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E (80) 93

COPY NO 56

5 September 1980

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MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

LOCAL AUTHORITY CURRENT EXPENDITURE: 1980/81

Memorandum by the Secretary of State for the Environment

1. The budgets submitted in April to my Department by local authorities implied a 'raw' planned excess on current expenditure of 5.6% (£740m at November 1979 prices). My Department has now analysed the 439 revised budgets out of a possible 458, received so far - covering 98.5% of expenditure. Planned excess has been reduced to 2.6% (£350m). The table at Annex A sets out the analysis of the revised budgets. Annex B shows a breakdown of the performance of authorities by political control.

2. Our problem now is to interpret this in the light of past experience and practice. The following table shows the performance of authorities at outturn compared to original budgets.

VOLUME OF CURRENT EXPENDITURE - COMPARISON OF BUDGETS AND OUTTURN

Year	Original Budget	Revised Budget	Outturn
	% above RSG settlement assumption		
1976/77	4.7%	2.8%(a)	-0.3%
1977/78	1.4%		-2.7%
1978/79	1.9%		-0.8%
1979/80	3.6%		0% (estimate) (b)
1980/81	5.6%	2.6%	not available (c)

(a) Revised budgets called for by Labour Government.

(b) The situation in 1979/80 is complicated in that after the election we called for a reduction of 3% on the original (Labour) target thus making the original budget 6.6% over our new target. Our latest estimate is that the original 3.6% overspend has disappeared but that they failed to achieve our further 3%. But, of course, the extent to which this was the normal underspend against budget or was due to our call for lower expenditure cannot be quantified.

(c) See below for estimate of outturn.

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The shortfall of outturn volume on budgeted volume in these years, expressed as a percentage of the settlement target, was

1976/77	5.1% (revised budget 3.1%)
1977/78	4.0%
1978/79	2.7%
1979/80	3.6% (estimated)

3. Colleagues will see from the above that outturn is always several % points below budgets. On the basis of the above it appears reasonable to assume that most, if not all, of the excess will disappear. However, two other factors are relevant and significant. First, the pattern above related to a period of rising expenditure. It is arguably easier to underspend when you are budgeting to increase than it is to get below budgets that are themselves reductions from previous outturn.

4. Secondly, 70% of current expenditure is accounted for by manpower. The fall in the manpower figures would therefore have to take place very fast to satisfy me that the excess could disappear. There are now the first grounds for optimism that our policies are achieving our purpose. This can be seen from the breakdown of the quarter by quarter reductions for the year ended June 1980

(Full time equivalents)		
3 months to 30.	9.79	7,000
" " "	31.12.79	4,000
" " "	31.3.80	3,000
" " "	30.6.80	15,000
Total Reduction in 12 months		<u>29,000*</u>

5. The Manpower Watch figures for June therefore suggest that we shall have seen the largest ever reductions in local authority manpower. They year on year reduction from June 1979 of 29,500 means that authorities will have reduced manpower by much more than the previous best performance in a year - 21,000 in 1977. Nevertheless, if the excess is to be wholly eliminated I believe that something approaching a further 90,000 will have to be achieved by March 1981. It is a matter of conjecture as to how close we will get and whilst I now believe that we will make significant inroads into that figure, I cannot guarantee that we will reach the target.

6. The need to achieve our public expenditure reductions, and the knowledge that we shall be seeking yet a further 2% reduction in expenditure, leads me, therefore, to take a cautious and conservative estimate. There is, of course, an element of judgement in this but my view is that we should work on the possibility of an excess of some £200m. (Just over half the budgeted excess).

7. When we last discussed this (E(80)17th Meeting, Minutes Item 2) we considered selective and non-selective options for action. These were set out in my paper E(80)63. I have re-considered all the

*For General Services (ie excluding law and order and STEP) the reduction in the year to June 1980 is 35,000

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options and in particular the three forms of selective action against overspending authorities which are outlined in Annex C.

8. My conclusions are as follows:

(i) CAPITAL MORATORIUM IN 1980/81

Reject - an immediate ban on new approvals would save only £40m, would further damage our relationship with the construction industry and impose capital cuts when more importantly we seek revenue cuts.

(ii) HOLD BACK CAPITAL ALLOCATIONS FOR 1981/82

Reject - this could not be entirely successful as authorities could seek to circumvent it through the flexibilities in the new capital controls system. Again, we would be reducing capital investment to allow authorities to protect current expenditure.

(iii) SELECTIVE ACTION

The general problem of local authority overspend is largely attributable to the minority of authorities which have chosen to ignore calls from successive Governments for expenditure reductions and restraint, and have pushed up their expenditure levels to unreasonably high levels. I have considered whether further selective action against the potential overspenders would be desirable, eg by imposing a direct limit on the level of rate increases or by requiring overspending authorities to submit their budgets on their proposed rate increases to a local referendum or election. All of them however bristle with practical difficulties. All would require major and highly controversial legislation. None could operate before 1982/83. In the circumstances I do not think it would be appropriate to pursue any of these at the present time, at least until we have seen how block grant affects authorities' behaviour during the coming year. In this context I should add that the preliminary work by the Grants Working Group has shown that block grant will bear very harshly on overspenders. Subject to any decision which we may take about safety nets, some of the highest overspenders could be liable to grant losses equivalent to a rate of 20p or more.

(iv) TRANSITIONAL ARRANGEMENTS

I propose that the transitional arrangements should apply to all authorities with rates above a threshold rate level set at 155p (30% above the normal level represented by the 119p "notional uniform rate") unless they have cut their rateborne expenditure in the current year in real terms (for technical reasons this rule will have to be expressed as a significantly below-average cash increase), or have achieved their two-year

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volume target. There will be a minimum penalty equivalent to a 1p rate, and larger excesses will attract larger penalties up to a maximum equivalent to a 5p rate. Details of the scheme are given in Annex D. The 5p maximum is harsh by the standards of grant changes in recent years - "safety nets" have usually limited losses to a maximum of 2-3p or less - and many of the overspenders who will be caught are also likely to be big losers in next year's block grant settlement. The total grant reclaimed under the arrangements will be about £174m.

(v) RE-ORDERING OF URBAN PROGRAMME 1981/82

Many of the highest spending authorities have partnership or programme status under the Urban Programme. While the majority have made efforts to reduce their expenditure (or are not in any case high spenders) a small number appear to be flouting our policy. These are most of the Docklands authorities in London (where however the partnership arrangements are due to be superseded by the Urban Development Corporation), and also Hackney, Islington and Lambeth. There is a strong case for not adding to the high levels of their expenditure by Urban Grant. The amounts of uncommitted expenditure for 1981/82 are relatively small, and are also shared among other authorities (GLC, ILEA, AHAs). Nevertheless, I think it right that we should be prepared to take clear action, and I would therefore propose to adjust the level of partnership allocations to these authorities for 1981/82 accordingly. I should make it clear that I am not seeking economies here and propose to redistribute the amount saved to other urban programme authorities. My aim is to let those authorities know that partnership has a real meaning.

(vi) CUT IN 1980/81 RSG CASH LIMIT

Cash limit cuts would put pressure on authorities by reducing their cash flow which could result in higher borrowing, higher rate increases in 1981/82 or reduced expenditure in this year or in 1981/82 - as I said in E(80)63 probably an unpredictable combination of all three. Nevertheless, I believe that this is our most potent, if indiscriminate weapon. In particular, it would enable us to say publicly that we were proposing to offset the likely real overspend by an equivalent reduction in grant. Even if this did result in an increase in local authority borrowing, that increase would be offset by the reduction in central government borrowing. Above all, it would emphasise for the benefit of authorities and the general public that we do not intend to allow local authority overspending to go unchecked. I propose therefore that we should reduce the cash limit on the 1980/81 Increase Order by £200m, £174m of which will be met from grant penalties under the transitional arrangements.

9. I feel I must tell colleagues that there is one aspect of my proposed action which is indefensible other than in the acute

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economic situation that we face. Obviously the response from 458 authorities was immensely varied. The table at Annex B shows the politics of this, but underlying this is an even more varied picture. Many of our own supporters have faced agonised public criticism in their determination to back the Government. Others, including, I fear, some of our own party have virtually ignored our request. The reduction in the cash limit in no way reflects the efforts made and will hit some disproportionately who have done what we asked. (Annex E shows the effects of a cut of £200m). We must also recognise that although it produces a saving in central government expenditure it does not necessarily produce a saving in public expenditure. Nevertheless, at present it is our only weapon involving substantial sums.

10. In the light of the above, colleagues may wish to consider a variation in the presentation of the cut in the cash limit. It would be feasible to withhold the £200m at first Increase Order in November this year and to undertake to reconsider at second Increase Order in November 1981 when we will have a clearer picture of outturn in 1980/81. Such action would appear fairer to our friends, would give local government as a whole a mammoth incentive to demonstrate that the excess will disappear and would enable us to avoid the accusation that we were punishing local authorities for a crime which they had not yet committed.

CONCLUSION

11. I therefore invite my colleagues to agree that I should take the steps outlined in paragraph 8(iv), (v) and (vi) above, the latter subject to the variation proposed in paragraph 10, and that I should seek an early opportunity coincidental with the publication of the June Manpower figures to announce these as our response to the revised budgets.

MH

Department of the Environment
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5 September 1980

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CURRENT EXPENDITURE VOLUME IN ENGLAND AND WALES 1980/81
REVISED BUDGETS

ESG current expenditure 1980/81	Totals £m (Nov 79 prices)	Analysis of figures in column 1 £m(N79)	£m (N79)
A RSG target	13,311		
B original budget	14,050	(i) original (crude) volume excess (B-A)	739(5.6%)
		(ii) sub-groups' estimate of overspend at outturn	359(2.7%)
C amendments to item B	- 150	comprising :	
		(i) effect of late returns (a)	-5
		(ii) correction of effect of errors by local authorities and changes to definition of income volume	-101
		(iii) revision of DOE forecast of uncapitalised (b) expenditure	-44
D amended estimate of original budgets (from B and C)	13,900	(i) amended estimate of original volume excess (D-A)	589(4.4%)
E revised budget (RER81B corrected for definition differences)	13,660 ^(c)	(i) revised budget: crude volume excess (E-A)	349(2.6%)
		(ii) savings attributable to revision of budgets (D-E)	240
		(iii) total savings over original budget figure (B-E)	390 ^(d)
F estimate of residual over-budgeting	75 to 225 (central estimate £150m)		
G possible outturn	13,440 to 13,580 (central estimate £13,510m)	(i) estimated likely residual volume excess at outturn (G-A)	approx 125 to 275 (central estimate £200m or about 1%)

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ANNEX B

ANALYSIS OF REVISED BUDGETS BY POLITICAL CONTROL

	<u>No of Authorities</u>	<u>Original Budget</u>	<u>Savings Requested</u>	<u>Savings Achieved</u>	<u>% Excess Remaining</u>
CONSERVATIVE	223	£8858.0m	£290.7m	£161.1m	1.5%
LABOUR	115	£3596.8m	£203.5m	£ 45.4m	4.7%
OTHER	120	£1699.9m	£ 90.1m	£ 21.3m	4.3%

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ANNEX C
SOME POSSIBLE FORMS OF SELECTIVE ACTION AGAINST OVER-SPENDING
AUTHORITIES

1. This note briefly considers three possible forms of selective action against over-spending authorities and notes some of the problems that would arise:

- (i) local referendum or election on budgets of over-spending authorities.
- (ii) limiting rate increases for overspending authorities
- (iii) cutting the capital programmes of over-spending authorities.

2. Preliminary Issues. For any of these approaches there are two preliminary problems:

- (i) to define overspending
- (ii) to establish a viable timetable for selective action.

3. Definition of Overspending. A simple objective definition of "overspending authorities" might be "authorities spending more than a specified percentage above their Grant-related Expenditure (GRE)". This might be assessed on the basis of their budget for a relevant base year (Year 1) as returned to DOE in April/May on the RFR return.

4. Timetable for Action. If overspending in Year 1 is only identified at April/May on the RFR return it will already be too late to intervene to limit the rate for that year or to require the budget and/or the rate to be submitted to a referendum or election. [It may also be too late to adjust capital allocations for that year]. This means that the corrective intervention may only take effect in Year 2. The only way round this would be if authorities could be made to submit draft budgets or provisional rate increase proposals to DOE around Christmas of Year 0 so as to permit intervention by Government before the finalisation of the budget and rates, and before the start of Year 1. This would however

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impose very severe practical problems on local authority's budgetary cycles which would not be easily surmountable, so that one might be driven back to intervention in Year 2. This would mean for example that authorities overspending in 1981/82 could only be subjected to the regulating action in 1982/83 when the overall economic situation might be rather different.

5. Local Referendum or election This would involve requiring authorities proposing to overspend grant-related expenditure assessments by more than a specified percentage (or to increase their rates by more than a specified percentage) to submit their proposed budgets to a referendum, or to submit themselves for re-election. Objective: to give the local electorate an opportunity to express direct disagreement with the high-spending policies of their authority. Problems: danger of setting-up a direct political confrontation between the local electorate (if they endorse their authority's budget) and the Government; difficulty of articulating the referendum or election issue in a fair and realistic way.

6. Limiting Rate Increases for Overspending Authorities
Objective: to compel authorities to trim their current expenditure by controlling their income. Main problem: risk of forcing authorities into bankruptcy if they refuse to trim expenditure and go for confrontation. This might lead to necessity for Government intervention either through Commissioners or Receivers to protect creditors and to maintain essential services.

7. Cutting the Capital Programmes of Overspending Authorities
Under the provisions of the Local Government Planning and Land (No. 1) Bill, as presently drafted, we could not take selective action in respect of the capital allocations of individual authorities without the danger of successful challenge in the courts. In any event, we should have to take powers to restrict all the flexibilities of the new capital controls schemes as these would enable authorities at least for a period to circumvent the reduced allocation by the use of capital receipts etc. Such action would undermine the grudging acceptance which we have now achieved for the new controls system.

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ANNEX D

THE TRANSITIONAL ARRANGEMENTS

1. The transitional arrangements provide for grant penalties for authorities with rates (which reflect their spending levels) above a specified threshold. The penalties are to be related to the size of the excess and expressed in terms of an equivalent rate poundage for the authority affected. London authorities' uniform rates are to be adjusted so that they are comparable with those of non-London authorities (which do not receive the special extra grant which has been paid to London to help keep rate bills down).

2. There is provision for authorities which would otherwise be penalised to be excluded from the scheme if they have made exceptional cuts in expenditure. In addition

- the City of London will be excluded (it features at the head of the list for technical reasons related to the fact that its services are provided primarily for a non-resident population);
- on application by any authorities affected, recognised expenditure on emergencies, loss of rates from closed steel works, and local contributions to urban programme expenditure will be excluded from the calculation of penalties (the effects of this will be very small).

3. The proposed scheme is based on

- a threshold of 155p (30% above the "notional uniform rate" that would be charged in any areas where expenditure was in line with assessed expenditure need);
- a penalty equivalent to a 1p rate plus the equivalent of a 0.05p rate for each 1p by which the authority's rate exceeds the threshold, subject to a maximum equivalent to a 5p rate;

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- a waiver for authorities whose cash increase in rate- and RSG-borne expenditure in the current year is at least a full percentage point below the average for their class (this will in practice exclude only authorities that have made a reduction in expenditure in real terms in the current year) or who have met their volume targets.

4. The results are shown in the table (the effects of exempting expenditure on emergencies etc cannot be calculated at this stage but will be very small).

Authorities	Uniform or adjusted uniform rate poundage	Penalty expressed as a rate poundage equivalent	Penalty in cash terms
1. [City of London*]	[160p]	-	-
2. Camden	256p	5.00p	£5.22m
3. Islington	236p	5.00p	£2.54m
4. Southwark**	213p	-	-
5. Tower Hamlets	210p	3.75p	£1.56m
6. Lambeth	208p	3.65p	£2.12m
7. Hackney	190p	2.75p	£1.01m
8. Haringey**	190p	-	-
9. Lewisham	181p	2.30p	£0.98m
10. Newcastle	179p	2.18p	£1.30m
11. Hammersmith	166p	1.55p	£0.51m
12. Swansea**	165p	-	-
13. Brent	163p	1.40p	£0.71m
14. Waltham Forest	162p	1.35p	£0.53m
15. Newham**	160p	-	-
16. Manchester**	159p	-	-
17. Greenwich	158p	1.15p	£0.42m
18. Afan**	157p	-	-
19. Doncaster**	157p	-	-
20. Sheffield**	156p	-	-
21. Hounslow	156p	1.05p	£0.50m
22. Wandsworth**	155p	-	-
23. Merthyr Tydfil**	155p	-	-
TOTAL			£ 17.4 m

* excluded

** qualifies for waiver

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ANNEX E

EFFECTS OF A CASH LIMIT CUT IN 1980/81

1. The table shows by class of authority and by region the effect of a £200m cut. These would be reduced for the majority of authorities by the grant reclaimed from high-spending authorities under the transitional arrangements (about £17^{1/2}m).

2. The effects of the resources element clawback of about £100m for the current year are also shown. These would be additional to the effects of the cash limit cut.

	Effects of £200m cut in cash limits 1980/81		Effects of resources element clawback	
	£m	As a percentage of expenditure	£m	As a percentage of expenditure
BY TYPE OF AUTHORITY				
Shire counties England	85.5	1.14	50.7	0.67
Shire counties Wales	12.3	1.45	9.4	1.10
Metropolitan districts	54.9	1.31	30.9	0.73
Inner London	12.2	0.81	0.8	0.05
Outer London	18.7	1.09	2.0	0.12
Shire districts England	13.6	1.06	8.2	0.64
Shire districts Wales	2.7	1.37	2.1	1.09
BY REGION				
South East	59.2	0.79	16.1	0.21
South West	15.3	1.18	10.6	0.82
East Anglia	6.0	1.09	4.0	0.73
West Midlands	19.1	1.02	9.3	0.50
East Midlands	14.8	1.26	8.5	0.72
North West	30.9	1.15	17.1	0.64
Yorkshire & Humberside	23.9	1.21	16.4	0.83
Northern Region	15.9	1.25	10.6	0.83
Wales	15.0	1.44	11.5	1.10

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