Local Gov. : Relations

File

(2)

PRIME MINISTER

Local Authority Spending in 1985-86

Discussion on the 1985-86 RSG is beginning. There are three problems:

(i) How to integrate a third tier of control - the expenditure levels on which rate capping is based - with the existing two - GRE's and expenditure targets which determine hold-back.

(ii) How to simplify this system and base it on two limits rather than three.

(iii) How to give the shire counties the better deal they were promised in this year's debate.

The aim is to achieve all three without adding more than is necessary to local authority expenditure.

Oliver Letwin's note summarises the debate. There is no action for you at this stage but you are likely to be asked to arbitrate after E(LA).

AT

5 March 1984

SECRET

2 March 1984 6

MR TURNBULL

LOCAL AUTHORITY SPENDING IN 1985/86

E(LA) will be meeting on Wednesday, 7 March, to discuss the pattern of local authority expenditure following the selective imposition of expenditure limits.

There are two problems:

1. The Government will now be setting three notional guides for spending: GREs, targets, and limits. This will be even more confusing than the present system.

2. If the targetting system remains intact, our supporters in the counties will be furious, because their targets will still be below their GREs, and they will still be penalised. They will claim that the Rates Bill has done nothing to help them.

Everyone agrees that the way to solve these problems in the medium term is to abolish targets, and to have a straightforward system of GREs and limits. But Patrick Jenkin and the Chief Secretary disagree about how this medium-term goal should be achieved.

Patrick Jenkin seems to want to alter the targetting system so that:

- targets for very high spenders merge with their expenditure limits; and
- targets for low spenders merge with their GREs.

His proposals mean higher targets overall. Once this has occurred, he wants to abolish targets for everybody.

The Chief Secretary argues that Patrick Jenkin's proposal would increase spending, because the general raising of targets would reduce the curbs on every local authority except those which are subject to limits. He seems to want to ensure that any rise in targets for those who spend below GRE is at least matched by reductions in targets for those who spend above GRE.

In this way, targets might eventually converge on GREs, at which point the targetting system could be abolished.

SECRET

Not needed

We strongly support the Chief Secretary. We agree with him that Patrick Jenkin's proposal would almost certainly cause a large increase in public spending. (We also agree with him, for technical reasons which are well exposed in the attached letter from Miss Rutter, that, despite Patrick Jenkin's fears, the Treasury system will ensure a fall in rates in the authorities subject to expenditure limits.)

We therefore suggest that the Prime Minister should be prepared:

- either to note her approval of E(LA)'s conclusions, if these favour the Chief Secretary;

- or to intervene on the Chief Secretary's behalf, if E(LA) goes against him.

But we also recommend that she should stress the need to determine, in advance, the likely effects of the Chief Secretary's scheme on individual authorities. The RSG system is so complicated that an investigation of this sort may well bring to light unforeseen difficulties with the chosen level of adjustments under any proposals. All of these schemes are at best necessary tinkerings with an unsatisfactory system.

OLIVER LETWIN

Approved by:

LOCAL Gov: Relations:

File

Treasury Chambers
Parliament Street London SW1P 3AG

Telex 262405 Telephone Direct Line 01-233 8030
Switchboard 01-233 3000

Barry Potter Esq
Cabinet Office
Whitehall
LONDON SW1

Your reference

Our reference

Date
1 March 1984

Dear Barry,

E(LA): EXPENDITURE LEVELS, TARGETS AND HOLDBACK

Both the Secretary of State for the Environment's paper, E(LA)(84)1 and the Chief Secretary's paper E(LA)(84)3 discuss the possibility that a rate capped authority may have an expenditure level above its expenditure target, and hence pay holdback even though it meets its expenditure level. I promised to let you have our rationalisation of why this does not necessarily produce a perverse result in terms of rate increases. I think it is easiest to do this by taking some illustrative examples - all numbers are, of course, hypothetical.

2. Take two authorities - A and B. A has a 1984/5 target of 1983/4 budget -6% (the maximum cash cut required outside the GLC), B has a 1984/5 target of 1983/4 budget - 3%. Both spend at 1983/4 budget +5%. Holdback on the 1984/5 tariff.

1984/5	Authority A	Authority B
Target	-6%	-3%
Budget	+5%	+5%
Overspend > Target	11%	8%
Holdback	86p	59p

Both authorities are rate limited in 1985/6. Assume that the expenditure level allows no increase in cash over 1984/5 budget; targets are set on the same basis as 1984/5.

1985/6		
Target	-6%	-3%
Budget = Expenditure level	0%	0%
Overspend > Target	6%	3%
Holdback (2-4-8-9-9)	41p	14p
Grant saving compared to 1984/5	45p	45p

3. The holdback schedule could be increased; provided the increase did not mean that authorities A and B had to meet more than an extra 45p in holdback, holdback should not cause rate increases. That would give considerable scope - depending on the size of the gap between target and rate limit. For example, if the holdback regime were toughened to 4-8-10-12-15-15 in 1985/6, Authority A would still only pay 64p of holdback, compared to 86p in 1984/5: equivalent to a grant saving of 22p.

4. This point is bought out in paragraph 7 of the Secretary of State's paper. The key is that the reduced expenditure flowing from a rate limit automatically reduces holdback liability unless offset by a steep increase in the tariff - or the setting of much harsher targets than in the previous year. But the point is far from intuitively obvious.

5. One further point. To exempt a rate limited authority from holdback in year one would cause enormous "re-entry" problems in year two, if that authority ceased to be rate limited and became subject to the normal discipline of targets and holdback.

6. This only focusses on the question of holdback. Obviously changes in grant and GREs can also affect year-on-year rate increases.

7. I am copying this letter to Robin Young and Philip Fletcher (DOE) and, for information, to Peter Shaw (DES), Peter Smethurst (DTp), John Dance (HO), George Kahan (DEemp) to Niall Campbell (SO) and Rowland Potter (WO) and to Oliver Letwin (No. 10 Policy Unit).

Yours,

Jill

JILL RUTTER