



PRIME MINISTER

LIVERPOOL CITY COUNCIL

1. The purpose of this minute is to seek your views on whether the Government should take any action following Liverpool's rate fixing last Friday. We have a meeting of MISC 109 to discuss it at 5.30pm on Wednesday (19 June).

Liverpool's Budget and Rate

2. We are in no doubt that the rate passed by Liverpool City Council, with its clear mismatch between estimated income and expenditure, would be found unlawful (on grounds of insufficiency to meet estimated expenditure) if brought before a Court. The City Solicitor, we understand, gave the same opinion during the budget debate. The Labour Group have made no attempt to "fudge" the deficit. The resolution shows a budget of £265m and a deficit brought forward from 1984/85 of £6m, notes that it would require a City rate of £241.9m (implying an increase in the total rate of 83%) to finance it and then proposes a rate increase of 9% which would raise only £125m - a gap of £117m. (Copy of resolution at Annex A). There is no suggestion that expenditure will be monitored through the year to keep it in line with income - and it is very doubtful with such a low rate that the City could achieve this even if it tried.

Comment

3. By making such an open challenge to the local government finance system, it is clear that the Council, whatever their ultimate objective, are seeking a confrontation with the Government. If the Council are allowed to get away with their action the lesson will be learned by other potentially obstructive authorities (including Lambeth who have yet to set their rate for 1985/86). In year 2 of rate limitation it would then become extremely difficult to prevent widespread deficit budgeting.



4. If the rate which the Council have fixed is allowed to stand, then the authority is likely to face early financial difficulties. The Treasurer has warned us informally that he may have cash-flow problems by the end of the month. It is unlikely that either the market or the Public Works Loans Board will be willing to lend to the City given the size, and clear existence, of the potential deficit; this is reinforced by the fact that the Government Broker will from tomorrow cease to approve any loans of temporary money on behalf of the National Debt Office to Liverpool or Lambeth. This will be seen in the market as a signal of the Government's attitude.

5. As colleagues will recall, the Council can only make a new higher rate if the present rate is quashed by the Courts on grounds of insufficiency. Without a new rate there must be a probability of collapse sometime before the end of the year, with sooner more likely than later.

6. We believe that with a higher rate increase (50%) and some savings, the Council could produce a balanced budget (Annex B suggests how this might be done). Whether it would be prepared to do so is another matter.

Options

7. We have three main options:-

a) To refuse to be drawn by the Council and leave any action to a local ratepayer and the Auditor; or

b) To ask the Attorney General to seek judicial review of the Council's resolution, the quashing of the rate, and the making of an Order against the Council to make a properly balanced budget and rate; or



c) To negotiate with the Council to fill the gap in the City's budget with either special grant or special borrowing consent. Since we have no powers to make special grants, and either course would be politically indefensible (not least in view of the Lambeth situation), this course is not considered further.

Examination of the Options

Option (a)

8. By doing nothing we would leave the field open to others to respond to the Council's action. There is however no evidence that anyone will come forward to challenge the rate and provide the Labour Group (or a coalition of moderate Councillors) with the opportunity to make a proper one. In particular it seems unlikely at present that local Conservative or Liberal Councillors will act.

9. The District Auditor is already carrying out an extraordinary audit of the City Council in connection with the delay in rate fixing and consequent losses. He will be issuing an official notice next week to the Councillors concerned specifying the losses which he considers have been incurred. This process could be extended to embrace the consequence of the deficit budget, but the Auditor has no power to challenge the rate itself; his action could rather be directed at identifying surchargeable losses. Nor would his action be immediate. Any disqualifications of Councillors flowing from surcharge would be very unlikely to take effect before the late autumn, even if there were no appeals. It could easily run into the New Year if, as seems likely, the Councillors concerned appeal.



10. If no action is taken against the rate, the key issue will be how credit holds up. As already indicated, the Government Broker is not going to lend further. There is therefore a strong risk of financial collapse at any time from July onwards, and it would almost certainly occur before the Auditor's activities reached conclusions.

Option (b)

11. Our only means of ensuring that the Council have a further opportunity to rate is action by the Attorney General. This might, if done immediately, prevent financial collapse and the need for Commissioners. It would also demonstrate the Government's clear intention to stop authorities playing fast and loose with the local government finance system.

12. However this action would call for very careful presentation. The Council would paint the Government as vindictively enforcing its policies through the Courts and, if they did eventually set a higher rate, would lay the blame at our door. Alternatively they might present what had happened as a forerunner for opening negotiations. Furthermore, were the Council given the opportunity to rate again, there is no guarantee that they would take it up. (If they did not, they would be in contempt of Court and open to fines and possible imprisonment.) We must accept that if the Attorney General acts - or indeed if we do nothing - the possibility of financial collapse and the eventual need to appoint Commissioners remains. We could therefore require the Commissioner legislation during the summer or early autumn - possibly during the Recess. And I believe we ought shortly to be approaching possible Commissioner candidates if there is to be any chance of our being prepared for early collapse.



Payment of Grants

13. In reaching a conclusion, there is one further immediate issue to bear in mind. We are still paying Rate Support Grant, since there is a statutory requirement to do so on the Secretary of State's best information about spending levels and there is no dependence in respect of RSG on a rate being made. But this year on legal advice we decided to make no payments of grants that are dependent on a rate being made (rate rebates, disabled rate relief, payments in lieu of rates on Crown properties and Enterprise Zones) until authorities had fixed rates. The relevant Accounting Officers (DOE, DHSS and Treasury) must now decide on the propriety of making such payments to Liverpool given the doubt over the legality of the rate. (The Treasurer has already told us that these payments would considerably ease his cash-flow position). This issue remains if we decide to do nothing.

Conclusion

This is an evenly balanced decision. In order to give Liverpool a second chance, and seek to avert the risk of collapse and Commissioners, the rate must be quashed. Ideally this would be done, not by Government, but by a local ratepayer or Councillor. Financial and political considerations make it unlikely that anyone will come forward.

The only other way to quash the rate is to ask the Attorney to act. We would then be sending a clear signal to any other authorities - Lambeth this year, and rate capped authorities next - that we are not prepared to tolerate deficit budgeting. This is the course which on balance I recommend.

However there is no option which guarantees to avert the possibility of early collapse and the need to introduce Commissioner legislation sooner rather than later. We therefore need to look again at

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our contingency preparations. And if we decide that the Attorney General should take action, it will be essential to prepare the ground by careful briefing to the Press so that it is clear that this action is necessary in the interests in the people of Liverpool to seek to prevent financial breakdown and chaos.

I am copying this to members of MISC 109 and to Sir Robert Armsrong, Mr Brearley and Dr Walker.

At Dani
for
P J

17 June 1985

Approved by the Secretary of State
and signed in his absence