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P.01416

PRIME MINISTER

Public Expenditure Survey 1984

You are likely to be holding a number of meetings over the next few days to consider the remaining stages of the Public Expenditure Survey in the light of the work done so far by the Ministerial Group on Public Expenditure (MISC 106): you have already arranged to see the Foreign and Commonwealth Secretary at 4:45pm tomorrow.

2. As background for those meetings the Secretariat of MISC 106 have prepared the attached notes setting out the position reached by the Group so far. I am afraid that it is inevitably a snapshot, taken at mid-day today, with a good many parts of the picture still not sharply focused; but I hope that it will help.

3. At the very least it shows clearly that even though the recommendations which the Group have either agreed with or put to the spending Ministers concerned are bound to be regarded as very severe, the remaining task is formidable. The Group will almost certainly be putting recommendations to the Secretary of State for the Environment on his programmes which he will regard as extremely, perhaps intolerably, severe; and there are big problems, of which you are well aware, in imposing large savings on the gas and electricity industries. Every pound conceded makes the Group's task more severe, not only as a matter of arithmetic but also by making it harder to persuade other spending Ministers that they have been fairly treated.



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4. I am afraid that there is also an unpleasant further complication. The figuring in the note takes account of a substantial increase in the provision for local authority current expenditure in all three years of the survey. Even so, some Ministers do not think that the increased totals for 1986-87 and 1987-88 make sufficient provision for the services for which they are responsible. The Secretary of State for Education and Science, in particular, has proposed that the figures should be increased by £200 million in 1986-87 and £425 million in 1987-88. The Lord President of the Council is holding a meeting of Ministers on Thursday 1 November to try to resolve the issues.

5. I am sending a copy of this minute, with attachments, to the Lord President of the Council and the Chief Secretary, Treasury, since they will be involved in your meetings.

P L GREGSON
Cabinet Office.
30 October, 1984

Attachments:



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MINISTERIAL GROUP ON PUBLIC EXPENDITURE (MISC 106)
PRESENT STATE OF PLAY

Note by the Secretariat of MISC 106

This note sets out the state of play after the first two weeks' work of MISC 106.

INITIAL POSITION

2. Before the Group started work the Chief Secretary, Treasury had reached agreement with the spending Ministers concerned on all major programmes except Defence; health and personal social services (HPSS); social security; housing, other environmental services and the Urban Programme; and the external financing limits (EFLs) of the gas and electricity industries. The Chief Secretary also reached agreement outside the Group with the Chancellor of the Duchy of Lancaster on the Arts and Libraries programme.

3. Within the HPSS and the social security programmes there were large and virtually unavoidable increases in expenditure due to changed economic assumptions, greater take-up of benefits, and other factors.

4. As a result, in order to meet the Cabinet's objective of holding to the agreed public expenditure planning totals the Group faced the task of finding further savings within the programmes mentioned in the first sentence of paragraph 2 above of about £1.1 billion in 1985-86, £1.4 billion in 1986-87, and £1.9 billion in 1987-88.

AGREEMENT ON SOCIAL SERVICES

5. The Group have agreed with the Secretary of State for Social Services that they should jointly recommend to the



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Cabinet a package of savings on his programmes, including those which he had identified in bilateral discussions with the Chief Secretary. On health and personal social services the Secretary of State will find total savings of (all figures in £ million):

<u>1985-86</u>	<u>1986-87</u>	<u>1987-88</u>
- 105	- 160	- 216

mainly from higher prescription and dental charges and extending the 'grey list' of items in respect of which doctors will be entitled to prescribe under the National Health Service only generic, not named proprietary, drugs.

6. On social security the Secretary of State will find total savings of:

- 218	- 585	- 735
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by a combination of changes in minor benefits, savings 'on account' of the recommendations expected to emerge from the current programme of social security reviews, and extending the payment by employers of statutory sick pay from 8 to 28 weeks. The implications of the last of these for employers' National Insurance contributions is under discussion between the Secretary of State and Treasury Ministers.

REMAINING PROGRAMMES

7. As a result of all this, the task facing the Group is to find net savings from the remaining programmes of £0.9 billion in 1985-86, nearly £1.0 billion in 1986-87 and £1.3 billion in 1987-88. Paragraphs 8 to 17 below describe the present situation on those programmes. The figures are collected in the table annexed to this note.

(A)
Total of lines
I + II + III in
the table.



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(a) Defence

8. The Government is publicly committed to plan to implement the NATO aim of real increases in defence spending of 3 per cent a year up to 1985-86. The Secretary of State for Defence has indicated that an addition to baseline of £105 million in that year would discharge that commitment; the Group are minded to recommend that the addition should be made, as part of an agreed joint recommendation on the defence programme.

9. For later years, the Group have indicated that they are minded to recommend no change on baseline, apart from an agreed addition of £300 million in 1987-88 in respect of the Falkland Islands.

10. The Secretary of State for Defence has pointed out that this will appear to entail a reduction in the real value of the Defence Budget (excluding expenditure on the Falklands). He has suggested that it would be desirable to state, when the figures are published, that they are subject to review. The Group have proposed a possible form of words for this purpose.

11. The Secretary of State for Defence has not yet responded to the Group's proposals on either the figures or the form of words.

(b) FCO (including ODA)

12. The Group are minded to recommend no change on baseline. The position has been fully reported in the minute of 25 October from the Lord President of the Council to the Prime Minister.

(c) Agriculture

13. The Group have proposed reductions of

- 65 - 115 - 150



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The Lord President
will indicate
the Jopling
response if
Cabinet imposes
these cuts.

from reductions in capital grants and in support for agricultural research and development and the Agricultural Development and Advisory Service (ADAS). The Minister of Agriculture, Fisheries and Food has not yet replied.

Other Programmes

14. The Group have reached only a preliminary stage in their consideration of the environment programmes and the gas and electricity industries.

15. On the Urban Programme, the Group have indicated to the Secretary of State for the Environment that they are minded to recommend reductions of

- 30 - 55 - 55

The Secretary of State has not yet replied.

16. On housing and other environmental services, the Group have not yet formulated proposals. But they recognise that in order to reach the planning totals agreed by the Cabinet they will have to make very substantial reductions, particularly on housing - of the order of several hundreds of millions a year. The reductions are likely to fall mainly on home improvement grants and new building by public authorities.

17. The gas and electricity industries are seeking increases in their EFLs amounting to:

+ 183 + 535 + 959

The Secretary of State for Energy is urgently exploring with the industries how far these bids could be reduced by cost savings and price increases. He has stated that his aim will be to identify reductions of the order of £2.2 billion over the three years. The Group will decide



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their recommendations to the Cabinet when the Secretary of State for Energy reports the outcome of his discussions with the industries tomorrow morning.

OVERALL POSITION

18. The overall position is thus that if the spending Ministers concerned accept the Group's recommendations on defence, FCO programmes and agriculture it will still be necessary to find nearly £1.0 billion in 1985-86, nearly £0.9 billion in 1986-87, and nearly £1.5 billion in 1987-88, from the environment programmes, and the gas and electricity industries.

Total (B)

19. To help Ministers in considering how this might be done, section V of the attached table sets out

(i) Possible proposals on the environment programmes, drawing on the Group's preliminary discussions. They are, of course, purely illustrative and not in any way intended to prejudge the Group's conclusions.

(ii) For the gas and electricity industries, the bids from the industries; reductions of the size at which the Secretary of State for Energy has said that he will aim, distributed between years in a stylized way; and the additional reductions required to meet the target agreed by E(A) in July.

20. To the extent that any programme is increased beyond the figures recommended by the Group the overall situation self-evidently becomes more difficult.

Cabinet Office.

30 October, 1984

MISC 106: CURRENT STATE OF PLAY

The figures below, unless otherwise indicated, show changes on baseline, and are in £ million.

	<u>1985-86</u>		<u>1986-87</u>		<u>1987-88</u>	
I. Agreed/expected changes on programmes not considered by MISC 106	+ 215		+ 407		- 592	
II. Agreed or virtually unavoidable additions on						
- HPSS	+ 303		+ 446		+ 813	
- Social Security	+ 737		+ 881		+2062	
III. Agreed recommendations on						
- HPSS	- 105		- 160		- 216	
- Social security	- 218		- 585		- 735	
TOTAL (A) to be offset by savings on programmes listed below)	+ 932		+ 989		+1332	
IV. Programmes on which MISC 106 have agreed recommendations	<i>MISC</i> (a)	<i>Ministers</i> (b)	<i>MISC</i> (a)	<i>Ministers</i> (b)	<i>MISC</i> (a)	<i>Ministers</i> (b)
- Defence	+ 105	+ 105	-	+ 145	+ 300	+ 533
- ODA/FCO	-	+ 40	-	+ 68	-	+ 79
- Agriculture	- 65	- 19	- 115	- 24	- 150	- 30
TOTAL (B) Sections I-IV (ie. remaining gap to be offset)	+ 972	+1058	+ 874	+1178	+1482	+1914
V. Other programmes						
(i) Housing						
- Gross expenditure	[- 227] + 403		[- 302] + 468		[- 430] + 480	
- receipts (increase-/decrease+)	- 300 - 300		[- 100] - 100		[-] -	
(ii) Other environmental services (OES)	- 29 + 43		+ 9 + 105		- + 94	
(iii) Urban Programme	- 30 -		- 55 -		- 55 -	

As noted in the main text the Group have not yet formulated proposals on either housing or OES. In particular, their recommendations on the housing programme are likely to be influenced by the expected level of receipts in 1986-87 and 1987-88, which are still under discussion between the Treasury and the Department of the Environment. The figures above are therefore illustrative, and based on the Secretariat's interpretation of the tenor of the Group's discussions. They imply the following totals for sections I to V.

+ 386 +1204 | + 426 +1651 | + 997 +2488

Memorandum item

Gas and electricity

Bids from the industries	+ 183	+ 535	+ 959
£2.2 billion reductions on bids	- 330	- 735	-1135
Implied reduction on baseline	- 147	- 200	- 176
Further reductions required to meet E(A) target for all nationalised industries	- 253	- 400	- 824
	- 400	- 600	-1000

NOTES

1. Column (a) shows the proposals made by the Group to spending Ministers;
Column (b) shows the proposals of spending Ministers; these do not all necessarily represent the final position of the spending Minister concerned.
2. The figures for gas and electricity are at a preliminary stage of discussion with the Group. They are therefore not fully comparable with the other figures in the table and are therefore shown as a memorandum item. A fuller explanation is given in the main text.
3. The table does not include the potential effects on territorial blocks budgets. These might be

+ 15 - 60 - 10