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PRIME MINISTER

14 October 1986

19/10
LOCAL AUTHORITY CAPITAL CONTROLS

Nicholas Ridley is due to announce tomorrow the Government's decision not to proceed in the 1986/7 session with major legislation on the local authority capital control system. He will be issuing a press notice and writing to the Chairman of the Local Authority Associations in terms of the attached letter.

The main points in the letter are:

- the Government cannot seriously consider abandoning direct control of local authority capital expenditure at this stage;
- but none of the systems canvassed in the consultation document commanded general support;
- the Government therefore intends to reconsider the issue alongside its proposals for reforming the financing and control of local authority current expenditure.
- in the meantime, the present control system will stand subject to the ending of advance and deferred purchase schemes, bringing leases fully within the control system and a number of other more minor changes such as the treatment of back-to-back schemes (where a local authority buys and then immediately sells an asset).

Peter Stredder

PETER STREDDER



2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

To the Chairmen
Local Authority Associations
in England

15 October 1986

At last month's meeting of the Consultative Council on Local Government Finance, I indicated that we were unlikely to put major legislation on local authority capital controls through Parliament in time for the 1987/88 financial year. I can now confirm that we have decided against major legislation on this matter in the next session of Parliament.

We have reached this conclusion after considering very carefully more than 370 responses to the Green Paper "Paying for Local Government" and the subsequent Consultation Paper on capital. The responses have come from the associations, from individual local authorities and from a wide range of other interested parties. I want to emphasise how grateful we are to all respondents for their constructive contribution to the review. We have also of course taken into account the views expressed in the reports by the Audit Commission and by the Comptroller and Auditor General; we await the report of the Committee of Public Accounts on the same subject.

The Government remains committed to the firm control of public expenditure, which is vital to economic recovery. Local authority expenditure is a large component in the total of public spending. So we do not believe, despite the arguments advanced by some respondents, that we can seriously consider abandoning direct control of local authority capital expenditure at this stage. On the other hand, it is clear that neither of the systems outlined in the consultation documents earlier this year commands general support within local government. Any new system should offer substantial improvements for both central and local government.

I believe that the control of local authority capital expenditure and borrowing is now best reconsidered alongside the proposals in the rest of "Paying for Local Government" for the wider reform of local government finance. There would be obvious advantages in introducing changes in the arrangements for current and capital together so that interactions between the two can be allowed for as fully as possible. Meanwhile, I would prefer to avoid the upheaval which comprehensive reform of the control system would create, for what would be a comparatively short period.

Until then, the present system of capital controls must stand. But two significant changes are needed. First, as I announced on 22 July, we intend to introduce legislation to change the treatment of advance and deferred purchase schemes with effect from midnight that night. At the time of that announcement, I said that we would consider an exemption so that authorities which genuinely needed to use the device for its proper purpose for an occasional project would not be disadvantaged. I can confirm that we do intend to introduce such an exemption. It will be restricted to one project, not exceeding a given value, per authority in a specified period of time. The precise details of the

GJS



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The Rt Hon The Viscount Whitelaw CH MC
Lord President of the Council
Privy Council Office
Whitehall
LONDON
SW1

My ref:

Your ref:

13 October 1986

NBM

Dear Lord President,

Thank you for your letter of 9 October giving your agreement to my making the announcement on the outcome of the review of local authority capital controls in the way outlined in my letter of 30 September. I have also seen the letters of 7 October from Wyn Roberts, 8 October from Kenneth Baker, 6 October from John Moore and 9 October from John MacGregor.

I have accepted John MacGregor's amendments to the letter to the Chairmen of the local authority associations. He also suggested that we consider extending the amendment on revenue bills to include the raising of the £3 million rate income threshold. I am happy that his and my officials should consider this as he suggested, but I do not think we can settle the matter before my announcement. I shall therefore omit the reference to revenue bills from the letter to the associations. I will consult colleagues again in due course.

I have noted Kenneth Baker's proposal on back-to-back schemes, with which I agree. This need not affect my announcement, which does not go into the details of the criteria for back-to-back schemes, but I would hope that John MacGregor could agree to the proposal in due course.

Finally I am happy to fall in with Wyn Roberts' suggestion that he would use the meeting of the Welsh Consultative Committee on Local Government finance on 15 October for making the announcement as regards Wales. I therefore intend to write to the Chairmen of the local authority associations in England, and to issue a press release, on that day.

I am copying this letter to the Prime Minister, colleagues on E(LA), the First Parliamentary Counsel and Sir Robert Armstrong.

Yours sincerely,

PP NICHOLAS RIDLEY

(Approved in draft by the Secretary of State and signed in his absence.)

LOCAL GOVT Relations PT30



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Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Nicholas Ridley AMICE MP
 Secretary of State for the Environment
 Department of the Environment
 2 Marsham Street
 LONDON SW1P 3EB

October 1986

Dec. Nickley,

NBRN

LOCAL AUTHORITY CAPITAL CONTROLS

Thank you for sending me a copy of your letter of 30 September to Willie Whitelaw about your proposed announcement. *will request.*

I am content with what you propose on timing and substance. I am prepared to accept the minor concessions on back-to-back schemes and Government CPOs which formed part of your major package, on the basis that they will be PES neutral and de minimis respectively, as you suggest. I should be grateful if my officials could be kept in close touch with further work on developing the details of these items.

I endorse the proposal to modify the provisions limiting individual local authorities' issue of revenue bills. At the same time it would be logical to update the limit on the minimum size of authority empowered to raise revenue bills, as a counterpart to the increased scope which the change would provide for most authorities. I am asking my officials to pursue this possibility with yours. But this need not affect the wording of your announcement.

I am also content with the text of your announcement, subject to three points:-

Paragraph 3, second sentence: amend to read:-

"Local authority expenditure is a large component in the total of public spending."

Paragraph 4, first line: insert "and borrowing" after "expenditure";

and

Paragraph 4: replace second sentence by:-

"There would be obvious advantages in introducing changes in the arrangements for current and capital together, so that interactions between the two can be allowed for as fully as possible."

I am copying this letter to the Prime Minister, Willie Whitelaw, other colleagues on E(LA), First Parliamentary Counsel and Sir Robert Armstrong.

Yours etc,
JH

JOHN MacGREGOR



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PRIVY COUNCIL OFFICE
WHITEHALL, LONDON SW1A 2AT

9 October 1986

Dear Nicholas

NBRM

LOCAL AUTHORITY CAPITAL CONTROLS

Thank you for your letter of 30 September with the draft of your proposed announcement of our decision not to introduce comprehensive legislation next Session, and with your proposals for minor changes to the system to be included in the Local Government Bill. *will request if required*

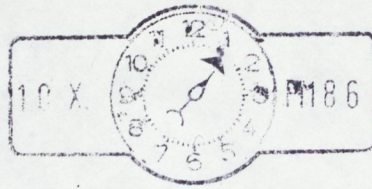
Kenneth Baker and John MacGregor have suggested slight changes to the proposals on back-to-back schemes and on revenue bill powers, and no doubt you will wish to consider these. But I understand that your announcement can be modified without difficulty so as to keep open these issues, and on that basis you may take it that you have the agreement of E(LA) to write to the local authorities next week. Wyn Roberts suggested an announcement in England and Wales on 15 October, and I would see no objection to that.

I am sending a copy of this letter to the Prime Minister, members of E(LA), First Parliamentary Counsel and Sir Robert Armstrong.

The Rt Hon Nicholas Ridley MP

RESTRICTED

LOCAL GOVT
RELATIONS



PT 30

CONFIDENTIAL

ccBG



DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

The Rt Hon John MacGregor OBE MP
Chief Secretary to the Treasury
HM Treasury
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

9 October 1986

NBM

Dear Sir

LOCAL AUTHORITY CAPITAL CONTROLS

I have seen the correspondence between Willie Whitelaw and Nicholas Ridley about the proposed announcement on the capital controls system.

I have no comment on the text of Nicholas' proposed letter to the local authority associations except to say that I hope you will agree that it should include the minor concession on Government compensation payments, to apply from 1987/88. Peter Bottomley has already written to you, on 30 April, to explain the difficulties the present anomaly has been creating in our relations with local authorities from whom we have to buy land for the roads programme. We have not pressed you on this point because we had been expecting a major reform of the present system. However, the changes planned for 1986/87 do involve a significant tightening of control which should enable us to afford this very minor and wholly reasonable concession.

I am sending copies of this letter to the Prime Minister, colleagues on E(LA), the First Parliamentary Counsel and Sir Robert Armstrong.

John Moore

JOHN MOORE

CONFIDENTIAL





DEPARTMENT OF EDUCATION AND SCIENCE
ELIZABETH HOUSE YORK ROAD LONDON SE1 7PH
TELEPHONE 01-934 9000

FROM THE SECRETARY OF STATE

The Rt Hon Nicholas Ridley MP
Secretary of State for the
Environment
2 Marsham Street
London SW1P 3EB

8 October 1986

Dr. M. T.

LOCAL AUTHORITY CAPITAL CONTROLS

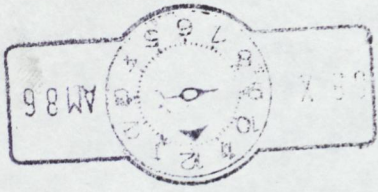
Thank you for sending me a copy of your letter of 30 September to the Lord President.

I have one small comment on your proposals. I believe that it would increase their appeal to local authorities if - as has been suggested in response to the Consultation Paper - we extended the concession on back-to-back schemes to include all such schemes where purchase and sale take place within 12 months, rather than restricting it to those completed within a single financial year. I am content with all of your remaining proposals.

I am copying this letter to the Prime Minister, members of E(LA), the First Parliamentary Counsel and to Sir Robert Armstrong.

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Local Govt

Relations

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CBB



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Oddi wrth yr Is-Ysgrifennydd Senneddol

WELSH OFFICE
GWYDYR HOUSE
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Tel. 01-233 3000 (Switchboard)
01-233 7448 (Direct Line)

From The Parliamentary Under-Secretary

7 October 1986

NB PT7

Dea Iard Pwysidant,

In Nicholas Edwards' absence I am responding to your letter of 19 September and Nicholas Ridley's of 30 September about local authority capital controls. I am content with what is now proposed.

I particularly welcome the proposals for back to back schemes and Government CPOs. These are changes which the local authority associations in Wales have been seeking for some time. Nicholas has indicated that we wish to consider further the precise form of deferred purchase exemption and some other minor proposals which could be included in amending regulations. I see no reason why these issues should not be pursued at official level and note that Nicholas' draft allows for this.

The proposed timing for the announcement of these plans suits us well. A meeting of the Welsh Consultative Committee on Local Government Finance is set for 15 October and will discuss progress on the Green Paper proposals. I hope that you and Nicholas Ridley will agree that it would be particularly helpful if our plans for improving the present capital control system could be announced on that day for both England and Wales.

/ I am copying this letter to the Prime Minister, colleagues on E(LA), the First Parliamentary Counsel and Sir Robert Armstrong.

*Ysgrifennu'n ddiogel
Duan Mair*

WYN ROBERTS

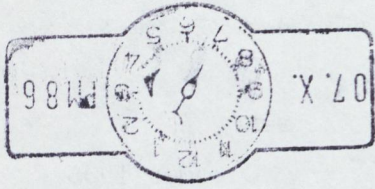
(Dictated by Mr Roberts and signed in his absence)

The Rt Hon Viscount Whitelaw CH MC
Lord President of the Council
Privy Council Office
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Local Govt
Relations

PT 30

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PRIVY COUNCIL OFFICE
WHITEHALL, LONDON SW1A 2AT

NBR

19 September 1986

Dear Secretary of State

At the meeting on 16 September, E(LA) were unable to reach a decision on where the balance of advantage lay between introducing reform of the local authority capital expenditure control system in 1986/87 and deferring it to the next Parliament, and agreed that I should discuss the matter further with the Prime Minister. I am sure that you and E(LA) colleagues will agree that our discussion had very clearly exposed the nature of the choices that faced us.

I am now writing to tell you that I reported the E(LA) discussion to the Prime Minister yesterday and that we agreed that the balance of advantage was against introducing comprehensive reform in this area in the next Session.

It is now settled that E(LA)'s decision on leasing can be effected by subordinate legislation. I take it, therefore, that the only significant provisions in this field that you wish to include in the Local Government Bill now being prepared are those on advance and deferred purchase arrangements that you undertook to introduce in your statement of 22 July. It may be, however, that you have some further minor suggestions to make and if so I should be grateful if you would let me know.

As we noted at E(LA), there is now the question of how these decisions should be presented, and I know that you are giving your mind to that. If I can be of any help please do not hesitate to let me know.

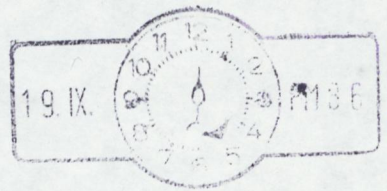
I am sending copies of this letter to the Prime Minister, colleagues on E(LA), the First Parliamentary Counsel and to Sir Robert Armstrong.

Yours sincerely

N. J. S. Gibbons

(Approved by the Lord President
and signed in his absence)

The Rt Hon Nicholas Ridley MP



LOCAL AUTHORITY CAPITAL CONTROL SYSTEM

Lord Whitelaw is coming to see you tomorrow morning about E(LA)'s conclusions on Nicholas Ridley's proposals for a new local authority capital expenditure control system. It has already been agreed to bring leasing within the control system in 1987/88 by secondary legislation though a decision has yet to be announced.

Under the present capital control system local authorities are allowed to spend on capital in any year:

- their allocations plus 10% 'tolerance'
- a proportion (20% for housing, 30% for other services) of the sum of the capital receipts generated in the year and capital receipts from past years not already used to justify spending;
- 'non-prescribed' expenditure eg leasing (although as noted above it has been decided that leasing will not justify additional spending from 1987-88 onwards).

The problems with this system are that:

- spending power from receipts and 'non-prescribed' expenditure is increasing year by year thereby leaving less and less room for allocations. This means regular bad publicity for the Government when it announces a total for allocations lower than the previous year;

- this makes it increasingly difficult to direct spending power where it is needed. Under the present legislation the Secretary of State may not take account of spending power from receipts when distributing allocations. Since in general (although there are exceptions such as Wandsworth) areas that need to spend (particularly on run-down housing stock) are not well endowed with receipts, the Government is also increasingly vulnerable to the charge that it is failing to deal with the problems of the inner cities.

There is a further problem in 1987-88 because the Government has given a commitment that allocations will be at least 80% of the 1985-86 level. This commitment can only be met by an increase in public expenditure which (in return for the leasing change) the Treasury have now conceded. But there is no commitment of this kind for 1988-89 and later years.

Nicholas Ridley has proposed a new system designed to overcome the disadvantages of the present system. It includes a number of changes:

- a. All capital expenditure will in future be 'prescribed' (ie controlled). Non-prescribed spending power disappears;
- b. The cash from receipts which still justify spending power may already have been used to redeem debt. Those receipts have already in commonsense terms been used. Under the new system they will not justify additional spending. This reduces the total of accumulated receipts by £3 billion.
- c. In order to reduce receipts justified spending power further and make it easier to control expenditure receipts will only count from the year after they arise. This reduces receipts available by £2 billion.

- d. In order to maintain an incentive to generate receipts and ensure that the total of receipts starts to diminish the proportion of receipts that authorities are allowed to spend will increase, probably to about 40%, and local authorities will be required to use up spending power from receipts before they use their allocations. At present, authorities may not need all the spending power available, many carry forward unused spending power from receipts into later years;

- e. in order to distribute allocations to where the need is greatest, the Secretary of State will be able to take account of spending power from receipts. The working assumption is that he will take account of 50% of such spending power. But he need not take account of any of it. It is this provision which will make the main contribution to changing the distribution of resources;

- f. as a quid pro quo for loss of other spending power, authorities will be able to add to capital spending power from revenue (including rents). It is hoped that the pressure on current spending (particularly when the community charge is in place) will keep this within bounds but there will be a reserve power to limit such spending. These pressures will not bite on rents and John MacGregor is insisting that the housing benefit cost of the charge should be met in full by a reduction in provision for local authority capital.

E(LA) agreed on Tuesday that the new system is desirable in principle. But many of them expressed doubts about the political wisdom of proceeding such a measure in an election year for the following reasons:

- it was not clear that the Bill could be ready in time to guarantee its passage before the summer recess next year;
- some of the key features of the Bill, particularly the reduction in the receipts that could be used to justify additional spending, might not survive passage through Parliament.
- the main effect would be to transfer resources from the Shires (which would be criticised by the Government's supporters) to the Cities (for which the Government would attract no credit).

The meeting concluded that Lord Whitelaw should discuss the position with you. We consider that the balance of advantage is against legislation in an election year. We share the reservations above although we accept the case for a change in the longer term. Provided the leasing change goes ahead the legislation is not needed to control public expenditure in 1988-89 as the 80% commitment no longer applies. The main effect of the new system therefore is to reduce spending power for some authorities and increase it for others. The distribution of gainers and losers is unattractive (based on a DoE estimate), as follows:

	<u>Gainers</u>	<u>Losers</u>
Shire Districts, Counties and Outer London	129	226
Metropolitan Districts and Inner London	29	19

Inner city authorities are partly to blame for both their lack of receipts and the condition of their stock (compare Lambeth and Wandsworth). In our view the answer is not to increase their spending power since this does not deal with the fundamental problems of poor management and monolithic ownership of rented housing.

A more fruitful approach is likely to be the transfer of run-down estates to private sector housing associations at a price reflecting the cost of ~~to~~ borrowing to finance renovation. Provided there is an appropriate regime of rent control (which in some cases means rents above 'fair' rent levels) this is a practicable way not only of renovating the stock without a call on public funds but also of encouraging efficient management and diversifying tenure.

PJS

PETER STREDDER