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CABINET  
MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

LOCAL GOVERNMENT FINANCE BILL : INTERIM RATING LEGISLATION  
Memorandum by the Secretary of State for the Environment

1. We discussed at E Committee on 2 November (E(81) 31st, item 1) the points raised in my minute of 29 October to the Prime Minister. I was asked to produce a note on some of the issues involved.

Background

2. Colleagues will recall that after two discussions on referendum and elections (E(81) 27th, item 1) and (E(81) 29th, item) the view prevailed that we should go for referendum as the trigger mechanism.

3. During the course of drafting my officials raised with Counsel the question as to what the central government would do if a local authority, having lost the referendum, wished to obstruct the government's policies. Counsel advised that in such a situation, without specific powers over rents, fares, etc I would be powerless to require an authority to take specific action. An authority might decide to achieve the overall limits by actions designed to create maximum resistance by damaging services perversly in order to seek the maximum opprobrium for the central government. They might, for example, raise rents unduly or close old persons' homes. I was immensely reluctant to include on the face of the Bill specific powers of direction which would arouse memories of Clay Cross and give an emotional flavour to the debate. But in view of Counsel's advice, I took the view it was necessary to take the powers in spite of these objections and wrote accordingly to colleagues. If colleagues decide, as I did, that it is wise to have these powers - subject to the points mentioned below raised by individual colleagues - a Bill is ready for introduction forthwith containing them, and has been circulated to members of L Committee under cover of my paper L(81)193. In the normal way a reprint of this Bill is now being carried out to take account of drafting amendments. I have taken advantage of this reprinting to request that an alternative version of the Bill, which excludes the powers of direction should colleagues prefer to proceed in this direction, is also available. I have been told that both versions will be available on Thursday morning, 5 November, I have requested that this should be by the time we meet in E Committee.

Particular issues on directions

4. There are some particular issues on the direction powers which were raised at E Committee on 2 November and my officials have spoken to Departments immediately concerned and my officials have been there were further points. I have now established that there are 3 issues relating to directions:

- i. can Wales make directions differently from England? The answer is yes. Directions would be individually tailored, any authority which was to be the subject of them;
- ii. the Secretary of State for Transport was concerned that the Bill should enable him to give directions in respect of passenger transport executives and the London Transport Executive. The Bill contains such a provision and instructions have been given by the Secretary of State for Transport to strengthen this. An amendment can be taken in committee;
- iii. are police authorities, magistrates committees, etc covered by the direction powers? The Home Secretary is considering whether it would be appropriate for the direction-making powers to cover these bodies, and, if so, whether the Bill is adequately drafted to do so. This decision is one entirely for the Home Secretary and his decision, whatever it is, can be incorporated, if necessary, into the Bill in Committee.

What happens if an authority refuses to obey the directions or reduce its expenditure?

5. Colleagues will remember that I proposed two options in the belief that they would act as a deterrent to the limited number of authorities caught by the interim measures. My proposal was that we set a realistic target for high spending authorities whereby, for example, if they cut their expenditure by say 7% they would escape our interim provisions. The target has to be set so that it is achievable and, balanced against the risk of either a referendum or an election, much preferable.

6. In my view, very few authorities faced with such an alternative would go for an election: But if they did, and won, we have avoided any risk of confrontation; whilst, if they lose, we would have a more sympathetic controlling party. Thus we are spared the great practical difficulties that arise if a hostile controlling group lose a referendum but remain in control, with the obvious potential in frustrating our policies.

7. There is thus no certain answer to the question as to how we deal with an authority that refuses to obey the direction. I would have to assume that local authorities will comply with central government policy; there are no powers in Scotland to send in commissioners to individual authorities but they were advised by their own officials that they were at risk of surcharge if they refused to reduce expenditure. My understanding is that Scottish office officials have reservations about the advice but in England, the Attorney has advised that the risk of surcharge would be valid). Confrontation is, however, equally

possible in either country. But when we took decisions to use referendum we knew that some authorities would go to the limits actively to frustrate the central government. In the end, we rely on the threat of surcharge. It is a very potent threat but we cannot guarantee its effectiveness in every hypothetical situation.

Political situation

8. The Bill has aroused intense interest since its provisions were approved by this committee (E(81) 27th) and included in the legislative programme by Cabinet on 24 September (C(81)32 items). Two major concerns have developed:-

- i. dislike of the referendum. This is an issue which has implications outside my own Department. Although we may indicate that polls are not without precedent in local government for some of our supporters they are a constitutional aberration. I hope that, particularly when the facts set out at (ii) below are known; selective intervention will be seen as a better alternative than the earlier system when all authorities were punished for the faults of the few. Concern then should be muted. Two further arguments exist. First, the publication shortly of our Green Paper on Alternatives to Domestic Rates will give encouragement to the interim nature of our proposals; secondly, if colleagues decided, we would accept an inevitable amendment in Parliament to limit the period within which these powers are available, to a specific number of years unless renewed by order.

- ii. many of our supporters have figures to support the assertion that many perceived low spending councils could be forced into a referendum against their will. Those colleagues who have followed our PESC discussions will appreciate how the published figures in the White Paper have been used by the local authority associations to encourage this view. Equally, colleagues who have followed the discussions in MISC 21 and MISC 62 will know that these anxieties may fall away. The earlier we can resolve the public expenditure issues now before us the sooner I can allay these anxieties.

The decision before us

9. In the light of these considerations we can either:-

- i. proceed with either of the 2 Bills before us - depending upon the decision we take about the powers of direction - forthwith. This gives us our best chance of getting a Bill enacted before the beginning of the next financial year;
- ii. amend the Bill significantly to remove the referendum provisions and substitute for them either elections, as I originally proposed, or a procedure of direct intervention as described in the Annex;
- iii. proceed only with the audit commission and block grant provisions in the Bill which are essential relying entirely on the block grant mechanisms and holdback to influence individual authorities spending decisions.

I think (iii) is unacceptable in view of the public statements we have made. (ii) either option here would delay the bill by two weeks in the view of the Parliamentary draftsman, and one of the raises the question as to whether a system of direct intervention could be introduced in England. I am grateful to the Secretary of State for Scotland for making available his officials to discuss the Scottish system with me. The Annex outlines the Scottish system and a possible variant of one aspect of it (substitution of a parliamentary order for the referendum). I give the reasons for rejecting the Scottish solution in the Annex itself.

10. Nor do I think the scheme of direct intervention set out in the Annex would be desirable. The constitutional hostility would be just as deep, if not more so, at so obvious a central government control. In practical terms the mechanisms would demand that we will increasingly be forced behind the formula-based targets we now use and more into a total scrutiny of individual services.

11. More authorities are bound to be involved. The deterrent element of election or referendum is removed. Indeed, some authorities might relish such a controversial relationship with central government, particularly if the choice is voluntary economies. I strongly believe that going for elections would be the best option but the delay in amending the Bill to provide for them would aggravate the task of the business managers in obtaining the enactment of the Bill for operation in 1982/83. If, however, the business managers considered that substituting election for referendum would ease the passage of the Bill through Parliament, lead to an early enactment of it, I would opt for this course. If they do not think so, however, I consider we should stick to (i) and introduce the version of the Bill that includes powers of direction.

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The Scottish System

The system in Scotland relies on the setting of non-statutory expenditure guidelines based largely on the volume of current expenditure - excluding consideration of rent levels and loan charges. It involves the use of a crude needs element formula which is set as to around 80% on a per capita basis, the remaining 20% being mainly decided on factors relating to the old, the young, density and sparsity of population. No detailed service by service calculation is involved. This is possible because the Secretary of State for Scotland is responsible for all local government services and has, since the reorganisation of local government in Scotland, given the expenditure guidelines to all his authorities. These guidelines, which are indicative not mandatory, represent the total of relevant expenditure which is divided up amongst authorities.

The selection of authorities who are considered to be planning excessive expenditure and therefore to be subject to the exercise of the Secretary of State's powers to withdraw grant (or, as now proposed, to require a reduction of rates) is affected in the first place by eliminating those which are within or nearer to guidelines; account is thereafter taken of population trends, the trend of expenditure over recent years measured against the guidelines, increases in the volume of expenditure and increases over recent years in rates. This can produce some apparent anomalies if used solely by reference to guidelines. For example, 2 Islands authorities who were well above the guidelines in percentage terms were not pursued on the basis of the "in house" criteria listed above. Indeed a large proportion of the authorities in Scotland also failed to meet the guideline criteria.

Where the Secretary of State wishes to take action against an authority he is required to place before the House a report subject to affirmative resolution in respect of each individual authority. He is required to give any authority against which he proposes to make a report time to make representations which, if he proceeds, are included in the report.

#### Could the Scottish system apply in England?

It will be clear to colleagues that the situation in England does not lend itself to such a system. First the block grant system based on GREs covering total expenditure of services for which different Secretaries of State have responsibility does not easily lend itself to a system of expenditure guidelines which take no account of individual services. Secondly, the use of "in house" criteria to evaluate the budgets of local authorities and to decide who should be subject to the measures would be totally unacceptable to local authorities in England who would be likely to appeal to the courts where they might well be upheld - see the recent Camden court case. Indeed a main plank of my defense in that case - on which I was specifically upheld by the judgement of the court - was that it was impossible for me to take account of the circumstances of individual authorities because I did not have the knowledge or expertise to do so. Thirdly, with 413 authorities in England the potential scale of the operation is unacceptable. Even if only 10% of authorities were to be involved (as in Scotland) it would present not just me but other colleagues with an unmanageable problem. Apart from anything else the size and scope of the authorities involved (eg GLC, ILEA, the London Boroughs) would be formidable.

Finally, although the Secretary of State for Scotland enjoyed a major success against the Lothian Council he did so not only because

his Department is responsible for all the services involved but also because they could concentrate their efforts on a handful of authorities. In England inevitably such a situation would not apply.

#### A scheme for direct intervention

The one feature of the Scottish system which could be adapted fairly readily for use in England would be the substitution of an order before the House for a referendum. A scheme on these lines, mentioned in paragraph 9 (ii) of the paper could be on the following lines:-

- i. the Secretary of State would set limits on main rates for authorities as proposed in the draft Bill;
- ii. an authority would not be able to levy a main rate or supplementary rate above those limits without making application to the Secretary of State before, say, June. The Secretary of State would consider the application and any representations make to him and put an order before the House of Commons setting out either the additional rate poundages he proposes to allow to those authorities mentioned in the order. (The Government would of course be blamed for these). The order might contain directions. The authorities would be free to rate up to any additional poundages or to make agreed borrowings when the order was approved. The House would be unlikely to accept a procedure different from Scotland where each authority has a separate order.
- iii. there would be no appeal from the Secretary of State's decision not to include an authority in the order or from the additional rate poundage or borrowing he was prepared to grant.
- iv. there would be no provision for local mandate by way of referendum or election.