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PRIME MINISTER 24 April 1990

LOCAL AUTHORITY EXPENDITURE CONTROL

Chris Patten's latest note concludes that a control system based on targets and incentives (Annex D) is simply too complicated to get up and running next year. Thus expenditure control would be limited to a revamped capping system.

This is going to leave you extremely exposed on the level of next year's Community Charge. If local authority spending next year rises 10% and aggregate exchequer finance (AEF) also 10%, then average Community Charge in England will rise by 12% to £405. If the figures altered just a bit (local authority spending up 12% and AEF 9%) average charge goes up to £430 which is 18% up on this year. So something has got to be done to limit expenditure.

More extensive capping is certainly one option. But, however widespread, it is a response after the event. The initiative in setting high budgets remains with local authorities. If they know capping is likely, hostile authorities will be all the readier to set high, unrealistic budgets, in the knowledge that the Government will take the blame for cutting them back.

Even if more extensive capping powers are taken the Government still needs to have some means of infuencing/controlling budgets before they are set, so that authorities are forced to be realistic and responsible at the outset, and so that if a generous grant settlement is given there is certainty that it will not leak into higher spending.

If targets related to SSA are not practicable, what else is there? In an attempt to answer this, may I urge you to reconsider a limitation related to the RPI. You rejected this idea at the last meeting on the grounds that it would simply validate existing high spending. So it would, but so would the targets system proposed in Annex D (para 6). It is made clear that any limitation for next year is, to be realistic, going to have to be based on this year's spending. In view of this I do believe an RPI-based system is worth another look.

If there is no realistic alternative for 1991 but to take 1990/91 spending as a base, an RPI cap (or, better, RPI-x to create efficiency savings) is worth consideration:

- it is easily understood. (One of Chris Patten's criticisms of the targets approach in Annex D is that it would simply not be understood.)

- it is simple. One measure of limitation would in effect apply to all authorities.

- it is inherently reasonable to demand that no local authority spends more in 1991/92 in real terms. This is a proper defence against any charge of 'cuts', and would give the Government the high ground in arguments over 'cuts'.

- it would mirror what has been done for business rates.

- an RPI ceiling would certainly need to go hand in hand with more extensive capping powers, in recognition that many authorities' 1990/91 expenditure is too high. It should also go hand in hand with an incentive system so that, in RPI-x, the larger x is the greater the benefit to chargepayers.

- but as an overall ceiling imposed on next year's spending it would at least contain the problem by preventing leakage. Within the safety of this overall ceiling the individual problems of high spending could then be tackled. And presumably it would be relatively easy to legislate for- the formula in the 1988 Act for limiting business rate increases to the RPI fits into a couple of pages.

CONCLUSION

In your preliminary consideration of Chris Patten's paper, I recommend you reconsider an RPI approach once more. It is not perfect, but given the absolute necessity to put a ceiling on local authority expenditure next year, in a defensible and easily understood way, it seems to be the best, if not the only blunt instrument available.

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