budgets to him by mid-July, and that he should warn them 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 its target, and he would make clear that the decisions on the amount of grant to be withheld from each authority would depend on a judgment of how reasonable was their response in presenting their revised budgets. It followed that, while he would threaten to withhold up to £900 million, the decision on how much of that total would be withheld, and on what basis, would not be taken until July when he would make specific proposals to the Committee. To threaten to withhold anything substantially less than £900 million would be ineffective: local authorities could avoid making any reductions in the volume of their spending by financing some of the excess from their balances and by making supplementary rate increases. The action which he proposed would be criticised as leading to yet further rate increases, and local authorities would seize the opportunity to lay the blame on the Government for such increases, including those which some of them were intending to make anyway. It should therefore be presented in the context of medium term measures for improving the rating system and increasing the discipline on the local authorities, such as he had proposed

in E(81) 53 and 54, and accompanied by an announcement of a longer term study into the alternatives to the rates. Of the medium term measures which he recommended should now be studied urgently, the most important were the proposed limit on the level of non-domestic rates for authorities spending over a specified threshold level; the establishment of an Accounts Commission to take executive responsibility for the audit of local authorities; and provision that expenditure above a certain level could not be financed by the main rate at the beginning of the year but by the levying of additional supplementary rates through the second half of the year for each additional tranche of expenditure above the approved level. The aim of the last of these measures was to maximise public pressure for economies to be made, and rate increases avoided, and this approach would be reinforced if supplementary rates were made subject to approval by local referendum or by requiring the council concerned to seek immediate re-election. If these medium term measures were to be implemented in the financial year 1983-84, it would be necessary to provide for them in new legislation to be introduced in the autumn of 1981. Longer term measures to replace the rating system by alternative local taxes would require further study, leading perhaps to legislation in the 1982-85 Session with a view to implementation in the next Parliament. There were no other options which the Government could take. The choice was either to abandon control of local authority expenditure, and to accept the consequences of this for the Government's public expenditure objectives, or to take action which could lead to rate increases, for which the Government would be blamed, and to introduce controversial legislation to reform the rating system by imposing constraints on the present powers of the local authorities.

In discussion the following were the main points made -

a. Some Ministers argued that the proposed level of grant to be withheld was too high. It would lead to a combination of cuts in services and increases in rates for which the Government would be blamed, particularly in the local press. The percentage prospectively overspend shown by the authorities' April budgets was very similar to that identified a year ago in their budgets for 1980-81. Subject

to confirmation when the outturn figures were available, it seemed that the decision to withhold grant of £200 million from the English and Welsh authorities in 1980-81 had been instrumental in bringing down the excess for that year to about 1½ per cent. This pointed to holding back grant in the order of £200-300 million for 1981-82. Others thought that to threaten to hold back as little as this would be ineffective in securing volume reductions, for the reasons put forward by the Secretary of State for the Environment; and, to the extent that authorities responded by reducing their budgets towards their target levels the amount of grant withheld in practice would be less than £900 million.

b. The proposed method of grant hold-back would be criticised as unfair and the Government would lose the support of those authorities which were making every effort to control their expenditure. Setting the target reduction in the volume of expenditure in 1981-82 in terms of expenditure in 1978-79 was arbitrary, and could penalise those authorities which had successfully controlled their expenditure in 1978-79 at the expense of those which had been profligate. Some authorities, and notably the Shire Counties, were overspending in relation to their volume targets but underspending in relation to their Grant Related Expenditures (GRE) which were intended to represent an independent assessment of their needs. Both the volume and the GRE bench-marks were open to criticism on the grounds that they did not take sufficient account of recent movements in population and consequent changes in demands for services. Unless special measures were taken, the Shire Counties would have to carry the burden of the £200 million overspending by the Inner London Education Authority (ILEA) which now had virtually no more grant to lose. The system should be such as to avoid penalising the local authorities for the level of expenditure by the Metropolitan Police whose budget was approved by the Home Secretary.

c. Provided that there were no legal impediments, it would be open to the Committee to consider in July, in the light of the revised budgets, whether exemptions might be made in whole or in part for local authorities which were spending below their GREs. There

should, however, be no reference to this possibility in the Secretary of State for the Environment's statement in June; otherwise those local authorities which were spending below their GREs, but above their volume target, would have no incentive to take action on the latter. While it would be right to take account of performance measured against GREs in considering the amount of grant to be withheld, GREs should not become the primary target; that would be to give those authorities now spending below their GRE an incentive to spend up to it.

d. Action in 1981-82 should be set in the context of an announcement that measures would be taken to reform the rating system in the medium term and, subject to further studies and consultations, to replace it in the longer term. Of the medium term measures proposed by the Secretary of State for the Environment, there was support in particular for the idea of linking increases in expenditure over a certain level with supplementary rate increases; it would be important to design such a system so as to prevent local authorities covering themselves by high initial rate increases. Further consideration should be given to whether such supplementary rate increases should be subject to referendum, either of the local electorate as a whole or of rate payers only, or re-election. There was a case for placing an overall limit on the amounts which an authority could raise by rates and by borrowing in a year; it would however be difficult for Government to enforce such limits on an authority which chose to overspend and then confronted the Government with the choice of either raising its financing and rating limits or bringing its services to a halt.

e. There was general support for the proposed Accounts Commission although it would take some time for the private sector accountants which it would engage to familiarise themselves with local authority systems and make effective proposals for savings. In practice the most promising route to savings was not through improvements in auditing but through management consultancy exercises, and the title and terms of reference of the new organisation should reflect this.

f. The Committee would need to give further consideration to the longer term proposals for replacing the rating system by alternative local taxes. If such solutions were adopted it would still be necessary to impose limits on the powers of a local authority to raise money from its electorate.

THE PRIME MINISTER, summing up the discussion, said that the Secretary of State for the Environment should now circulate a further memorandum summarising his proposals and taking account of the points made in the Committee's discussion. In particular he should cover the question of the amount of grant which might be withheld; the points which had been raised on the ILEA and the Metropolitan police; the form of the referendum which might in future accompany supplementary rate increases; the amendment of the title of the proposed Accounts Commission to take account of its role in covering both the management systems and the accounts of the local authorities; and the timing and coverage of his statements to Parliament, and to the Consultative Council on Local Government Finance, in the week beginning 1 June.

The Committee -

1. Invited the Secretary of State for the Environment to circulate a memorandum, for discussion at their meeting on 21 May, summarising his proposals for local government expenditure and financing in England and taking account of the points made in their discussion.
2. Agreed to discuss, at their meeting on 21 May, the proposals for dealing with expenditure by the Scottish and Welsh local authorities in 1980-81 and 1981-82 set out in the memoranda by the Secretary of State for Scotland (E(81) 55) and by the Secretary of State for Wales (E(81) 56).

Cabinet Office

19 May 1981