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The Rt Hon John Major MP
Chief Secretary
HM Treasury
Treasury Chambers
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Dear John
COMMUNITY CHARGE CAPPING IN SCOTLAND

Thank you for your letter of 3 May. *FILE WITH PG*

As you surmise, I have been giving a good deal of thought to Scottish local authorities' budgeted overspending this year and whether it would be appropriate to respond by using my community charge capping powers. As you would expect, there are some very conflicting considerations.

The overall picture is of budgeted expenditure 11.4% higher than budgets for 1988-89. This clearly involves a real terms increase - though, bearing in mind new burdens imposed since last year (including in particular school boards and community charge collection) and also that actual rates of inflation experienced by local authorities will have been higher than GDP or RPI figures, the volume increase will not be so high as 6% - perhaps 3.5% to 4%. In accordance with experience in past years, I would expect actual expenditure by the end of the year to be somewhat lower than this.

I was interested in your speculations as to the reasons for this. My own view, based on post-mortem discussions which my officials have had with senior local authority staff and on a meeting that Ian Lang and I had with the Convention of Scottish Local Authorities 2 weeks ago, is that several factors were involved. In the first place, the ending of grant penalties must have had some impact. Second, the change in grant arrangements will have been seen by some authorities as providing an opportunity to increase their spending while obfuscating the reasons for the increase. Third, I think that many local councils have seen all too clearly the pressure that community charge arrangements will quickly bring to bear on their spending arrangements, and will have decided on a last burst for growth while they felt that the going was still good. There is certainly evidence that the 2 traditionally high spending authorities - Lothian and Strathclyde Regions - went to enormous efforts (albeit starting far too late in the last financial year) to tailor their budgets to what they regarded as acceptable community charge levels.

You will gather from this that, while Scottish authorities' budgeting for this year is very disappointing, I do not think we need be unduly

depressed about it. It is against that background that I have been considering use of the charge capping powers.

You will be familiar, from our exchanges in previous years, with the legislative background and constraints. The statutory test for using the charge capping power is whether an authority's planned expenditure is "excessive and unreasonable". In reaching a view on this I must have regard to the financial and other relevant circumstances of the area of the authority; and in addition I may have regard to other considerations including the expenditure or planned expenditure of other comparable authorities in the year concerned or in any preceding year, general economic conditions, and "such other financial, economic, demographic, geographical and other criteria" as I consider appropriate.

In practice, in the absence now of expenditure guidelines, I have to have regard to "the financial and other relevant circumstances of the area" by reference to assessed needs; and the other factors are taken into account by comparing each authority which may be a candidate for capping with comparable authorities in respect of its increase in expenditure over the previous year, its increase in expenditure volume over the previous year and over a longer period, and its expenditure per head on the same basis. The comparator authorities for Regions are (because of their small total numbers) all other Regions with the same range of functions, but for District Councils the establishment of comparator authorities is itself a fairly complex statistical exercise.

These procedures have been refined over the years, and have been the subject from time to time of detailed consultation with the Scottish Law Officers. In particular, in the Scottish legislation the test of "unreasonableness" is in addition to the test of being "excessive". We take the view that "unreasonable" is to be construed in the Wednesbury sense as meaning so unreasonable that no reasonable person would plan such expenditure. This has generally been regarded as a very strict test.

All this will be familiar to you - and certainly to your officials - but I have thought it worth setting out in some detail for a very good reason. The care with which I and George Younger before me have exercised these powers has meant that we have never yet been challenged in the Courts. I would be particularly reluctant to cut any corners in the procedure this year when authorities may be more than usually liable to challenge me, and when any adverse court decision would be particularly damaging for future use of the powers.

On that basis, I am quite clear that I could not take action against any of the Regional Councils. Their average budget to budget increase is 10.5%, against which the highest increase is Highland's at 13.5% but they are only 3.6% over their assessed need which is well below the Regional average. In the case of Lothian their increase is 11%. But their volume increase is the lowest of all Regional authorities, both over a one and a 5 year period, and their expenditure per head is below the regional average.

The District Council position is different and, as your officials will have advised you, there are certainly several District Councils reporting substantial budget to budget increases. Your officials have a detailed working paper which identifies 3 District Councils as candidates for capping. You ask if I could adjust the criteria in order to throw up around 6 candidates. Quite apart from the legal impropriety of

exercising a discretionary power in that way I could only do so if I was to set aside part of my well established and defensible scrutiny tests. To do so would in my judgement only increase the risk of challenge. But even as regards the 3 identified by the scrutiny, the issues are not entirely straightforward. In particular, Glasgow's budget includes provision for substantial expenditure on a one-off basis, related to the City's designation next year as European "City of Culture". There would be very obvious difficulties in taking action against Glasgow in these circumstances. That leaves me with Clydebank and Stirling District Councils, against whom clear cases for action could certainly be sustained.

Obviously, I have thought carefully about proceeding with these 2 authorities. But I am far from clear as to the advantages of doing so, and I see considerable disadvantages. The main practical point is that capping these 2 authorities would make very little difference to the total budgeted overspend by Scottish authorities - about £3.5 million, out of total budgeted expenditure of £4126 million. It is hard to believe that this would have any desirable demonstration effect on other authorities. It may, indeed, simply point up the limitations on the practical application of these powers. As you say the fundamental objective is to establish better accountability. We should give accountability a chance to work. Obviously, as you recognise, any community charge capping will be controversial. It would also undoubtedly generate a good deal of criticism, which is likely to focus on our abandonment of local accountability. The practical question is whether it is worth stirring controversy for such little return. My own feeling is that, unless we can use the capping powers to make a substantial difference to spending levels or to make some very clear political point, it is not worth doing and we simply risk bringing the underlying philosophy of the new system into disrepute.

There are 2 other aspects to the issue. The first, which you recognise in your letter, is the risk of giving the wrong signals in respect of future years; and there may also be some risk that failure to take action this year could prejudice future action, in a legal sense. But I think that it will be perfectly possible to elaborate counter arguments (if we are ever required to do so) on the basis that the circumstances in this first year of the new arrangements are exceptional; that action - or lack of action - this year is attributable to the changeover and the need to let the new system settle down; and that my decisions this year offer no necessary precedent for future years.

The other question is whether, if I fail to use the powers this year, this will create any awkward precedent for Nicholas Ridley next year. I cannot see that it would. My capping powers are of course unchanged in substance from those that I had under the rating system, and their use has been well established in rate capping over a number of years. Second, as I understand it, Nicholas faces a number of far-left authorities in England who pose problems of quite a different order from those which I face. Third, in determining whether a Scottish authority's expenditure is "excessive and unreasonable", what I undertake is a comparative exercise in which the comparators are other relevant Scottish local authorities with similar assessed needs. I have never compared expenditure of a Scottish with that of an English authority and, of course, there would be no basis for doing so since our needs assessment arrangements are different. All of these points could apply equally in reverse. And finally, the new English capping legislation (benefiting

from our experience) operates by reference only to expenditure being "excessive" - ie the statutory test in England is different. In his letter of 16 May, Nicholas recognises that a read across from the Scottish situation is unlikely.

In the light of all these points I do not propose to undertake any charge capping this year. But one point that does occur to me, on looking at the matter again in the light of your letter, is that I should perhaps take an early opportunity to make clear that this decision should not be taken as a precedent for the future. I will look for an early opportunity to make this point, either in a public speech or in one of my forthcoming meetings with the local authority associations.

I am copying this letter to members of E(LF), to the Lord Advocate, and to Sir Robin Butler.


MALCOLM RIFKIND

LOCAL COST: Rating PTL

