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PREM 19/1192

~~SECRET~~

CONFIDENTIAL FILING.

Public Expenditure and Cash Limits

ECONOMIC
POLICY

At 1: May 1979.

At 28: September 1984.

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
11.9.84							
13.9.84							
24.9.84							
28.7.84							
1.10.84							
5.10.84							
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12.10.84							
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18.10.84							
19.10.84							
20.10.84							
15.10.84							
<p>PREM 19/1192</p>							
<p>PART ENDS.</p>							

PART 28 ends:-

MISC 106(84) Stm Mtg 15/10/84

PART 29 begins:-

CST to NIO 19/10/84

Subject

SECRET



file SKH

31

cc Master

10 DOWNING STREET

From the Private Secretary

18 October 1984

Territorial Expenditure

When your Secretary of State met the Prime Minister today he expressed his misgivings about the proposed study of public expenditure in the territories. The Prime Minister noted his views. It was agreed that she would convene a meeting of territorial ministers, the Lord President and the Chief Secretary to consider whether such a study should be conducted and if so, what its terms of reference should be and how it should be carried out.

I will be in touch to arrange the meeting and the preparation of papers.

I am copying this letter to Janet Lewis-Jones (Lord President's Office), Colin Jones (Welsh Office), Graham Sandiford (Northern Ireland Office), Richard Broadbent (Chief Secretary's Office), and Richard Hatfield (Cabinet Office).

Andrew Turnbull

John Graham Esq
Scottish Office

SECRET

CST.

PRIME MINISTERMEETING WITH SECRETARY OF STATE FOR SCOTLAND

In addition to the Chairmanship of the Lothian Health Board the Secretary of State for Scotland is likely to raise the proposed study of needs assessment in the territories. You will remember that the Chief Secretary spoke to you about this before suggesting such a study ~~with~~^{to} the territorial Ministers. Progress has been slow and to date Mr. Hurd has agreed in principle to such a study provided the other territories agree (he is arguing that it should take until eternity to be completed). Mr. Edwards is likely to agree as he hopes it will demonstrate that Wales is hard done by.

Mr. Younger is still objecting to the principle of such a study. He feels even knowledge of its existence would be very controversial and that if, as he no doubt ~~feels~~^{fears}, it demonstrated that Scotland is being over-provided for, he would find it difficult to secure acceptance of the required public expenditure cuts.

I suggest you do not enter into substantive discussion with him but offer to hold a meeting with the Lord President, Chief Secretary and the territorial Ministers to consider whether to conduct such a study and, if so, how it should be handled.

AT

17 October, 1984

NBSM AT 17/10



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R J Broadbent Esq
Private Secretary to the Chief Secretary
to the Treasury
Treasury Chambers
Parliament Street
LONDON
SW1P 3AC

16 October 1984

Dear Richard,

will register if required

You sent me a note of the Chief Secretary's meeting with my Secretary of State on 1 October about Public Expenditure.

We are content with the note, except for one point. We do not accept that it was agreed that the further study on the Northern Ireland Block should have a deadline of June 1985. As was explained at the bilateral, we do not believe that a thoroughgoing and worthwhile exercise can be completed in time to inform the work on the 1985 Survey. Our reasons for holding this view were fully explained at the bilateral and appeared to be understood by the Chief Secretary.

We consider that the discussion would be more accurately reflected by replacing para 9(iii) with the following:-

"Northern Ireland would participate in further work on needs assessment provided that the other territorial Departments did so and there was access to appropriate information from Whitehall Departments. Officials should aim to report by June 1985 but it was recognised that the thoroughgoing exercise which was required might well take longer to complete. The modalities to be discussed in the first place between officials."

I should be grateful if you would adjust the note of the meeting accordingly. A copy of this letter goes to Andrew Turnbull (No 10).

Yours ever,

Graham Sandiford

G K SANDIFORD

CONFIDENTIAL

MMcC



10 DOWNING STREET

Prime Minister ①

The Treasury has pitched
its assumptions as
optimistically as it could.

I understand that the
addition to public expenditure
of adopting these assumptions
is only £150 million, rather
than be £500 million mentioned
at MISC 106.

Content?

AT

17/10

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S E C R E T

Blueway

27^A

FROM : S A ROBSON
DATE : 16 OCTOBER 1984

PS/CHIEF SECRETARY

c.c. Chancellor of Exchequer
Mr Bailey
Mr Monck
Mr Burgner
Mr Scholar
Mr Webb
Dr Bird

MISC 106 : GAS AND ELECTRICITY

Attached is the full briefing for the meeting on October 19.

2. It consists of my submission of 12 October giving a general overview plus detailed supporting material.

3. Could you please circulate to MISC 106 members. I am dealing separately with No 10 and the Cabinet Office.

SAR

S A ROBSON

S E C R E T

CONFIDENTIAL

FROM : S A ROBSON
DATE : 12 OCTOBER 1984

Chief Secretary

c.c. Chancellor of Exchequer
Mr Bailey
Mr Monck
Mr Burgner
Mr Scholar
Mr Webb
Dir Bird

MISC 106 : GAS AND ELECTRICITY

This is a general brief for the meeting on October 19. Detailed briefing on the elements of our approach is attached.

2. The position is basically as follows. In order to meet the E(A) target for nationalised industries you have asked Mr Walker to produce savings on gas and electricity (compared to baseline) to (£m).

1985-86	1986-87	1987-88
-400	-600	-1000

He has offered nothing so far and has merely endorsed the industries bids which together total (£m) :

+183	+535	+959
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This means the gap is

585	1135	1959
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These figures are in paragraph 1 of the MISC 106 paper.

3. Your proposals for closing this gap can be described as follows :

ESI

- Financial target rising to 4½% over next 3 years; averaging 3.6% (para 5 of paper)	-250	-400	-700
- Savings on capital expenditure, asset sales and efficiency (para 5 of paper)	-175	-375	-450

	1985-86	1986-87	1987-88
<u>BGC</u>			
- savings on capital expenditure and in other areas (para 8 of paper)	-70	-150	-260
- average 4 per cent real price increase (para 6 of paper)	-220	-440	-774

If these measures were all agreed, they would more than cover the gap. Annex I of the detailed brief covers BGC and Annex 2 the ESI. Each Annex has a contents page.

4. The key points to make are :

- (a) the savings on capital expenditure and in other areas are relatively small for both gas and electricity and are no more than an attempt to substitute for the absence of market pressures for efficiency. For BGC the savings are equivalent to 1 per cent of costs in 1985-86 rising to 3 per cent in 1987-88. For the ESI, the cuts build up about 8 per cent of costs.
- (b) the ESI financial target is well below returns in the private sector (currently about 8½ per cent). It could be achieved with prices rising little or no faster than inflation (i.e. 4-5 per cent) if the industry really went for the cost savings open to it in the way a private sector company would.
- (c) gas is underpriced and something around 20-25 per cent. This is based on figures from BGC and the department. You are only looking for to close about half this gap.

5. Mr Walker may use the following.

Baseline should be increased on account of corporation tax - this was considered by E(A) and rejected. The target was set on the existing baseline. Commentators would see messing with the baseline as a pure "fiddle". In any case our savings are justified on merit regardless of the treatment of corporation tax. Private sector companies have to trim their affairs to meet their CT payments; so should nationalised industries.

Treasury totally unrealistic- not so. Mr Walker's officials have been consistently unable to rebut our proposals. They have latterly refused to enter into any dialogue about them.

Proposals would upset electricity unions during miners strike- this is pure scare tactics. The unions have shown themselves wholly responsible in relation to exploiting the miners strike and in relation to increasing the efficiency of the electricity industry in the past.

Treasury proposals lead industries into huge profits - these industries have vast capital assets (ESI over £35bn, BGC over £14bn), their returns would not be large. ESI at $3\frac{1}{2}$ per cent would be well below most large public sector companies (e.g. BP at 8.7 per cent, ICI at 6.8 per cent, Hanson Trust at 18 per cent) BGC profits might rise to 8-9 per cent by 1987-88, unless the money were taken out using the gas levy.

Gas levy increase would not help public expenditure. Formally correct but it would help PSBR. The position on the gas levy could be carefully spelt out in public expenditure presentation - as it was in the main table of the 1982 White Paper.

BGC have a financial target of 4 per cent - true but when this was set Treasury and Energy Ministers specifically agreed that it was subject to review of BGC's prices.

Price increases fuel inflation - It is not the Government's policy to tackle inflation by holding down nationalised industry prices. The increase in gas price would add only about 0.3 percentage points to the RPI by 1987-88.

International comparisons - Domestic gas prices are the lowest in Europe alongside the Dutch. Prices in France and Germany are 40-50 per cent higher. Industrial gas prices are 20 per cent below Continental levels. On electricity, industrial prices are in line with the Continental, apart from France with its large nuclear generating capacity.

S. A. Robson
S A ROBSON

BRITISH GAS CORPORATION

The Treasury's proposals for savings are made up as follows (£ million) :

A. Savings on gas purchase, capital investment

asset sales and efficiency	1985-86	1986-87	1987-88
1. reducing surplus gas supplies	-25	-45	-115
2. phase out R&D into SNG	-10	-20	- 40
3. increased land sales	-5	-10	- 10
4. reduced capital expenditure	0	-40	- 55
5. reduced working capital	-20	-30	- 40
6. lower trading costs	-10	-20	- 30
Total after adjustment for tax consequences	-70	-150	-260

B. Gas prices

7. Gas price increases	-220	-440	-774
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Detailed notes on each are set out in the following sections.

S E C R E T

- BGC are loathe to supply relevant facts and figures. A Wood Mackenzie analysis confirmed that BGC will have surplus supplies into the late 1990s. Wood Mackenzie also show that this surplus gas will be found in storage (i.e. Rough) in BGC's own fields (i.e Morecambe) and third party peak supplies. These are the areas where savings are proposed.

- There is evidence that BGC is not making full use of its ability under interruptible supply contracts to cut off supply to industrial consumers at times of winter peak. The essence of these contracts is that customers accept this risk and get correspondingly cheaper gas. As BGC is not in practice cutting these supplies to help meet peak times of demand it means these consumers are getting gas on the cheap (quite apart from the question of economic pricing). BGC should exploit its interruptible contracts to the full.

Defensive

Should not confuse peak demand with annual demand where no surplus is expected
Proposals aimed at peak demand and gas purchased but not for sale in IFR period. The proposals would in no way jeopardise BGC's ability to match annual supply and annual demand.

BGC nearly ran out of gas in 1981-82. Could happen again. Statutory duty to supply
BGC's forecasts show peak surpluses much higher in 1987-88 than ever expected in 1981-82. Even after Treasury proposals, BGC will have an unprecedented margin to meet demand, including demand in severe winter .

Surpluses needed in case Frigg gas ends prematurely

Already taken account of in BGC's contingency margin (the "overall risk adjustment",) which would be preserved under Treasury proposal. Proposals are aimed at surpluses in excess of what is needed for insurance.

S E C R E T

2. Phase out research into substitute natural gas (SNG)

	1985-86	1986-87	1987-88	£ million
Savings proposed	-10	-20	-40	

BGC are currently spending around £30 million a year on research into the production of synthetic gas from coal. In 1987-88 they want a further £10 million for a design study for a prototype full-scale SNG plant. And they are retaining around sites in cities (some hundreds of acres) for ultimate use as SNG plants. Our proposal is to run down the research work by 1987-88. SNG is seen as one possible replacement for UKCS natural gas.

Points to Make

- The increase in forecast North Sea reserves and the prospect of higher levels of sales of gas by the USSR to Western Europe means that the time when SNG is needed is receding. Sir Denis Rooke has recently been quoted as saying that the UK will not need to depend on SNG before 2050. As a result this R&D is far ahead of its time. It needs shelving.
- BGC want to complete the present phase of R&D before putting it on the shelf. Between now and 1990 this will cost around £200 million. It is unlikely that the technology will stand still. The research done in this period will almost certainly be out of date by the time it is needed. It is money wanted.
- if possible the private sector should build and run SNG plant. There is already some interest by oil companies in the US and, when the time is right, interest should also emerge in this country. It would be wrong to give BGC such a lead in this technology at the taxpayers expense that it can effectively "shut out" the private sector.

Defensive

ACORD endorsed this programme as the most economic way of preserving the considerable technological advances made so far

ACORD (Mr Walker's advisory group of scientists) are concerned only solely with the science; not with the economics of SNG, nor with whether it is right for a nationalised industry to do the work. If the work is worthwhile, it will be picked up by the private sector.

S E C R E T

To stop the programme now would risk all future benefits

Not so. There are plenty of examples of a technology being put on ice for a period and without detriment to the benefit (e.g. conversion of coal into petrol; vulcanised rubber). In any case the work BGC does today will be out of date when SNG needed.

S E C R E T

3. Sale of Land

	1985-86	1986-87	1987-88	(£ million)
Savings proposed :	-5	-10	-10	

BGC currently has holdings of over 1700 acres of unused and underused land. the latest DOE register showed that this had increased recently. BGC is also planning to buy a further 1000 acres. Ending work on SNG (2. above) should release further sites.

Points to Make

- Nationalised Industires are source of the largest holders of unused land. Must keep up pressure for disposal. Manifesto said that Government would increase efforts to dispose of spare land.

- BGC currently hold around 25 sites for future SNG production. Even if SNG work were to continue, wrong to hold sites for up to 50 years. Assuming an end to SNG, some at least of the sites could be sold quickly.

Defensive

Sites are often old town gas sites and are chemically contaminated.

Cost of relamation is high.

Recognise difficulties, but release of SNG sites provides opportunity for a new market. Must be scope for increased receipts. There will be buyers if the price is right.

4. Reduce capital expenditure

	1985-86	1986-87	1987-88	(£ million)
Savings proposed :	-	-40	-55	
of which :				
exploration	-	-20	-40	
onshore	-	-20	-15	

Points to Make

- BGC's forecast expenditure on exploration for gas and development of gas fields increases markedly towards the end of the IFR period (up from £41m in 1984-85 to £146m in 1987-88). Ministers are looking for BGC to divert itself of the bulk of its interests in gas production and exploration. This activity should be left to private sector. BGC could sell its interests in these fields.

- The savings proposed onshore are small - about 5 per cent of programme - despite the fact BGC has offered no clear explanation for its investment plans. Why, for example, does it want to spend £100 million a year on capital expenditure in an area called "administration and general"?

- Proposals not excessive compared to planned capital investment programme of around £700m a year.

Defensive

Programme already tight. Bid represents savings on baseline and lower than historical level of investment

Previous level of capital spend contained substantial provision for Morecambe and Rough projects (over £2bn in total). This expenditure has in the event taken place quicker than expected and so fell in 1983-84 with consequent reductions in the IFR period. This is merely a timing change, not a change in the size of the programme.

Investment meets appraisal guidelines

We have no evidence that BGC's investment programme meets 5 per cent RRR. Indeed return on assets forecast to decline to below 3 per cent by 1988-89. Suggests that investment is not producing 5 per cent return. BGC produced no material on nature and justification for, programme - despite requests.

S E C R E T

Exploration expenditure not within BGC's control

We have taken into account the degree of control BGC has over exploration expenditure in the proposals for savings. In any case BGC should be divesting itself of its offshore involvement; and this would itself reduce size of investment programme (as well as producing receipts from the sale).

S E C R E T

5. Reduce Working Capital Requirements

	1985-86	1986-87	1987-88	(£ million)
Savings proposed :	-20	-30	-40	

This is made up by a £10m a year reduction in stocks of working materials (other than gas), a squeeze on debtors and reducing the forecast decline on gas creditors.

Points to Make

- Need to keep up pressure on working capital. BGC's want to see working capital increasing from £900 million to £1.8 billion over the IFR period.
- Reductions sought far from excessive. Stocks level of materials rose significantly in 1983-84 and BGC propose holding to this increased level.

DefensiveReducing stocks would mean a poorer service

Rationalisation of unnecessary store facilities, computerisation of records and other efficiency improvements should mean that there is scope for making savings through improved efficiency, rather than reduced service.

Debtors are planned to decline over IFR period. Not possible to improve further

Relationship between debtors and turnover remains virtually constant over period. BGC take pessimistic view of the economy over the next few years and so are too pessimistic about customers' ability to pay.

Reduction in gas creditors results from changing pattern of gas supplies

Accept this has some effect, but does not explain full change in forecast figures. BGC failed to produce any sensible explanation. Must be scope for improvement.

6. Reduce Trading Costs

	1985-86	1986-87	1987-88	(£ million)
Savings proposed :	-10	-20	-30	

BGC is on target to achieve its performance aim of a 12 per cent real reduction in unit net trading costs between 1983-84 and 1986-87 compared with 1982-83. The savings proposed represent a further small push for efficiency. About half the savings of 12 per cent were achieved in 1983-84 - leaving 3 years to get the other 6 per cent.

Points to Make

- Important to keep up the pressure for efficiency gains and improvement in productivity. BGC's Corporate Plan this year contained no information on efficiency indicators.
- Accept that BGC already achieving significant improvements in net trading costs. But about half of the savings required to meet performance aim were achieved in the first year. This suggests that the performance aim will not be tight enough discipline in the later years. The Select Committee on Energy drew attention to this.
- BGC's net trading costs are about £2 billion. Savings sought only represent a further $\frac{1}{2}$ per cent per year improvement.
- BGC's plan show an unexplained 19 per cent rising in net trading costs (other than wages) between 1984-85 (£731m) and 1985-86 (£870m).

DefensiveShould not force BGC to exceed performance aim

Performance aim is a target not a ceiling. If further efficiency savings are available, would clearly be right to go for them.

7. Increase Gas Prices

	1985-86	1986-87	1987-88	(£ million)
Savings proposed :	-220	-440	-774	

BGC plans to increase tariffs roughly in line with the rate of inflation over the IFR period. This compares with their view last November (when their financial target was set) that prices should increase by about 1 per cent real a year. The Treasury proposal is for prices to rise on average by 4 per cent real a year from 1 January 1985 (i.e. 8-9 per cent nominal if inflation runs at 4-5 per cent). Note : Savings are pro rata to the increase in prices; each 1 per cent real a year over the period contributes :

	-55	-100	-194
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Points to Make

- Proposals entirely consistent with successive Government's views on nationalised industry pricing as set out in a series of White Papers. 1967 White Paper (Cmnd 3437) stated that prices should generally cover "the cost of supplying on a continuing basis" including "provision for the replacement cost of fixed assets needed for the continued provision of service, together with a satisfactory rate of return on capital employed". The Department of Energy's own Green Paper on Energy Policy in 1978 echoed this in similar uncompromising terms.
- BGC has an implicit subsidy from Government since two thirds of its gas comes from contracts negotiated before 1975 which are low price because they are exempt from the North Sea tax regime. The subsidy is currently around £1½ billion. To earn its present financial target rate of return without subsidy would mean raising prices by about 25 per cent. Treasury proposals would remove about half of the subsidy by the end of the IFR period.
- No more reason that gas should be subsidised in this way than that car drivers should get petrol free of North Sea taxes on the crude oil.
- Underpricing of gas gives the wrong signals to consumers. It increases demand for gas (when there is overcapacity in electricity generation) and leads to wasteful investment. Even BGC recognise that there will need to be substantial real increases in prices in the 1990s as the older fields get exhausted. There is a clear economic case for moving towards economic prices now.

- Treasury and D/En officials have, following a remit from the PM in October 1983, been examining in detail the breakdown of BGC's costs and how they should be reflected in prices to the consumers. Using BGC's own figures, the analysis confirms, in the Treasury's view, the current 25 per cent underpricing in the domestic market. (The figure reduces to about 17 per cent in the mid-1990s as a result of price increases which BGC acknowledge will be necessary by then). The position is broadly similar in the non-domestic markets but with interruptible sales to industry underpriced by 33 per cent.

- D/En argue that the analysis shows that the price per therm is at economic levels but admit that BGC is not covering other costs notably for connection and other consumer-related costs. The Treasury view is that these costs must be recovered from the consumer; in the price per therm if they cannot be recouped in any other way.

Defensive

The Treasury proposals would result in an unacceptably high level of profits With 4 per cent real price increases, post-tax project in 1987-88 would be around £850 million (compared with £401 million in 1983-84). The (pre-tax) return on assets would be around 9 per cent, compared with the present financial target of 4 per cent. But compare :

	post-tax profit 1983	CC return on net assets
BP	£710m	8.7%
Royal Dutch/Shell	£1878m	7.9%
GEC	£310m	20.0%

BP and Shell's figures post-tax profit figures take account of North Sea tax regime. If it were not for the implicit subsidy to gas consumers BGC would be making a loss with present prices.

Treasury proposals would force BGC to exceed its financial target

The Chancellor and D/En Ministers agreed in November 1983 that BGC's financial target was provisional and subject to review in the light of the review of pricing policy. When pricing proposals have been agreed, we can look at the implications for the financial target.

Sir Denis Rooke and the BGC Board will not accept the price increases

The Treasury proposals are clearly in line with successive Government's policy on energy pricing, and are consistent with the Corporation's statutory objection obligations.

Price increases can only be imposed using the gas levy, and this does not help public expenditure

∟ The gas levy is a charge on BGC's costs aimed at recouping for the Exchequer some at least of the benefit BGC gets from its cheap supply contracts. Gas levy payments are currently around £500m. But the levy is treated as revenue in the Government accounts. Thus if the levy were increases to force the price increases, there would be no benefit to public expenditure. The revenue side PSBR would however benefit. ∟ We shall need to look at the size of the levy following agreement on prices. What is important now is to get agreement on prices. Even if the levy were used we could spell out the point in public expenditure presentation - as we did in 1982.

Price increases would be an additional burden on industry : indirect taxation

Raising prices towards economic levels is not a tax; it is merely removing an economic distortion and leads to better overall resource allocation. Comparison with industrial gas prices on the continent shows there is considerable scope for increases. (Latest figures show that UK industrial firm contract prices are nearly 20 per cent below the lowest continental prices).

Price increases are inflationary

Gas customers have had little increase for two years. Since October 1982 gas prices have risen only 4.3 per cent (see table). Inflation is best defeated by keeping down the level of public expenditure. Removing economic distortions will improve the health of the economy. In any case, gas price increases would add only 0.3 per centage points to RPI by end 1987-88.

Some major contracts (e.g. ICI) cannot be increased as fast as the Treasury propose.

What the Treasury propose is an average 4 per cent per year. How this is split between customers is largely for BGC to decide.

GAS PRICE INCREASES

Domestic

April	1980	17%
October	1980	10%
April	1981	15%
October	1981	10%
April	1982	12%
October	1982	10%
January	1984	4.3%

Industrial

Percentage increase on previous quarter of
average firm/interruptible non-domestic prices

1979	1979	Q1	0.7
		Q2	2.6
		Q3	19.0
		Q4	13.3
	1980	Q1	3.2
		Q2	8.2
		Q3	12.6
		Q4	1.9
	1981	Q1	-
		Q2	0.2
		Q3	-
		Q4	-
	1982	Q1	-
		Q2	3.4
		Q3-1984 Q1	-
	1984	Q2	about 1½
		Q3	about 1½
		Q4	about 1½

ELECTRICITY SUPPLY INDUSTRY (ESI)

The Treasury proposals for savings are made up as follows (£ million) :

	1985-86	1986-87	1987-88
A. Savings on capital investment, asset sales and efficiency			
1. More realistic Sizewell timetable	-20	-70	-50
2. Defer refurbishment of transmission, distribution and telephone systems	-60	-50	-50
3. Defer/cancel new electricity generating projects	- 5	-60	-100
4. Lower provision for connecting new customers	-	- 5	-10
5. Reduction in cost of carrying out Area Board investment	-10	-20	-25
6. Miscellaneous small savings on capital expenditure	- 5	- 5	-15
7. Area Board non-operational investment	-40	-80	-80
8. Lower coal stock	- 5	-15	-25
9. Lower stocks of nuclear manuals	-20	-50	-50
10. Improvements in debtors and creditors and lower engineering stocks	-10	-20	-20
11. High asset sales	-15	-20	-25
12. Higher connection changes	-20	-30	-40
Total after adjustment for tax consequences	-175	-375	-450
B. Financial target			
13. Financial target averaging 3.6% over next three years	-250	-400	-700

Detailed notes on each are set out in the following sectors.

1. SIZEWELL TIMETABLE

1985-86	1986-87	1987-88
-20	-70	-50

Treasury has no wish to delay the project, but ESI's timetable does not allow time for :

- (i) Public and Parliamentary debate of Inspector's report, even if on time.
- (ii) Modifications to design (e.g. from safety recommendations).

ESI assume that Inspector's report on Sizewell enquiry submitted in July 1985, Government's formal decision in October 1985 : first "concrete poured" in September 1986.

Points to make

ESI timetable unlikely because :

- (i) Government is committed to publish the Report and will have to allow debate in Parliament (in recess until beyond October).
- (ii) Mr Walker acts in a quasi-judicial capacity and will have to hear objections : haste could lead to legal challenge.
- (iii) The Inspector may recommend design changes : he has said he is not satisfied about ESI's arrangements with the Nuclear Installation Inspectorate.

Treasury figures assume start in March 1987, i.e. a six month slippage.

Capital Expenditure (Investment)

The investment figures are :

Capital expenditure in UK	1985-86	1986-87	1987-88	£m
Baseline	1195	1095	1123	
Provisional approval(1)	1016	767	-	
Revised bid compared to baseline	+23	+139	+99	
Treasury proposals compared to baseline (and as percentage)	-77 (-6%)	-71 (-6%)	-151 (-13%)	
Gap	100	210	250	

(1) Following IFR 83 ESI was given provisional approval to spend these figures : Treasury proposals are higher, so there could be no suggestion of bad faith.

S E C R E T

2. DEFER REFURBISHMENT OF TRANSMISSION, DISTRIBUTION AND TELEPHONE EXPENSES

	1985-86	1986-87	1987-88	£m
Savings sought	-60	-50	-50	
Total provision proposed by ESI	240	255	280	

Points to Make

1. The level of disconnections from faults in the transmission and distribution system is running below the ESI's own targets (about $1\frac{3}{4}$ hrs per customer/year compared to 2 hrs).

2. MMC found in February 1984 that South Wales Board made no "attempt to assess the justification for particular levels of expenditure" [on refurbishment] and recommend full economic appraisal. We should not get committed to this programme until that has been done. Treasury has accepted a well founded case by Mr Younger for the North of Scotland Board.

3. CEGB are planning to purchase a complete new internal telephone and data transmission network costing (£50m), which could be deferred. Some circuits are rented from BT/Mercury, but CEGB also plan their own microwave and optical fibre links - it is questionable whether they need to enter that business.

S E C R E T

3. DEFER/CANCEL NEW GENERATING PROJECTS

1985-86	1986-87	1987-88	£m
-5	-60	-100	

Points to make

1. Given present overcapacity, no new projects are essential.
2. New wind energy and hydro-electric projects could be left to the private sector (under the 1983 Energy Act which gives a favourable framework). Mr Younger has agreed to drop these projects in Scotland - they are even less promising in England and Wales.
3. Following miners strike, it is most unlikely that we shall want to convert oil burning stations to coal burning. In any case the economics have not been established properly.
4. Some, though not necessarily all, new combined heat and power projects could be left to the private sector.

S E C R E T

4. LOWER PROVISION FOR CONNECTION OF NEW CUSTOMERS

1985-86	1986-87	1987-88
0	-5	-10

Points to make

1. Industry assume current high level of new business continuing indefinitely - there should be a down-turn in later years with the normal business cycle.

S E C R E T

S E C R E T

5. REDUCTION IN COST OF CARRYING OUT AREA BOARD INVESTMENT

1985-86	1986-87	1987-88
-10	-20	-25

Treasury figures imply a 5 per cent real cost reduction by 1987-88.

Points to make

1. MMC commented on Yorkshire Board that costs of undertaking new investment "have been higher than they otherwise could be" (because the Board had only rarely had to ration capital expenditure).
2. Some Boards (e.g. East Midlands) have indicated scope for real reductions.
3. MMC suggested South Wales contract out more work to see whether this is cheaper than "own labour".

S E C R E T

S E C R E T

6. MISCELLANEOUS SMALL SAVINGS

1985-86	1986-87	1987-88
-5	-5	-15

For example; halting £10m refurbishment at CEGB's Headquarters in the City.

S E C R E T

7. AREA BOARD NON-OPERATING EXPENDITURE

1985-86	1986-87	1987-88
-40	-80	-80

Background : "non-operational" expenditure covers vehicles, computers, land/buildings not directly required for supplying electricity.

Points to make

1. The level proposed by the ESI has increased by some 20 per cent since last year's IFR.
2. ESI have not been able to demonstrate that this programme meets the 5 per cent rate of return criterion. Nonetheless you have said you will not pursue these savings if the industry accepts the higher Financial Target.

8. LOWER COAL STOCKS

1985-86	1986-87	1987-88
-5	-15	-25

For the reasons given in Appendix A(b), Treasury consider ESI coal price assumption is too high. This affects the value of coal stock too.

[Defensive : decision on the volume of coal stock cannot be taken until after the miner's strike. ESI's current assumption of restoration to pre-strike levels is sensible meanwhile.]

9. LOWER STOCKS OF NUCLEAR MATERIALS

1985-86	1986-87	1987-88	£m
-20	-50	-50	

Points to Make

The ESI currently hold 7 years stock of nuclear fuel valued at £100m. This is much higher than their own targets of under 2 years. Treasury's proposed reduction - about 15 per cent over three years - could be achieved by a combination of :

- (i) not replacing extra fuel consumed by higher output from nuclear stations - see Appendix A(c).
- (ii) rephasing supply contracts (with Rio Tinto Zinc) as was done for Australian coal contracts last year.
- (iii) Selling. The spot market is weak but CEGB expect it to firm up during the next two years.

[Defensive : we are not asking CEGB to do anything uneconomic. A case has been put to DEN that, after taking account of interest and stocking costs, there is a cost saving in selling now and buying again later - they have not replied.]

S E C R E T

10. IMPROVEMENTS IN DEBTORS AND CREDITORS AND ENGINEERING STOCK HOLDINGS

1985-86	1986-87	1987-88	£m
-10	-20	-20	

Points to Make

1. ESI are assuming 2 per cent improvement in debtors. But performance indicators show 20 per cent variations between Boards. This suggests a faster rate of average reduction is possible; perhaps 4 per cent by 1987-88.

2. , On engineering stocks, the MMC were complimenting Boards earlier reductions but suggested even lower level were feasible.

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S E C R E T

11. SALE OF ASSETS

	1985-86	1986-87	1987-88	£m
Increase disposals by :	-15	-20	-25	
∟ ESI present projections	-25	-18	-17	7

Points to make

1. At 1 January 1984 ESI had over 2500 acres of unused or underused land, at 250 sites. Scottish Electricity have sold sites previously acquired for power stations but not now needed. CEGB could do so too.

2. Treasury accepts that asbestos stripping has reduced sale value of old power statins for other purposes, but CEGB have been slow to encourage as a going concern sales to private sector generators.

3. CEGB, which raises no finance itself, doesnot need Headquarters in the City (St Paul's Churchyard). Sale of the long-lease could give net receipts whether or not Board moved out of London. Follow example of large companies such as ICI, Blue Circle.

S E C R E T

12. HIGHER CONNECTION CHARGES TO NEW CUSTOMERS

1985-86	1986-87	1987-88	£m
-20	-30	-40	

Points to make

1. 50 per cent under charging cost of new connections is a cross-subsidy between existing and new customers.
2. Both consultants (Deloittes) and MMC have suggested review of current policy.
3. A convenient way of increasing receipts without raising electricity prices as such.

Defensive

1972 MMC recommendations. It is true that the majority of MMC recommended against full recovery in 1972 (Cmd 5036) when Government was holding down NI prices for counter-inflation reasons. But in their 1983 Report on Yorkshire Electricity they say "since that [ie 1972] report was produced, there have been changes in tariff structure and economic background, so there may be a case for reviewing connection charge policy".

Cost of new housing

Recognise that this change could add £1-200 to cost of a new house. Prepared to phase in over 3 years to give the housebuilders, building societies time to adjust.

13. FINANCIAL TARGET

Treasury's proposal is that rate of return on current cost assets be increased to 4.5 per cent by 1987-88 (compared to ESI's proposed 2 per cent) and average 3.6 per cent over IFR period. This would produce savings of (£ million) :

1985-86	1986-87	1987-88
250	400	70

It would require an operating profit of :

Rate of return (%)	2.8	3.6	4.5
Increase in operating profit compared to ESI proposal	+300	+610	+970

Points to make

2. Treasury assessment is that this return could be achievable by a combination of (at 1987-88 values) :

(a) Increasing prices in line with inflation, giving £350-400m, ESI assume inflation of 5 per cent, and :

Treasury price path	+5.0	+5.0	+5.0
ESI price path	+4.2	+3.4	+3.8

(b) Reduction in operating cost, giving £620m (see details at Appendix A). Treasury is not trying to "manage the Industry" but ESI's projections are noticeably cautious. MISC 106 may recall that when pressed last Autumn, they produced a further £250m savings for 1984-85.

3. This approach gives the right incentive to increase efficiency. If the ESI make more cost gains then real price reductions would be possible.

Defensive"Treasury proposals mean huge profits"

It is true that operating profits (i.e. before interest and tax) would be higher. But "bottom line" profits after interest and tax would be around current levels (mainly because of higher Corporation Tax). The figures are :

Operating Profit (before interest and tax)(1)

	Current Target		Next Target		
	1983-84	1984-85 (pre-strike)	1985-86	1986-87	1987-88
ESI proposal	+901	+642	+740	+760	+775
Treasury proposal	+901	+642	+1040	+1350	+1750

Bottom Line Profit (after interest and tax)(2)

ESI proposal	+456	+242	+190	-130	-140
Treasury proposal	+456	+242	+400	+300	+500

Key points :

(a) ESI proposal involves bottom line losses of £80m over 3 years. The Comptroller and Auditor General criticised D/En (in a July 1984 report) for setting targets "which were not fully consistent with the statutory [breakeven] duty". The ESI proposal would repeat that error.

(b) There are companies with lower current cost assets than ESI which make higher bottom line profits (e.g. BP - £710m and Shell £1878m in 1983).

Notes

- (1) Operating profit is difference between revenue and operating costs.
 (2) "Bottom line" profit is operating profit less interest and Corporation Tax.

"Government told Select Committee in Energy that there are "good prospects" of the 1985-86 electricity prices increase being below the rate of inflation"

True, but this was not reported in the Government's response to the Select Committee report. The coal strike has removed the public expectation of lower electricity prices in 1985-86. Under the Treasury proposal, prices would still have fallen in real terms during this Parliament. Figures are :

S E C R E T

	Domestic	RPI	Industrial
1979-80	18	20	21
1980-81	20	13	24
1981-82	11	10	13
1982-83	9	5	7
Total 1979-80-1982-83	86	56	81
1983-84	0	5	0
1984-85	1.5	4.5	2.5
Treasury proposal - in line with inflation to 1987-88	5	5	5
Total 1983-84-1987-88	17	27	19

Load Management Schemes

Treasury is content for the Industry to decide on the future of these schemes.

[Background : load management schemes were introduced in the 1980 and 1981 Budgets. They give large users discounts of up to 15 per cent in exchange for occasional interruptions of supply. The schemes expire at the end of 1984-85. There is doubt whether the cost savings (£120m a year) match the price reductions, and hence whether a cross-subsidy may be involved. But this is a matter that can be left to the ESI as long as they meet their financial target. Treasury would not favour any sudden changes.]

S E C R E T

OPERATING COST SAVINGS IDENTIFIED BY TREASURY

The following figures give savings, compared to ESI, projected in 1987-88. In total they save £620m. With prices rising in line with inflation (£350-450m) this gives the £970m improvement in profit required to increase the return on assets to 4.5 per cent in that year.

	(£ million)
	<u>Savings by 1987-88</u>
(a) lower coal/oil prices than industry assumption	130
(b) full use of new electricity link with France and existing link with Scotland	70
(c) 20 per cent greater output from nuclear power stations	150
(d) Lower nuclear fuel costs	40
(e) Faster manpower rundown	75
(f) Lower real earnings for workforce	120
(g) Lower depreciation plus other savings	<u>50</u>
	635
(h) Less higher nuclear R&D costs	<u>15</u>
	<u>620</u>

Details on each item supplied on following pages.

A number of the savings will reduce ESI's coal burn and hence NCB sales. But the Treasury thinks it wrong in principle to shield NCB from market pressures by foregoing savings; and is prepared to cope separately with the public expenditure implications for NCB.

(a) Lower coal/oil prices (£130m by 1987-88)

On coal prices. ESI assume real increases cumulating to 2 per cent by 1987-88 and at 2 per cent a year thereafter.

Points to make

1. This is not consistent with their joint understanding with NCB for a 1.5% real reduction by 1987-88. Current policy is to link NCB prices to world levels.
2. Recent studies by Treasury and Energy officials and by Scottish Electricity cast doubt on earlier projections of steep increases; and suggest world prices should remain roughly constant in real terms during the later 1980s (as a central assumption).

On oil prices, ESI assume real growth of 3 per cent a year to 1987-88.

Points to make

1. Interdepartmental and oil industry projections suggest no real growth.

∟ Defensive : Heavy fuel oil prices have hardened by about 5 per cent this year but that reflects :

- (a) Heavy buying by CEGB during the miners strike.
- (b) The weakness of sterling against the dollar due to the US elections and the miners strike. ∟

Background

ESI's projections on coal price match that original (1982) evidence to the Sizewell enquiry. We understand why they might not wish to change their figures now; but financial planning should make more realistic assumptions.

(b) Full use of new electricity links with France and existing link with Scotland (£70m)

ESI assume use of only one of the two new links to France (second completed in 1986).

Points to make

1. Prime Minister said in recent Ministerial correspondence that the logic pointed to utilising both links fully - that is the right basis for financial planning.

2. By 1988 further cheap supplies from Scotland should be available as the new Torness nuclear station comes on stream.

Background

Using the links, particularly with France, is 30 per cent cheaper than burning coal.

S E C R E T

(c) 20 per cent more output from nuclear stations (£150m)

Points to make

1. ESI projections are over-pessimistic, assuming lower levels of output from AGR stations than has already been achieved at some.
2. Department of Energy have set the Atomic Energy Authority the objective (in Cmnd 9143) of helping the nuclear industry to achieve "power output at rated levels on all stations [Tsy underlining] by 1988". Treasury figures assume that is achieved.
3. Mr Younger has already agreed savings from assuming the higher level for the Hunterston AGR in Scotland.

S E C R E T

S E C R E T

(d) Lower nuclear fuel costs (£40m)

The ESI has negotiated real price reductions from British Nuclear Fuels plc. But the Company have told DEn and Treasury officials that they "hope to do better" and would accept a more demanding cost reduction aim from Government. Since BNFL are already earning over a 5 per cent return on this (monopoly) business, Treasury is content to see the further cost reductions passed on in even lower prices to the Electricity Boards.

S E C R E T

(e) Faster manpower rundown (£75m)

ESI are assuming a 5-6 per cent reduction by 1987-88, but most of this comes from closing older power stations as new investment bears fruit. There is evidence of further scope for reductions of, perhaps, 5 per cent.

Points to make

1. ESI's own performance indicators for Area Boards show much wider variations in employees per 1000 customers than explicable by trading and geographical differences. The average is 16 per cent higher than the three leading Boards.
2. ESI's latest cost per unit for distribution and transmission is 30 per cent higher than for Scottish Electricity (Source : Scottish Electricity performance review).
3. MMC have commented in their reports on the need for the greatest "vigilance over numbers employed" (while commending Boards earlier efforts).

Particular quotes are :

- (a) Yorkshire Board should "as a matter of urgency consider ways of reducing its surplus of technical staff over a shorter timescale than in the past".
- (b) South Wales Board should "adopt a more questioning approach to manpower costs" and "take steps to restore and improve on previous productivity levels" [following] "a significant drop" [in recent years].

4. CEGB have already indicated to DEN that they have excess staff in their regional organisation and in power station building/research divisions.

(f) Real reduction in level of earnings (£120m)

ESI assume earnings per employee rising by just under 1 per cent a year faster than inflation. Since 1979, earnings have increased by about 15 per cent more than manufacturing industry generally, taking ESI to near the top of the earnings league.

Points to make

1. Treasury recognise the industrial strength of certain key workers (totalling about 20,000 out of 130,000 employed in the industry). But excess pay levels are general. For example, a 1983 survey showed ESI copy typists earning - after 17 increments - about 10 per cent above leading industry employers (ICI, Shell) and 30 per cent above, more comparable, Clearing Banks/Insurance.
2. Treasury proposals for real reductions averaging about 1.5 per cent a year are based on :
 - (a) Increases in line with inflation for the sensitive groups.
 - (b) Increase of about 2 per cent less than inflation for the others (this is the same as the Civil Service pay factor for 1985-86).

S E C R E T

(g) Minor savings (£50m)

MMC Reports indicate scope for savings in many areas, including :

- (i) Closer analysis of purchase costs.
- (ii) Computer development.
- (iii) Elimination of losses on repair business.
- (iv) Contracting out maintenance work.

Savings on capital expenditure also reduces depreciation.

S E C R E T

S E C R E T

(h) Higher nuclear R&D costs (adds back £15m)

Transfer of cash from AEA (£22m) offset by £8m reduction in fast reactor funding.

S E C R E T

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Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

16 October 1984

Andrew Turnbull Esq
10 Downing Street
LONDON SW1

Dear Andrew

The Prime Minister will wish to be aware of the economic assumptions which the Chancellor is proposing for public expenditure in the years 1985-86 to 1987-88. Most will be published in the Autumn Statement, the Government Actuary's November Report and the next Public Expenditure White Paper.

For the Autumn Statement the main assumptions are:-

	<u>Unemployment</u>	<u>Inflation</u>	<u>Average Earnings</u>
	(GB, narrow, millions)	(per cent rise in RPI, year to May)	(per cent rise, underlying year on year)
1984-85	3.0 =	-	7½* =
1985-86	3.0 =	4¾ =	7* =

(*These figures reflect "underlying" increases which take no account of the impact of the miners' dispute. The miners' dispute will probably reduce the 1984-85 figures to about 7 per cent and raise the 1985-86 figure to 7½ per cent.)

The figure for unemployment in the current financial year 1984-85 should not in itself cause much surprise. The total, on the definition used by the Government Actuary (GB, excluding school leavers and temporarily stopped), stood at nearly 3 million on a seasonally-adjusted basis in September. So the assumption implies, broadly, little change over the next few months. But it is of course higher than the figure of 2.85 million for 1984-85 which was published in the February 1984 PEWP and repeated in the July Report of the Government Actuary.

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For 1985-86, projections are inevitably more uncertain. But it would seem unwise to base further expenditure projections on an assumption that unemployment will start falling soon. The proposed figure of 3.0 million for 1985-86 is consistent with little net movement through the year.

On inflation, the last published figure of $4\frac{1}{2}$ per cent for the RPI increase up to the end of 1984 now looks a little optimistic. It is however likely to be much nearer to the eventual outcome (probably about $4\frac{3}{4}$ per cent) than commentators thought at Budget time. The likely overshoot is more than explained by the rise in mortgage interest rates. It is possible that the 12-month figure could rise again early next year to about 5 per cent, reflecting the path of the RPI through last year, but the underlying path should still be downward. The proposed assumption that the 12-month increase will be about $4\frac{3}{4}$ per cent next May would be consistent with these general trends.

There are some complex presentational issues connected with the assumptions about increases in average earnings. These are not of great importance to the public expenditure projections, but are needed by the Government Actuary to forecast income from National Insurance Contributions.

The earnings figures for 1984-85 will be heavily influenced by the effects of the miners' dispute. Even on the assumption that the strike is settled by the end of the year the simple loss of miners' earnings during the dispute will reduce the average increases for the financial year by about $\frac{2}{3}$ per cent. Thus, an "underlying" increase of about $7\frac{1}{2}$ per cent will reduce to just under 7 per cent. In 1985-86, we would get the opposite effect: taking a reduced 1984-85 level as "base" the recorded increase between the years would be raised by about $\frac{2}{3}$ per cent. Although some reduction in "underlying" increases is to be expected between the years, the relevant figures would then look like an increase from 7 per cent to $7\frac{1}{2}$ per cent.

To avoid this presentational difficulty without distorting the Government Actuary's calculations, the Chancellor proposes to ask him to give greater prominence in his explanation about the figures to an "underlying" reduction from about $7\frac{1}{2}$ per cent to about 7 per cent than to the actual figures. In smaller print, qualitative mention will be made of the impact of the miners' dispute and of the figures of 7 per cent and $7\frac{1}{2}$ per cent respectively which have actually gone into his forecasts.



Later years of the Survey

Assumptions are also needed for the later years in the Survey period. Those on unemployment and prices have in previous years not been published until the Public Expenditure White Paper. This year, they might be revealed earlier if total expenditure figures are to be provided. The proposed paths are as follows:

	<u>Unemployment</u> (GB, narrow, millions)	<u>Inflation</u>	
		<u>RPI</u> (per cent rise in year to May)	<u>GDP Deflator</u> (per cent rise)
1984-85	3.0	(5.1)	4 $\frac{3}{4}$
1985-86	3.0	4 $\frac{3}{4}$	4 $\frac{1}{2}$
1986-87	3.0	4	4
1987-88	3.0	3 $\frac{1}{2}$	3 $\frac{1}{4}$

The assumption of a flat path for unemployment after a recent rise is fairly conventional. The last set of published figures showed unemployment staying at 2.85 million for the years 1984-85 to 1986-87. Reflecting the increases that have actually taken place this year, the proposal is now to show a level of 3.0 million for all years.

On the RPI, and GDP deflators the figures are likely to cause no surprises. On the RPI no change is proposed for May 1986 from the figure of 4 per cent shown in the last PEWP. A further deceleration to 3 $\frac{1}{2}$ per cent is assumed for the year to May 1987.

Yours ever
David

D L C PERETZ



F.C.S.
16

~~OFF to CP to Monday~~
C.S.R.A.
24A

PRIME MINISTER

MINISTERIAL GROUP ON PUBLIC EXPENDITURE (MISC 106)
FOREIGN AND COMMONWEALTH OFFICE PROGRAMMES

As you know, MISC 106 have been meeting under my chairmanship to discuss the public expenditure programmes on which the Chief Secretary, Treasury has not reached agreement bilaterally with the spending Ministers concerned. We have had two meetings with the Foreign and Commonwealth Secretary to discuss the programmes for which he is responsible: the Overseas Development Administration (mainly the aid programme); and the Foreign and Commonwealth Office (Diplomatic Wing). Unfortunately, we have not been able to reach agreement with him. In view of the political considerations involved, I think it would be helpful if the Foreign and Commonwealth Secretary and I could discuss the position with you.

BACKGROUND

ODA

2. The baseline for the programme is as follows (all figures in £ million):

1985-86	1986-87	1987-88
1263.8	1298.6	1320.4

The position reached after the bilateral discussions was that bids and savings (resulting partly from a carry over of aid programme expenditure from 1983-84 and partly from other factors) had been agreed totalling:

+ 6.2	- 2.2	- 2.9
-------	-------	-------

3. The Foreign and Commonwealth Secretary sought further changes of:

0	+ 58	+ 115
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mainly to restore part of the cut-backs in bilateral aid which have resulted partly from the real reduction in the aid programme since 1979 and partly from the increase in the proportion of the programme taken up by multilateral aid.

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8. The Chief Secretary sought reductions of:

- 10

- 15

- 20

He considered that, to the extent that the additions identified by the Foreign and Commonwealth Secretary were unavoidable, they should be offset by savings elsewhere. He further considered that sufficient savings were available to achieve the net reductions he proposed without any significant damage to our foreign policy.

9. After his initial discussion with MISC 106, the Foreign and Commonwealth Secretary had a further look at his bids. He decided that a number of items could be absorbed or postponed, though with great difficulty, and that he could accordingly reduce his bids to a net total of:

+ 33.5

+ 42.8

+ 43.6

compared with those in paragraph 7 above. He considered that he could not absorb these sums within his baseline without sharply reducing functions or geographical coverage.

VIEWS OF MISC 106

10. MISC 106 were grateful to the Foreign and Commonwealth Secretary for the thoroughness with which he had re-examined his programmes. They also recognised the political difficulty of imposing reductions in the services provided by the BBC and the British Council. On the other hand, they felt that a number of the bids put forward by the Foreign and Commonwealth Secretary, such as provision to cover the Property Repayment Services, reflected problems which all departments had to cope with. Similarly, most departments had to cope with difficulties arising from single very large capital projects, such as the Moscow Embassy.

11. Most important, however, was the general political background. The Cabinet have set MISC 106 the objective of formulating recommendations which will allow the agreed planning totals to be held. In order to achieve this we are having to consider deep cuts in

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extremely sensitive domestic programmes, such as health and social security, and housing. I can readily expand on this if you wish.

Against this background, the Group did not think that it would be justifiable to recommend any increase over the combined ODA and FCO baseline: indeed, some members of the Group argued in favour of recommending net reductions. The Group recognised that the implications of recommending no increase in baseline provision might be a reduction in the aid programme in order to accommodate inescapable increases in expenditure on the Diplomatic Wing, and that this would not be politically easy. Nevertheless, they were clear that the difficulties of this course were less than those that would follow from conceding an increase in the size of the two programmes together.

FUTURE ACTION

12. For reasons which the Group understood, the Foreign and Commonwealth Secretary was unable to accept this view. Given the importance of the issues, I think it would be helpful if you could discuss them as soon as possible with the Foreign and Commonwealth Secretary, the Chief Secretary and myself.

13. I am sending copies of this minute to the Foreign and Commonwealth Secretary, the members of MISC 106, and to Sir Robert Armstrong.

WJW

15 October 1984

SECRET

OUTSTANDING ISSUES

(a) Expenditure

The Foreign Secretary seeks the following additions:-

Overseas price adjustment since October 1983	16.0	16.0	16.0
Sterling shortfall Oct 82-Sept 83	7.5	7.7	7.9
Property repayment services	3.0	3.8	4.3
FOLIOS "electronic office" project	1.9	3.2	3.3
Moscow/London Embassy sites	0.4	2.0	4.1
Security works overseas	1.1	1.4	1.6
BBC External Services:			
(a) Pay award and improved conditions of service	2.1	2.7	3.1
(b) Bringing forward modernisation of monitoring service and audibility programme and reinstating Caribbean service	3.6	5.6	2.6
(c) New electronic distribution system at Bush House	0.6	1.7	2.5
British Council:			
(a) Risen costs, including rent	3.0	3.0	3.1
[(b) ODA share of risen costs	1.7	1.7	1.7]*
(c) Increased activities	3.1	5.2	7.7
Military training in Caribbean	1.3	0.8	0.2
Increase in overseas estate purchase programme	2.0	2.0	1.9
Additional costs of overseas student scheme	0.9	1.0	1.2
Sundry small one-off items	1.5	1.5	1.6
TOTAL	49.7	59.3	62.8
<u>Less</u> Sundry offsetting savings	-3.7	-3.7	-3.7
NET TOTAL	46.0	55.6	59.1

* This is ODA's share of the British Council's costs. The Treasury position is that this should be met from the aid programme as part of ODA's general financing of the British Council; and is not therefore a legitimate bid on the FCO (Other) programme.

SECRET



10 DOWNING STREET

From the Private Secretary

cc HO
SO
LPS
DTI
CST
CO (2)

DES
15 October 1984

JARRA1Q
23A

MISC 106: R & D EXPENDITURE BY DEPARTMENTS

The Prime Minister has received the attached comments from the Chief Scientific Adviser, Cabinet Office, on the R & D expenditure of Departments whose bids will be considered by MISC 106, and where R & D constitutes a significant element of their expenditure.

The Annual Review of Government-funded R & D announced in Cmnd 8591 (Government observations on the report "Science and Government" from the House of Lords Select Committee on Science and Technology) was established to take a horizontal look at Government-funded R & D plans in the PES cycle. The 1984 Review, together with the views of the Advisory Council for Applied Research and Development (ACARD) on the expenditures covered in the Review, were drawn to the attention of members of the Cabinet (David Barclay's letter of 6 August). In addition, Dr. Nicholson subsequently gave the Prime Minister his personal impressions, based on the scrutiny of Departmental objectives and expenditure plans made by his Secretariat while preparing the 1983 and 1984 Annual Reviews.

The Prime Minister has noted Dr. Nicholson's view that generally the picture is one of rigidity and lack of change to meet changing circumstances, with the distribution of Government-funded R & D substantially out of balance. She endorses the validity of the overview approach advocated in Cmnd 8591, and accepts that for the Review process to succeed the need for cuts in some areas of R & D will need to be examined alongside the need for maintenance of R & D expenditure or even increases in expenditure in others.

The Prime Minister has previously indicated that she will take a co-ordinating role on science and technology issues which straddle the responsibilities of several Ministers. She believes it will be helpful to members of

SECRET

MISC 106 to be aware of the views of ACARD and Dr. Nicholson on the distribution of Government-funded R & D.

I am sending a copy of this letter and the attachments to the Private Secretaries to other members of MISC 106, and to Richard Hatfield and Robin Nicholson (Cabinet Office).

(ANDREW TURNBULL)

Miss Janet Lewis-Jones,
Lord President's Office.



MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister
CONFIDENTIAL

The Rt Hon Peter Rees QC MP
Chief Secretary to the Treasury
Treasury Chambers
Parliament Street
London SW1P 3AG

NBRM
AT
15/10

15 October 1984

REPORT ON AGRICULTURAL DEVELOPMENT AND ADVISORY SERVICE

Thank you for your letter of 12 October 1984 giving me your preliminary reactions to this report on substance and procedure.

I am glad that you feel that the report is a major contribution to the development of policy towards ADAS. I agree; indeed, I should perhaps remind you that it was at my initiative that Professor Bell was asked to produce his report in the first place. I also share your wish to move forward as quickly as possible. However, if I may say so, I think your letter gives a misleading impression on what may be possible and sensible to seek to do in the context of this year's PES exercise. In particular I cannot accept that the proposal in the penultimate paragraph of your letter to write in now, without any proper appraisal of the possibilities and consequences, a cut of £40 million in my PES provision for 1986/87 and 1987/88.

The figure of £40 million you mention is of course no more than a broad indicator of the present scale of ADAS resources (mainly staff costs) devoted to advisory work: it is in no way a considered estimate of what could be saved by implementing the recommendations of the Bell report. The Bell report, from which I fear you have quoted very selectively, did suggest, and I agree with this, that Ministers should give consideration to the possibilities of making charges to contribute towards the cost of advisory work. But it pointed to various areas, welfare and conservation work, where it would be difficult to apply charges; it emphasised that the introduction of charges would call for "careful planning and gradual introduction"; it envisaged charges being set at levels which the market would bear without seriously damaging a vital service to the industry; it raised the question of whether differential rates of charge should be considered for producers who might otherwise be denied access to advice and up to date technological information.

/This latter point

11 5 OCT 1984



This latter point raises delicate issues as does the whole question of the primary legislation that would be needed for any major extension of charging. Other parts of the report considered the question of whether the more widespread application of information technology could not make major contributions to a more efficient and compact service: to translate this possibility into well considered proposals will also call for a major study and investment appraisal.

It is only necessary to enumerate a few of the major questions posed by the report to see that it would be utterly simplistic, counterproductive and indeed contrary to the principles of sound financial management we are now seeking to establish throughout the Government to proceed in the way you suggest. I am not seeking to argue that the present ADAS arrangements should not be changed or to deny that it may not be possible to make significant savings in future by moving in the direction Bell suggests. But what I do insist most strongly is that the major changes necessary must be adequately prepared for by drawing up a proper plan of detailed implementation on the basis of the further studies that are obviously necessary. I am glad to see that your letter accepts the need for this further work; and I would hope that you would, on reflection, now accept that it would be quite unreasonable and indeed counterproductive (in terms of the likely public response) for this year's PES to have firm figures written into it before this very necessary follow-up work has been carried out.

I am sending copies of this letter to the Prime Minister, the Lord President, the Secretaries of State for Trade and Industry, Scotland, Wales and Northern Ireland, and to Sir Robert Armstrong.

MICHAEL JOPLING

Pl. Agree on R & D with.

+ B. Young 21A



Prime Minister

Agree that Dr. Nicholson's views on priorities be made available to Lord President and Chief Secretary?

I see no reason why this should not be extended to other members of MISC 106.

12 October 1984

W0749

PRIME MINISTER

Agree?

Yes no

AT

12/10

MISC 106: R & D EXPENDITURE BY DEPARTMENTS

1. When I minuted you on the Annual Review of Government Funded Research and Development (W.0495, 27 July 1984), I said that I believed the Review showed Government-funded R & D to be substantially out of balance, the present position having developed over many years as a result of the varying bargaining skills of Departments in the PES round; also that we are over-committed in R & D for defence, agriculture and nuclear energy and under-committed in basic research and in strategic research for areas such as the environment and manufacturing industry. I did, with your agreement, communicate to the Chief Secretary the views that I expressed to you, and provided some guidance for his officials on the questions that could be put to Departments during the PES bilaterals.

2. Following your meeting with Lord Jellicoe and Sir James Gowans on MRC funding, you asked me how areas of Government funded R & D which might be inadequately supported could have their funds increased without increasing overall public expenditure. I pointed out that Government had accepted the validity of the horizontal look at Government-funded R & D in its response to the House of Lords Select Committee report on 'Science and Government' and that the Annual Review of R & D now provided a basis for a judgement to be made on areas of waste in Departments' R & D expenditure and areas which were inadequately supported.

3. With MISC 106 starting to meet next week, I have therefore prepared some further comments on relevant R & D expenditures in MAFF, MOD and DOE which are attached. In summary they recommend that MISC 106 should seek, in full, the suggested reductions in support for agricultural R & D, the burden of cuts falling on support for improvement of agricultural productivity and the associated advisory services; they inform the Committee of the work you have asked to have put in hand on defence R&D that may have implications for the

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next PES round; and they seek to protect the R & D activities of DOE relevant to radioactive waste disposal and other areas.

4. Since you have indicated that you wish to take a co-ordinating role in science and technology issues which straddle the responsibility of several Ministers, you may wish to send the comments to the Chairman of MISC 106 from your office in which case a draft Private Secretary's minute is attached. Alternatively you may prefer me to send the comments direct to the Lord President and the Chief Secretary.

5. I have copied this minute and the attachments to Sir Robert Armstrong.

MBN

ROBIN B NICHOLSON
Chief Scientific Adviser

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~~DRAFT PRIVATE SECRETARY LETTER~~

to Janet Leary Jones

MISC 106: R & D EXPENDITURE BY DEPARTMENTS

The Prime Minister has received the attached comments from the Chief Scientific Adviser, Cabinet Office, on the R & D expenditure of Departments whose bids will be considered by MISC 106, and where R & D constitutes a significant element of their expenditure.

The Annual Review of Government-funded R & D announced in Cmnd 8591 (Government observations on the report "Science and Government" from the House of Lords Select Committee on Science and Technology) was established to take a horizontal look at Government-funded R & D plans in the PES cycle. The 1984 Review, together with the views of the Advisory Council for Applied Research and Development (ACARD) on the expenditures covered in the Review, were drawn to the attention of members of the Cabinet (David Barclay's letter of 6 August) . In addition, Dr Nicholson subsequently gave the Prime Minister his personal impressions, based on the scrutiny of Departmental objectives and expenditure plans made by his Secretariat while preparing the 1983 and 1984 Annual Reviews.

The Prime Minister has noted Dr Nicholson's view that generally the picture is one of rigidity and lack of change to meet changing circumstances, with the distribution of Government-funded R & D substantially out of balance. She endorses the validity of the overview approach advocated in Cmnd 8591, and accepts that for the Review process to succeed, the need for cuts in some areas of R & D will need to be examined alongside the need for maintenance of R&D expenditure or even increases in expenditure in others.

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The Prime Minister has previously indicated that she will take a co-ordinating role on science and technology issues which straddle the responsibilities of several Ministers. She believes that ^{it will be helpful to members of MISC 106 to be aware} ~~the correct~~ distribution of Government funded R&D should be a factor in the MISC 106 discussions and that the ~~advice~~ of ACARD and Dr Nicholson should be taken into account.

I am sending a copy of this letter and the attachments to the Private Secretary ^{to} of the Chief Secretary. ^{reference of MISC 106, to Richard Hatfield}

and ^{Admiral} ~~Admiral~~ Nicholson
(Cabinet Office)

SECRET

COMMENTS FROM THE CHIEF SCIENTIFIC ADVISER, CABINET OFFICE, FOR MISC 106

Ministry of Agriculture, Fisheries and Food - support for reductions
proposed by MISC 100

1. Two areas in which Government support should be reduced are for R & D and for the Agricultural Development Advisory Service (ADAS). MISC 100 recommended that MAFF's expenditure on agricultural R & D should be halved but had to treat ADAS as sub-judice because of the in-house review in train.
2. MAFF will probably seek to delay decisions on R & D funding pending the outcome of further reviews and advice by the Priorities Board. MISC 106 should ignore such arguments, since it is highly unlikely that the Priorities Board will recommend that R & D support should be reduced. A halving of support for R & D by the end of the PES period would not be unreasonable.
3. MISC 106 may wish to consider the areas of MAFF R & D activity where they would wish support to be reduced. The following table taken from the 1984 Annual Review of Government-funded R & D shows the purposes of projected expenditures of MAFF for 1985/86 -

	£m
Supporting statutory duties	13.4
Supporting purchasing duties	0.1
To improve technology	103.2
Supporting policy formulation and implementation	10.5

It would be difficult to argue the case against support for R & D in relation to the statutory responsibilities of the Department, since such expenditures stem from the Government legislation - even though some of the routine monitoring carried out by MAFF is undertaken voluntarily and the value of some of this work is questionable. Similarly, there is no obvious argument against R & D expenditure to support policy formulation. One would need more information on MAFF policies in order to understand the R & D expenditures involved. The expenditures to improve technology are by far the largest and most difficult to justify. The major proportion (£86.5m) supports research in agriculture. Such a

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high level in support of improvement of agricultural technology must be questionable given the very large subsidy which farming incomes already receive under CAP arrangements.

4. The long-awaited review of ADAS is, I am told, now complete although I have not seen a copy. Farmers support for improving technology through ADAS is additional to the R & D expenditure quoted in paragraph 2. Roughly half the MAFF complement is composed of ADAS officers and although MAFF claim that more than a third are concerned with statutory duties, this does not seem to be their main activity and the majority are concerned with general advisory duties whether in agriculture or agricultural science. Such officers are engaged in advising farmers on the results of R & D. Any reduction in the R & D budget could therefore produce further savings in the ADAS Agriculture Service. Similarly the ADAS Agricultural Science Service would need to be examined, since it is largely concerned with the exploitation of R & D and any reduction in R & D should again produce savings. MAFF is protectionist about ADAS (attention is rarely drawn to manpower, interest areas, cost effectiveness, etc) and may, if MISC 106 were to allow latitude, apply the cuts elsewhere.

Conclusion

1. MISC 106 should seek to implement, in full, the MISC 100 proposals for reductions in support for agricultural R & D.
2. The burden of cuts should fall on support for improvement of agricultural productivity and the associated advisory services.
3. As a consequence of this reduction, further savings in Government support for the agricultural advisory services should accrue.
4. MAFF should be directed by MISC 106 to ensure that reductions are made in the areas designated and not spread across the board.

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Ministry of Defence - status of current studies

1. The Advisory Council for Applied Research and Development (ACARD), commenting on Government-wide R & D funding plans revealed in the 1984 Annual Review of R & D, said that the justification for so much defence R & D should be closely examined. ACARD argued that current and projected levels of Defence R & D expenditure preempt a significant fraction of the Nation's R & D resources, especially in areas of actual or potential growth, and that the return to the economy of expenditure on Defence R & D is significantly less than that of expenditure on civil R & D in the same industrial sectors. The Prime Minister has asked Sir Robert Armstrong to advise her on how the issues raised by ACARD can be considered interdepartmentally.

It is expected that a group under Cabinet Office chairmanship will begin work when the current PES round is completed, and will report to Ministers by the end of June 1985.

2. The Prime Minister has also asked for there to be an examination of the case for transferring a sum (such as £20m) from MOD to the Science Vote, for basic or strategic research of interest to MOD to be undertaken through the universities and Research Councils. The proposal, made by Sir Keith Joseph, is now being examined by the Chief Scientific Adviser (Cabinet Office) together with the Chief Scientific Adviser (MOD) and the Chairman of the Advisory Board for the Research Councils. The likely outcome of such a transfer in terms of the strength of the science base in the country as a whole and the MOD's ability to use this base to fulfil its responsibilities for the defence of the country will be considered.

Again, it is expected that a report on this question will be available for the next PES round.

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Department of the Environment - need to protect R & D budget

Treasury have argued that the funds required for the rationalisation of the Building Research Establishment sites and for newly levied VAT on UKAEA research contracts should be found from offsetting savings, and that the "DOE - Other" programme as a whole should take its share of savings to be found across the board. Such an outcome would result in reductions in the volume of R & D being conducted in support of important Government policies (on radioactive waste disposal, housing, the inner city) and in R & D in support of the construction industry which already receives much less R & D support than other industrial sectors. I must advise against any cuts falling in this way and recommend that DOE R & D budgets are maintained at their current level.

SECRET

SCI
Econ 101: Public Expenditure R2

Structure of the assignment - 100 marks

The assignment is divided into two parts. Part 1 is a short answer question (20 marks) and Part 2 is a long answer question (80 marks). The short answer question is based on the lecture notes and the long answer question is based on the lecture notes and the article 'The Role of Government in the Economy' by J. B. Hicks.



Parker
Speakers
file

ANNEX A

2/10

06

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon George Younger MP
Secretary of State for Scotland
Dover House
Whitehall
SW1

12th October 1984

Dear Secretary of State

TERRITORIAL BLOCKS: NEEDS ASSESSMENT

At our PES bilateral we agreed to meet soon to settle terms of reference for the in-depth study of territorial needs assessment which I have proposed.

2. The attached draft terms of reference have now been prepared jointly by our officials, in concert also with Northern Ireland and Welsh Office officials. If you would like to have a word about them, I should like to try to do so over the next day or two, Perhaps you could let me know how you would like to proceed.

3. You are, I know, anxious to discuss also the nature of the collective decision that has to be taken, bearing in mind that the exercise will bring in Whitehall departments, as well as territorial departments and the Treasury. I entirely accept that this, and indeed the handling of the exercise throughout, are highly sensitive matters which will need careful thought - but I hope too that we can find a way to expedite the decision process.

4. I am sending copies of this letter to Douglas Hurd and Nick Edwards.

Yours sincerely

Richard Broadbent

for PETER REES

[Approved by the Chief Secretary]

DRAFT TERMS OF REFERENCE

"To the extent feasible, to devise and apply a methodology for the assessment of needs and standards of public services within the three territorial blocks, as presently defined for public expenditure purposes, and the comparable English programmes: account is to be taken of existing published and unpublished work - including the 1979 Needs Assessment Study - and of the implications of established practices and structures in each of the four countries, and any other factors special to each country. For any programmes now within a territorial block but not covered in the original study, with the exception of the social security programme in the Northern Ireland block, new methodology should be devised. Conclusions should be embodied in a report to be submitted by 15 June 1985: whether or not the upshot is a serviceable methodology, can be considered at the time."



H M Treasury

Parliament Street London SW1P 3AG

Switchboard 01-233 3000

Direct Dialling 01-233 8819

Mr R R Hillhouse (By Mufax)
Scottish Office
New St Andrews House
St James Centre
EDINBURGH EH1 3TB

11 October 1984

Dear Russell,

TERRITORIAL BLOCKS

I promised to set out in a letter our own present thinking on how an in-depth study of needs assessment in the territorial blocks might be run.

2. I must emphasise that these are only Treasury ideas at this stage. This is somewhat outside the normal run of Cabinet Office activity, and we are not yet fully apprised of their views.

3. Our present assumption is that the Cabinet Office take responsibility for the arrangements. This would offer you and the other territories a guarantee of neutral and impartial chairmanship. We would envisage an official steering committee meeting from time to time, whose membership it might be possible to limit, apart from the Cabinet Office chairman, to Principal Finance Officers in the territorial departments, and a Treasury representative; this committee would be backed up by a number of working parties, each dealing with one of the block expenditure programmes. The task remitted to the committee would be that set out in the proposed terms of reference, which (following consultation between us and the other territorial departments) are now being sent by the Chief Secretary to the three Secretaries of State concerned.

4. We expect that most of the work would be done in the series of working parties, which would run concurrently for most of the period of the study, and would need to meet frequently with an intensive work programme. The key members of these working parties would be representatives of the same departments as would participate in the steering committee, but it would be necessary to bring in other

(English) departments as work on the methodology required. Working papers would in general be submitted by the territorial departments and the Treasury. The role of the Cabinet Office chairmen, especially of the working parties but perhaps also of the steering committee itself, would combine a normal chairmanship function with, when appropriate, technical arbitration of disputes about methodology. The Cabinet Office would also steer the writing of the final report, which we envisage taking a month.

5. Throughout all aspects of the exercise there would be much attention to security, which would be the subject of careful discussion with the Cabinet Office before the exercise started.

6. I am sending copies of this letter to Melvyn Jeremiah (Welsh Office) and Brian Lyttle (DFP Belfast).

Yours,
Bill

W J E NORTON

CONFIDENTIAL



NDPT

BT
12/10

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Michael Jopling, MP
Minister of Agriculture,
Fisheries and Food
Whitehall Place
SW1A 2HH

12 October 1984

Dear Minister

REPORT ON AGRICULTURAL DEVELOPMENT AND ADVISORY SERVICES

Thank you for your letter of 9 October enclosing a copy of Professor Bell's report. I thought you would like to know my reactions both on substance and on procedure. *will request, if required*

On substance the report is, if I may say so, a major contribution to the development of policy towards ADAS. I would not endorse all of the assumptions the report makes about the Government's role vis-a-vis the agricultural industry or the justifications for continuing national agricultural support; but Professor Bell has recognised fully that ADAS's work must take proper account of the Government's general economic policies and of constraints upon public expenditure. This is particularly evident in the report's comments about charging for services provided (the full force of these comments is perhaps not brought out in the conclusions). I cannot but endorse Professor Bell's judgement that it is entirely appropriate that farmers, growers, consultants and whoever else in the industry avail themselves of advisory and promotional services should meet the cost of their provision; and his recommendation that further detailed consideration should be given to the possibility of charging for statutory and regulatory work.

As for procedure, I look forward to receiving the draft statement which you promise. But your letter makes no mention of the fact that the future level of provision for ADAS is an important element in our continuing discussions about public expenditure. As you point out, there remains a great deal of detailed work to be done in order to translate the principles discussed in the report into detailed decisions: I have always accepted that detailed changes in ADAS must be worked out carefully in the light of Professor

Bell's comments, and that it would be unrealistic to plan for any savings in the cost of the service before 1986-87. But you will recall that we have been asked to consider, in this year's Survey, all aspects of agricultural support and to establish in which cases objectives could be achieved at lower cost.

Against that background, I remain convinced that we should, in this year's survey, take credit for substantial savings in the two later years of the Survey period in expenditure on ADAS. My proposal is that we should plan for net reductions of £40 million for each of the two later years - based on Professor Bell's estimate (paragraph 14 of his report) that the full cost of ADAS advice and promotion in 1983-84 was £37.3 million, and on the forecasts which your officials produced earlier this year. Equivalent savings could of course be produced by a somewhat lower recovery rate together with charges for statutory and regulatory work.

I am copying this letter to the Prime Minister, the Lord President and the Secretary of State for Trade and Industry (in view of their involvement in earlier discussions on this subject), to the Secretaries of State for Scotland, Wales and Northern Ireland, and to Sir Robert Armstrong.

Yours sincerely

Richard Broadbent

for PETER REES

[Approved by the Chief Secretary]

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From the Minister's
Private Office

cc NO under report
To ~~106~~ X
Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

File

Andrew Turnbull Esq
10 Downing Street
London SW1

12 October 1984

Dear Andrew

As you requested, I enclose a copy of Professor Bell's report on ADAS. You may also find it useful to refer to the note that my Minister has circulated to the members of MISC 106, giving his preliminary reactions to the report.

X | As I told you over the telephone, we are giving the report extremely limited circulation to named persons only, and I would be grateful if you would ensure that it is handled with particular care.

Yours ever
/r

C I LLEWELYN
Private Secretary

MANAGEMENT-IN-CONFIDENCE: PERSONAL TO THE NAMED ADDRESSEE

COPY NO: 36

ADDRESSEE: 10 DOWNING STREET

REPORT OF A STUDY OF ADAS

BY

ITS DIRECTOR GENERAL,

PROFESSOR RONALD L BELL

SEPTEMBER 1984

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APPENDICES

1. List of visits
2. List of written submissions
3. List of meetings with outside organisations
4. Current organisation and functions of ADAS
5. Information Technology

I INTRODUCTION

1. On joining the Ministry last March as Director General of the Agricultural Development and Advisory Service, I was asked by the Minister, the Rt Hon Michael Jopling, MP to carry out my task of familiarisation with the Service in such a way as to enable me by the end of six months, to let him have my views on the future shape and direction of the Service. My study was given the following terms of reference:

- (i) To assess and define the importance of the main services provided by ADAS having regard to:
 - (a) the benefit of those services both to the Ministry and its policies and to the agricultural, horticultural and related industries;
 - (b) the quality of the services;
 - (c) the net public cost of carrying them out;
 - (d) any similar services provided elsewhere;
 - (e) the Government's wider economic policies.

- (ii) In the light of this assessment to examine whether:
 - (a) ADAS has the right priorities and whether there is a need for change in the present range and level of services;

- (b) any of the services currently provided by ADAS could in the future be economically and effectively provided by the private sector either direct or under contract to ADAS; and
- (c) there is scope for passing on some or all of the cost of any ADAS service to the users rather than the taxpayer.

2. In carrying out this remit, I have been supported by a small team **comprising** Mr C R Bodrell, Head of Management Services Division, Mr K B Baker, Deputy Regional Veterinary Officer, Leeds, Mr D E Bawcutt, Assistant Regional Agricultural Officer, Wolverhampton and Mr M J Ibbotson, Principal with specialist background as an Economic Adviser.

3. Conduct of the Study - It was clearly necessary for me to get to know the Service as quickly and as comprehensively as possible. This has involved an intensive programme of visits and discussions designed to cover all aspects of ADAS work both at Regional and Divisional and at the headquarters levels. Whilst it was not possible in the time available to visit every ADAS Unit, a selection of Regional, Divisional and Area Offices has been covered as well as the major laboratories of the Agricultural Science and Veterinary Services and also the Experimental Farms and Stations. Visits have/also been made to Wales, Scotland and Northern Ireland for discussions with colleagues in ADAS and the other Agricultural Departments.

A list of the visits undertaken is at Appendix I. I have had personal discussions with about 550 ADAS staff and have met many more.

4. The Ministry's announcement of my appointment and the remit which I had been given included an invitation to any interested organisation to submit views and comments.

Written views have been received from numerous organisations and individuals. These are listed in Appendix 2. There has also been a number of meetings - listed in Appendix 3 - with some of those who submitted written evidence and discussions with members of the Minister's Eastern and South Eastern Regional Panels.

5. Members of my support team have joined me in the range of visits and discussions and have carried out a number of desk studies of key topics. A great deal of ground has had to be covered in a relatively short time, but I believe that I have gained a sufficiently clear picture of this wide-ranging Service to be able to propose a general strategy for ADAS as we move into the second half of the 1980s. My report avoids the discussion of detail because many of my proposals will require further study and investigation before action can be taken.

II CURRENT ORGANISATION, AIMS AND OBJECTIVES, AND FUNCTIONS OF ADAS

6. Organisation - ADAS was formed in 1971 with the merging of the former National Agricultural Advisory Service (NAAS), the

Agricultural Land Service, the Land Drainage Service and the State Veterinary Service. ADAS is staffed by professional, scientific, technical and industrial staff and organised into four services: Agriculture Service, State Veterinary Service (SVS), Agricultural Science Service (ASS) and Land and Water Service (LAWS). Each is headed by an officer at Grade 3 level. Apart from the ASS which operates at Regional level, the other Services operate at Regional, Divisional and Area Office levels in England and Wales. Apart from the field staff of the SVS, ADAS does not operate in Scotland.

7. There are, currently, 4,800 staff in ADAS distributed between the four Services as follows:

Agriculture	1628	(33%)
Veterinary	1447	(31%)
Agricultural Science	1110	(23%)
Land and Water	622	(13%)

8. Aims and Objectives - The role of ADAS in line with MAFF aims is to foster an efficient, competitive, market-orientated and environmentally conscious agricultural industry in England and Wales, particularly by promoting the transfer of relevant technological information and/^{the} adoption of sound business, marketing and husbandry practices.

9. Functions - In pursuit of these aims and objectives, the principal functions of ADAS are to:

- (i) provide information and advice to farmers and growers to help them develop technically efficient and financially sound farm businesses;
- (ii) identify problems requiring further investigation and to carry out the necessary research and development;
- (iii) contribute to advice given to Ministers and administrative colleagues on the scientific, technical and business implications of policy proposals and their implementation;
- (iv) assist in the execution of Government policy measures such as plant and animal health and hygiene regulations, land drainage and other capital grant schemes, disease eradication, and safeguarding agricultural land in relation to other land uses.

10. A fuller description of the functions of each Service is at Appendix 4.

11. These functions, which might succinctly be classified as statutory, advisory, and research and development, currently consume the following resources expressed in man years:

Functions

<u>Service</u>	Statutory Regulatory & Scheme (man years)	Advice & Promotion (including Agricultural Services Scheme) (man years)	R & D (man years)
Agriculture	287	650	691
Agricultural Science	254	304	552
LAWS	284	257	81
Veterinary	941	233	273
Weighted Average (per cent)	37%	30%	33%

12. The exercise of these functions clearly reflects the substantial measure of Government involvement in the agricultural sector. A question, fundamental to my study, is whether the objectives of ADAS which so closely reflect the objectives of the Ministry towards the agricultural industry could be more effectively and efficiently achieved by other means and, in particular, by a lesser degree of public sector involvement. I have considered this question in relation to each of the three main functions of ADAS and the report discusses and recommends a number of changes. My overall conclusion, however, is that the continuing need for a substantial public service to meet the objectives is inescapable given:

- (i) the high content of statutory and regulatory work;
- (ii) the fact that the industry has to operate in the extremely competitive EC environment

with other Member States providing direct support of one sort or another to their industries;

- (iii) the widely scattered and disparate nature of individual farm businesses which need to be kept up with technological progress and cannot reasonably be expected to do this for themselves;
- (iv) the need for a service which provides impartial advice; and
- (v) the need to provide advice which pays proper regard to environmental and other public interests.

13. Importance of main services provided - ADAS provides a range of services both to the industry and to the Ministry, the importance of which cannot be measured on a single scale. The Service has, however, established priorities in carrying out its functions. ADAS, as its name suggests, has two main functions, firstly of developing agricultural technology to the point where it can be put to use by the industry and, ^{secondly,} in ensuring that this happens through its promotional and advisory activities. However, there is a symbiosis between these two functions and the statutory function to which the Service is obliged to give top priority. This last-named function currently occupies over one third of its manpower resource. The advisory and promotional effort which to a large degree has been demand-led commands second priority and R & D comes next. That said, as the table in paragraph 11

shows, the contributions to these three main functions vary considerably between Services. Thus, the SVS is most heavily involved in statutory work and the ASS in R & D, whilst Agriculture Service provides a particularly large contribution to the front line advisory effort. LAWS effort is divided fairly evenly between statutory and advisory work, with some R & D back-up.

14. The total net cost of ADAS in 1983/84 was £122.7m which includes the cost of support services both at Headquarters and in the Regions. £37.3m of these costs can be attributed to Advice and Promotion, including the Agricultural Services Scheme, £45.6m to Statutory, Regulatory and Scheme work and £39.8m to Research and Development. ADAS generated receipts of £7.3m in 1983/84 for the chargeable services it provided and for the produce which it sold from the EHF's and the EHSs.

15. During 1983 the value of final agricultural and horticultural output in the UK was of the order of £10,600m and its contribution to the gross domestic product was 2.1%. Our self-sufficiency in the products which we can produce in this country is now about 76%, compared with 67% in 1970/71. Moreover, the volume of exports has grown very substantially in this period. This is a reflection of the considerable increase in yields which have occurred and of the increase in productivity which the industry continues to achieve. This increase in productivity is estimated at 2% per annum on average. While it is not possible to assess in any detailed way the contribution which ADAS has made to the increases in agricultural productivity in this country over the years there can be no doubt that,

without it, this increase would not have been achieved. Many factors, including capital grants have of course made their contribution. But developments in technology, improvements in animal health, livestock and crop husbandry techniques and the production of new and better varieties have been extremely important and ADAS has had an unparalleled role in taking results of research from private and public sector laboratories, developing them and transferring the new technology to the industry.

III THE FUTURE REQUIREMENTS

16. Because an organisation is recognised as having made a significant contribution to the improved efficiency of a national industry it does not follow that the full range of services that it provides should continue to be provided or that the whole cost of such services should necessarily be borne by the taxpayer. In making my own assessment of what I see as a future requirement for a government-sponsored development and advisory service, I have had regard to the likely economic framework within which such an organisation would function over the next decade and the interests which the organisation would be required to serve.

17. The National Interest and the EC - During and since the war a major element of Government agricultural policy has been to encourage economic production and productivity though with much greater emphasis in recent years on cost-effectiveness and on the needs of the market. Of late there has been

an increasing volume of criticism of the cost of agricultural support and the production of large surpluses of key commodities. The Government has been pressing in Brussels for reductions in the real level of Community support. The more success there is in achieving this goal, the greater will be the need to foster the highest levels of efficiency in British agriculture. Efficiency is of course, not a matter of producing the highest levels of output regardless of cost, but of achieving the most favourable ratio of input to output having regard to the needs of the market.

18. Membership of the Community, places British agriculture in a highly competitive environment. Member countries give significant support to their agricultural industries (including the provision of research, development and advisory services) over and above that arising from the CAP. Government policy may, therefore, be expected to continue to encourage a healthy agricultural and horticultural industry in the United Kingdom capable of maintaining its competitiveness within the Community. The basis of this will, as previously, be the application and improvement of known techniques and the search for, and development of, new technology. This suggests that it will continue to be in the national interest for government to provide support for agricultural and horticultural

research and development and to ensure that the industry has access to information on new techniques and technology with which to maintain its efficiency and enhance its competitive strength.

19. But the national interest is concerned not simply with the economic health of the industry. The impact of modern farming methods on the countryside and on wildlife and farm animals has attracted criticism from a society which is showing increasing awareness of environmental and welfare issues. Section 41 of the Wildlife and Countryside Act 1981 placed upon Agriculture Ministers the duty to provide advice on the conservation and enhancement of the natural beauty and amenity of the countryside. This need has not diminished. Indeed concern about the effects of modern agriculture on the environment continues and Ministers accept that this concern must find a positive response in government.

20. The Needs of the Industry - The pressures facing the farming industry during the remainder of the 1980s are not hard to predict. Community measures designed to reduce surpluses will force producers to adapt ever more closely to market realities.

The quest for increased efficiency will accelerate. Efficient producers may be expected to continue to expand their businesses forcing the less efficient to look for alternative enterprises and additional sources of income or to leave the industry.

The need to pay closer regard to environmental questions seems bound to develop. The requirements of the market for top quality, well presented produce, will continue to increase encouraged by the precise demands of the large retail outlets and of the consumer and by the work of Food From Britain.

There is also a burgeoning interest in the health aspects of the national diet which will increasingly be brought to bear on the type and quality of agricultural produce that is required. These developments are not entirely new, but the pressures for substantial cut-backs in Community spending on agriculture and the reality of the recent measures in the milk sector mark a major change that farmers perceive as a shift in policy which, combined with the other pressures mentioned above, signal more challenging times ahead.

21. In these circumstances, farmers and growers may be expected to have even greater need of expert advice of a kind which ADAS is well equipped to provide. This is the strongly held opinion of many who have submitted views. The heavy demands placed upon the Service following the introduction of milk quotas provide clear evidence of the industry's dependence on ADAS help and guidance. Very substantial resources are being devoted to helping farmers to adapt to the new circumstances.

22. The agricultural supply industry embracing agrochemicals, veterinary pharmaceuticals, feeding stuffs and machinery is likely

to come under the same pressures as agriculture. The ^{ever} increasing quest for improved efficiency in farming coupled with safety requirements demands extensive cooperation with the public service and in particular with ADAS. ADAS has a close working relationship with the agro-chemical industry under the Pesticides Safety Precautions Scheme and great reliance is placed upon ADAS information services, monitoring of pests and diseases and the warning schemes. There are also the private sector agricultural consultants who provide a limited advisory service to producers and who rely heavily on the specialist advice and services provided by ADAS.

23. The Requirements of Other Organisations - ADAS interacts with a large number of other organisations which have an interest in the agricultural scene. These include the Nature Conservancy Council, the Countryside Commission and the Farming and Wildlife Advisory Groups (FWAGS) whose main concern is with the effects of agriculture on wildlife and conservation; and the Agricultural Training Board which is concerned with the training of farmers and farm workers. It also has links with planning authorities and the Department of the Environment in furtherance of the Minister's land use policies and with the NCB in connection with restoration of open-cast coal sites. There is no indication that the demands of these organisations upon ADAS will diminish. Indeed, bodies like the NCC and the ATB have taken the opportunity of this Study to stress the importance to them of greater cooperation with the Service.

24. The Requirements of the Ministry - Within the Ministry, senior ADAS officials contribute practical advice to policy makers and Ministers based on the breadth and intimacy of the Service's knowledge of the industry gained through its daily contact with farmers and farming at all levels. Of course, much information is also obtained through the major organisations such as the NFU, the Marketing Boards and the various bodies like the MLC as well as the professional organisations. But this cannot replace the impartial, in-house contribution which ADAS provides.

25. The Service also performs the major task of implementation of a wide range of statutory functions, some of which - like the Milk and Dairies Regulations - are obligatory for all dairy farmers, while others, like the Maedi Visna Scheme in the animal health sphere and the Capital Grants Schemes are there for farmers who choose to avail themselves. Some of these functions might be capable of being performed by other official or Government agencies, and a number of options for hiving off have been examined in recent years. But the task of carrying out these functions creates opportunities for advisers to influence the efficiency of the industry and to that extent fits well with the objectives of the Service. More importantly, policy makers in the Ministry do not consider that these tasks could be performed better by other agencies; indeed the integration of policy making and its execution within the remit of one department probably leads to the most efficient administration of such policies. In the course of the manpower economies in recent years ADAS has been required to reduce its

resources committed to implementing statutory functions to the minimum consistent with providing a reliable service; but this work has been and continues to be treated as a first priority.

IV ADAS RESPONSE TO THE REQUIREMENTS

26. Research and Development - There are two very strong reasons why ADAS needs to continue to carry out development work. Firstly it is vital that the results of agricultural research carried out in the UK or elsewhere should be developed to the point where they can be utilised by or on behalf of the industry. Secondly, the ability of ADAS to carry out its statutory and advisory functions depends very much on its being actively involved with the latest technology.

27. Because of the importance of development work, it is important that, if funds for R & D are being reduced, ADAS should concentrate its efforts on the D end of the R to D spectrum. The distribution of public funds as between research and development does not adequately reflect the fact that development work is very much more costly than research. It is up to ADAS to ensure, so far as it can, that most of its R & D efforts go into converting research results into useable technology. I say "most" rather than "all" because it is important that a sufficient effort be devoted to the monitoring of development work in other countries. There is evidence that inadequate attention has been given to this aspect.

28. A very large fraction of all of the R & D which is carried out in ADAS is concentrated either in central laboratories

(CVL and satellites; Harpenden, Slough, Tolworth, Worplesdon; FDEU and the Farm Buildings Group), on the Experimental Husbandry Farms and Horticultural Stations, or in the Regional Science laboratories. In order to ensure that the work here is on topics of highest priority the procedures for approving the initiation and continuation of such work should be brought much more closely into line with those used for the commissioning of research which is contracted out. Further, to ensure that this in-house work is of the highest quality, that it is well coordinated with relevant work in Universities and AFRC Institutes, and that it is likely to produce results of benefit to the industry, it should be inspected periodically by an external review group comprising academics, members of AFRC staff and representatives of the industry.

29. The procedures discussed above are neither feasible nor necessary for the many small investigations which are carried out by staff in VI centres and by members of staff of Agriculture Service and LAWS based in Divisional and Area Offices. There is also a range of work carried out in the regional laboratories of the ASS which do not form part of a national programme. This work should not be classified as "R & D", valuable as it is for providing solutions to important problems. Rather, it should be seen as part of the advisory or statutory work in which these staff are primarily engaged. They should be encouraged to continue with such investigations as part of their service to the industry and as part of their Continuing Professional

(CPD)

Development/and training. But the effort expended on these activities at present is greater than their degree of priority would seem to justify. A useful guideline might be to place a ceiling of not more than 15% of these staff's time on CPD - this provision to include all elements of training. Careful management of this limit should lead to some saving in posts.

30. The transition from research to utilisation does not consist of a simple sequence of steps but rather of a complex series of iterations. For this and other reasons it is necessary for there to be a genuine partnership between those responsible for the research and those for the development. This is not easy to achieve but there is an excellent opportunity for progress to be made on the experimental centres. This extensive facility encompasses the whole range of farming types, soil types and geographical situations found in England and Wales. Some are better focussed and located than others. They do, however, provide a very special situation where new elements of technology can be tested as part of a complete farming system. To fully exploit this opportunity their terms of reference need to be made more clear, the staffing strengthened by the redeployment of specialists from other parts of ADAS and their efforts focussed on fewer projects. They should build up existing contacts with AFRC Institutes to ensure maximum benefit from research. At the other end, there is a pressing need to ensure that their own results are passed on to their colleagues and are demonstrated in a truly commercial situation through greater exploitation of the Development Farm concept. Steps should also be taken to ensure that the results of their work are ^{rapidly} written up for publication

in refereed or, if appropriate, other journals having a wide distribution.

31. A further stratagem for improving the rate of adoption of the results of development work is for ADAS to seek to involve the industry in the identification of and payment for appropriate projects which would be of national benefit. Since the pay-back time on development work can be relatively short it should be easier to attract external funds for development work than for research. I recognise, however, that the kind of development work that is most likely to attract commissions from the private sector is that related to products rather than production systems. ADAS should endeavour to exploit the opportunities. The possibility of raising revenue for R & D via a levy on the industry is mentioned in paragraph 51.

32. Advice to the Industry - The Service's role, which it is uniquely placed to fulfil, of interpreting and communicating the results and application of research to/^{the}industry and in focusing on environmental issues seems beyond doubt. It would be irresponsible to think in terms of abandoning this role without there being an adequate alternative in sight to take its place. It should continue to be the aim of the Service to ensure the speedy adoption of new and existing technology. In part, this will continue to be met through responses to problems posed by individual farmers and others in the industry / but I believe the Service could be more positive through active promotion of development work findings. The adoption of the advisory project approach, advisory centres and well conceived demonstrations and conferences facilitate this thrust. In many instances it is possible for ADAS to work in conjunction with other organisations in these activities and this should be encouraged.

33. Although the individual farm visit is an effective mode of operation there has been some shift of emphasis towards other techniques of getting over advice to farmers. Nonetheless there remains scope for further developing these techniques. In particular, more effort should be devoted to group activity. Such groups might be organised by farmers or other agencies eg the ATB, or the MLC, and the Service should actively seek to exploit these opportunities rather than duplicate activity or fail to respond to openings created by others. The industry will also be looking to obtain information and advice very quickly through use of modern information technology and the Service must be equipped and ready to meet this demand. I deal with this subject at greater length in Section V.

34. With the growing interest in environmental questions, the aim of the Service must be to reconcile the purely economic interests of the industry and the individual farmer with the wider public interest. Since the enactment of the Wildlife and Countryside Act, 1981, the Service has been grappling with this problem but there is need to encourage changes of attitude and appreciation among all advisers employed in the field. Sound conservation principles will need to be incorporated into all aspects of agricultural and horticultural practice; similarly in the urban fringes, farmers need encouragement to take the lead in improving access to the countryside and helping to acquaint the public with all that is involved in food production. No other organisation is as well placed or qualified as ADAS to take on these tasks. I also see scope for the State Veterinary Service and the Veterinary Investigation Service to play a more

active role in the promotion of animal welfare and preventive medicine, in cooperation, as appropriate, with the private practitioner.

35. I foresee a developing need for farm business, socio-economic (including diversification) and environment-related advice in the wake of adjustments to the CAP. The private sector may be expected in certain parts of the South and East of England to continue to provide a certain amount of farmer-sponsored consultancy for arable crops. Their contribution is less well developed in the livestock sector. But farmers and others in the industry are going to need the specialist, scientific knowledge which ADAS commands and within the Service a higher priority must be given to the need for all AAO's, HAO's and some LAWS personnel to develop business management, socio economic and conservation skills to meet the increasing demands for advice of this nature. The development of specialisation at the AAO level and the degree to which it has been taken within certain disciplines is encouraging.

36. In addition to giving technical advice, the Service is capable of providing services to the industry that are only partially met by the private sector. The VIS and Agricultural Science Service each provide diagnostic and analytical services on a chargeable basis. My impression is that these services are not vigorously marketed. Moreover the number of plant and

soil samples which are examined and charged for in support of advisory work seems disappointingly low. I believe that this owes something to the current system of collecting charges before results are provided. The Agricultural Services Scheme should be thoroughly reviewed with the aim of finding out what the industry requires and of seeking to improve the speed of service and to increase the volume of throughput. The review needs also to examine the pricing policy both as to the levels of charges and methods of payment. I have noted the recommendations of the VIS study that the system of charging for diagnostic work should also be reviewed.

37. Advice to Policy Divisions - As mentioned in paragraph 25, in a department like MAFF, Ministers and policy divisions need constant access to scientific and professional advice. The department's record of policy formulation based on science and technology is a good one, particularly in the field of animal and plant health where, of course, much of the work of the Service is statutorily based. There are, however, areas in the Ministry where the links with ADAS are not as well forged and where policy managers acknowledge that there is scope for greater cooperation and consultation.

38. As MAFF's science and technology arm, ADAS provides the basis of the Department's scientific input into policy formulation both at home and in Brussels. Every opportunity should be taken to strengthen this. There is a twofold need: firstly, for policy divisions to be more actively aware of the body of expertise

which ADAS has in technical matters and to use it; secondly, for ADAS staff, particularly those at Headquarters, readily to cooperate in the process of policy formulation and more actively to orientate their duties to that end.

39. As a decentralised organisation, one of the strengths of ADAS is its interaction with the farming community. It is thus well placed to monitor the performance of the industry and to have some influence over that performance. This offers the opportunity for ADAS to be active in promoting and furthering MAFF policies.

40. Statutory, Regulatory and Scheme Work - As indicated in paragraph 26, ADAS will continue to be required to undertake the numerous statutory, regulatory and scheme activities pertaining to agriculture, horticulture and animal and plant health. This considerable commitment seems unlikely to diminish.

41. There are certain aspects of these activities which need to be highlighted. Firstly, such work demands and receives the highest priority, whilst its volume is often unpredictable. Secondly, I suspect there is the tendency to devote undue time to it, in an effort to ensure that all eventualities are covered. This open-ended commitment detracts from the time available for other activities and means should be sought to minimise this effect. There are a number of ways in which this could be done.

42. Firstly, there is the information highlighted in our management information systems /regarding manpower effort which the various schemes currently absorb. Systematic study of this information should lead us to question whether or not the effort involved is consistent with the aims and purposes of individual schemes. Secondly, the management of staff who devote only a part of their time to carrying out a statutory function needs to be tightened up possibly through the prescription of average time allocations per case and more careful monitoring of performance. These are thoughts that need further consideration in consultation with senior management in the department.

43. The possibility of raising charges for statutory, regulatory and scheme work justifies careful consideration. In principle there is no reason why charges should not be introduced for many of these functions. I recognise however that many of the schemes are of a sensitive nature involving the control of animal diseases where the public interest could be prejudiced.

V IMPLICATIONS FOR THE FUTURE WORK OF ADAS

44. All that I have seen, read and heard in the last six months convinces me of the continuing need both within the Ministry and in the industry for a strong ADAS. There is, however, need for some directional change both in the Service's coverage and management of its R & D effort and in its advisory and promotional activities. There is also scope for the Service to attract funds in both these areas as well as, possibly, in its execution of its statutory functions. These possibilities are discussed at greater length in this Section of the report.

45. Marketing of Services - ADAS has tended to be a reactive organisation, responding to the demands and needs of the farming industry. What is now required is a positive, pro-active approach to its activities, and this approach must embrace the concept of marketing in all its aspects starting with an exploration of what the customer wants.

46. ADAS has a great deal to offer. Advice, promotional events and technical publications are generally of immediate benefit to the individuals concerned. Advice is sought in the expectation that, if followed, it will benefit the farm business. Attendance at promotional events and the reading of advisory literature is similarly motivated. In this sense, none of these services provided by ADAS are any different from the many others which individual farmers purchase. In principle, therefore, it seems entirely appropriate that farmers, growers, consultants and whoever else in the industry avail themselves of these services should meet the cost of their provision.

47. The introduction of charges for advice will, however, require amendment to the Agriculture (Miscellaneous Provisions) Act 1944. The Act provided for the establishment of the National Agricultural Advisory Service for the purpose of providing technical advice "free of charge". Section 41 of the Wildlife and Countryside Act refers to the requirement placed upon Ministers by the 1944 Act and extends the duty to provide free advice to include advice on the conservation and enhancement of the natural beauty and amenity of the

countryside. It seems unlikely that Ministers would wish to introduce charges for the latter though in the nature of things, this type of advice is inexorably linked with technical advice affecting the whole farm business. This will need to be taken into account in determining the approach to charging as well as the level of cost recovery that might be appropriate.

48. It has also to be recognised that the introduction of charges for a service which for so long has been provided free is bound to have undesired effects. Dependent on where the level of charges is pitched, there could be a substantial fall in demand which could jeopardise the dual objectives of maintaining a competitive, domestic industry, whilst seeking to influence those decisions of farmers and others which could otherwise have deleterious effects on the environment. The relationships between advisers and clients are likely to change and some of the good features attaching to a free service are likely to be lost forever. Farmers will be less inclined to cooperate with ADAS, for example, in permitting the free use of their farms for promotional events. There will be difficulties for advisers in balancing the demands of the department with the demands of the paying customer. Many ADAS staff are, naturally, very apprehensive about the changes in approach that will be required both in terms of "marketing" their services and in charging for them. The industry will also share this apprehension. If, therefore, Ministers decide that it is right to introduce charges for advice, it will call for careful planning and gradual introduction. It would clearly not be

sensible to look for full cost recovery at once. Indeed, it might well be preferable to make clear that in the national interest, the Government intends to continue to provide a specific level of service and to aim for recovery of no more than a proportion of its cost. This would allow charges to be fixed at levels which the market will bear and avoid the risk of killing off the Service.

49. There is, also, considerable concern that the introduction of charges across the board would effectively preclude some producers from gaining access to information and advice. This raises the need to consider whether a system of differential charging might be feasible. The difficulties of operating such arrangements should not, however, be under-estimated and it is suggested that this option should be thoroughly examined as part of the further studies that will be necessary before proposals for implementation of my recommendations are finally made.

50. An alternative to raising charges against the provision of advice to individuals is to seek to recoup that proportion of costs which might be thought appropriate via a compulsory levy on all agricultural/^{output.} This would avoid many of the difficulties foreseen in paragraphs 46 to 48, but cuts across the principle that the individual beneficiary should pay for the advice/service that he receives. A levy system would also do nothing to stimulate the provision of private sector services similar to those provided by ADAS. The case for raising levy revenue to help

finance R & D is somewhat stronger because the benefits are less obviously restricted to individuals and serve the general good of the agricultural industry. The Minister may wish to have the levy option further examined.

51. Privatisation and Contracting Out - ADAS already contracts out a significant proportion of veterinary work to private practitioners. The opportunities for moving any further significant areas of ADAS work into the private sector appear to be very limited at present. A policy of direct charging for the services provided would be likely, however, to encourage the development of private sector agencies capable, in time, of taking over some of the functions. At this stage, that eventuality can be seen only as a possible long term consequence of a charging policy rather than as a declared objective.

52. There could be some research activities which would benefit from being hived off as a consequence of an orientation towards development. Though these are likely to be very limited, they are worthy of further study.

53. There appears to be little, if any scope for privatising or contracting out of statutory and regulatory functions. One or two of the more obvious possibilities have, I understand, been explored recently eg the testing of samples for IBAP schemes, where privatisation has been found to be more costly than retention in-house.

54. Information Technology - Throughout ADAS, only a modest start has been made with the application of information technology. Hitherto, all ADAS services have relied almost exclusively on traditional methods of communication both within the Service and in their contacts with the industry. The Service has pioneered the presentation of agricultural information through Prestel, but only a small proportion of advisory staff and farmers actually have access to this service and greater emphasis now needs to be given to extending the range of information provided by such means.

55. I am convinced that there are great opportunities which the Service must grasp to step up its efficiency and effectiveness by making far greater use of information technology. As explained in Appendix 5, this will call for a considerable investment in hardware, software and manpower. A substantial training investment will also be required to ensure that the new technology is well used. Once the databases have been set up, however, and this will take up to five years, the possibility of staff savings can be foreseen as the Service uses the new technology to improve its efficiency in terms of speed and accuracy of response both to in-house work and to the demands of the industry. There is the added advantage that, where charging is in operation, any computer based information service has an intrinsic capability for automatic invoicing.

56. As information technology develops I foresee a reduced need for ADAS advisory publications. Currently there are too

many titles covering too many types of publication. More attention needs to be given to market requirements and this suggests a move to more readable, attractively presented and aggressively promoted material. Other than for awareness literature, all publications should carry a price and whenever possible farmers and growers should be encouraged to join annual subscription schemes.

57. The telephone information services are a useful adjunct to advisory activity but more effort is required in promoting these services and in improving their timeliness and availability.

58. Local radio also represents a valuable opening for ADAS information. This medium could be more fully exploited through the greater use of integrated promotional programmes in addition to news services.

59. Deployment and Management of Staff - The major resource of ADAS is its professional and support staff whose salaries and expenses account for a very large part of the total cost of the Service. If the proposals outlined in this report were adopted it would be necessary to examine in detail their implications for the deployment and management of the staff. In the short term, there is no requirement for a major reorganisation as a necessary pre-condition for implementation. Certain changes of a specific and limited kind would be necessary and these are detailed below.

60. As already suggested I envisage economies in staff once the turnover to computer-based information supply has been fully developed. To get to this point however there will be the requirement, in the immediate short term, for a substantial redeployment of existing specialist staff to build up the databases and to develop applications software. This implies some loss to the front-line service of specialist expertise in the short term, but I believe that this is an investment well worth making to achieve the leap forward that the turnover to computer-based information services will mean for the Service and the industry. Appendix 5 explains in greater detail how I envisage this redeployment of effort working.

61. Another area in which a redeployment is called for is in that of the experimental centres. I outline in paragraph 29 the opportunities which I see for better use of this resource. To make best use of the unique opportunity which the centres offer requires the staffing to be strengthened by the transfer of appropriate specialists from Agriculture Service, Science Service and possibly LAWS and SVS also.

62. In paragraph 35 I have referred to the requirement for greater involvement by the Service in conservation, farm animal welfare and socio-economic activities. This calls for some redeployment of effort but the requirement is not so much for more specialist staff as for strengthening the front-line advisory effort with better preparation for and encouragement to pursue these aspects of advisory work. There is the requirement for the deployment of additional staff resources here.

63. As I have said, I believe that the new approach that I have set out can be implemented through the present structure of the Service. But in the longer term I can foresee that changes in the approach to our work may lead to the need for organisational changes within the Service. For instance, a feature of ADAS which I find very surprising is the extent to which it is organised on a discipline basis rather than functionally. Whether or not this derives from the academic background where the Service had its origins, I believe that an organisation which is as "downstream" as ADAS should have a greater emphasis on a functional grouping of its staff with a greater delegation of responsibility to these groups so as to enable them to respond effectively to the needs of their customers. I should like to give these thoughts further consideration in consultation with senior colleagues before developing them further.

VI CONCLUSION AND RECOMMENDATIONS

64. During the extensive programme of visits and interviews which I have made as a preparation for this report I have been struck by the enthusiasm and dedication of ADAS staff and by the high esteem in which the whole Service is held by the industry which it serves. Clearly it has rendered to that industry a most valuable service. The needs of the industry are now entering a period of change. At the same time, with pressures on public spending, the whole of the Government Service is seeking ways of carrying out its functions more economically and more effectively. ADAS must respond to both these requirements. It has in the past shown the capacity to meet changes in its

stride and I believe that it can do so again. Given that the required changes are well articulated and carefully managed ADAS has a challenging future to which it should look forward with confidence.

65. The following recommendations are confined to matters of broad principle concerning ADAS functions. If the principles are approved it will be necessary to work out the details of and methods for their implementation.

66. Research and Development - Most effort should be concentrated at the D end of the R to D spectrum. Any work which is very far from this end or which is carried out in small units of doubtful viability should be critically examined with a view to its termination or to its being hived off. (Paragraphs 27 and 52)

67. All of the R & D which is carried out at central or regional laboratories/units/experimental centres should be subject to the same commissioning arrangements as are applied to external contractors and should be subject to periodic external review. (Paragraph 28)

68. The widely-distributed investigational work carried out by staff in the Divisional and Area Offices and in VI Centres

should not be classified as R & D. It should be seen as part of the advisory work of these staff and as part of their Continuing Professional Development, managed locally and subject to a prescribed time allocation which taken together with other training should amount to no more than an average of 15% of their time. (Paragraph 29)

69. The terms of reference of EHF's and EHS's should be sharpened up and their staffing enhanced by the inclusion of appropriate specialists drawn from all ADAS disciplines. (Paragraph 30)

70. Improved interactions between the experimental centres and the Institutes of AFRC should be sought. (Paragraph 30)

71. Industry should be invited to help identify development projects and to contribute to their cost. (Paragraph 31)

72. Greater attention should be paid to the need to monitor development work carried out overseas. (Paragraph 27)

73. Advice and Promotion - A "marketing" approach should be adopted in the provision of all advice (including publications) and promotion to the industry. This should involve continual consideration of what the customer wants and is prepared to pay for. (Paragraph 45)

74. Wherever there is a clearly identifiable and substantial benefit to the customer Ministers may like to consider whether the customer should bear part or all of the cost of providing the service whether by direct charging or by general levy. (Paragraphs 46-50)

75. There should be a commitment to the principle of using computer-based information technology as the method by which a great deal of information and advice is provided to the industry in the late 1980's. A substantial redeployment of effort should now be made in all four Services of ADAS so as to prepare for the transition. (Paragraphs 54-55)

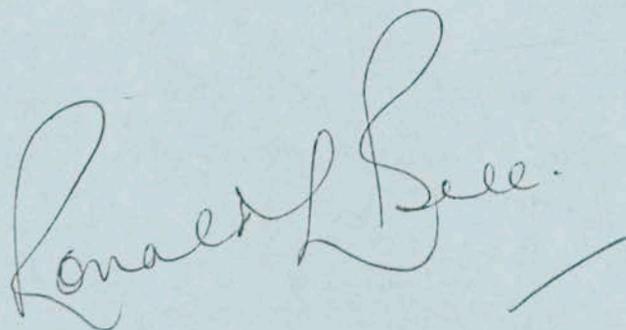
76. Whilst there will be a continuing need for advice which helps farmers and growers to maintain their competitiveness a certain proportion of advisory effort should be earmarked for guiding them in conservation and animal welfare aspects. (Paragraph 62)

77. All ADAS officers should recognise their role in monitoring the performance of the industry on behalf of MAFF so as to provide information to guide policy decisions. ADAS as an integral part of the Ministry should actively promote and further Ministry policies. (Paragraphs 37-39).

78. The role of HQ officers of ADAS in providing technical advice to policy divisions on both the formulation and application of policy should be more extensively recognised and such cooperation encouraged. (Paragraphs 37-39)

79. Statutory, Regulatory and Scheme Work - ADAS should continue to carry out this work. (Paragraphs 25 and 40). The possibility of charging should however be examined in the case of each scheme so as to reveal where recoupment of costs could be made without prejudice to the public and national interest. (Paragraph 43)

80. Final Remark - Much of what is said in my report will not surprise members of the Service nor the farming community. There is, I am sure, a realisation that directional changes are necessary both in the industry and in the service which ADAS will be required to provide. On the other hand, I do not under-estimate the problem of managing the transition to a more commercially-orientated Service which will call for imaginative leadership at all levels and a not inconsiderable change of approach by all staff.

A handwritten signature in cursive script, reading "Ronald L Bell", with a horizontal line underneath.

RONALD L BELL

VISITS TO ADAS OFFICES, LABORATORIES, ETC

Luddington EHS (A)	24.4.84
Midlands and Western Regional Office (Wolverhampton) (A)	24.4.84
Stafford Area Office (A)	25.4.84
Bakewell Area Office (A)	25.4.84
Worksop Area Office (A)	25.4.84
Chesser House, Edinburgh (DAFS)	2.5.84
Lasswade Laboratory (V)	2.5.84
Newcastle Divisional Office (L)	10.5.84
Agricultural Restoration Unit (Newcastle) (L)	10.5.84
Northern Regional Office (Leeds) (L, V)	11.5.84
Leeds Animal Health Centre (V)	11.5.84
South Western Regional Office (Bristol) (AS, L)	17.5.84
Taunton Divisional Office (L)	18.5.84
Guildford Divisional Office (A, V)	22.5.84
Winchester Animal Health Centre (V)	22.5.84
Winchester Area Office (A)	22.5.84
South Eastern Regional Office (Reading) (A)	23.5.84
Extension Development Unit (Reading) (A)	23.5.84
Agricultural Computing Unit (Reading) (A)	23.5.84
Norwich Divisional Office (L)	29.5.84
Eastern Regional Office (Cambridge) (AS, L)	30.5.84
Field Drainage Experimental Unit (Cambridge) (L)	30.5.84
Carmarthen VIC (V)	5.6.84
Carmarthen Divisional Office (A, L, V)	5.6.84
Wales - Park Avenue, Aberystwyth (L)	5.6.84
Trawsgoed EHF (A)	6.6.84
Newtown Area Office (A, L)	6.6.84
Worcester VIC (V)	13.6.84
Liscombe EHF (A)	14.6.84
Midlands and Western Region Sandland 84/Irrigation 84 Demonstration (A, AS, L)	26.6.84
Gleadthorpe EHF (A)	27.6.84
Boxworth EHF (A)	27.6.84
Brogdale EHS (The National Fruit Trials) (A)	29.6.84
Central Veterinary Laboratory (Weybridge) (V)	5.7.84
Harpenden Laboratory (AS)	6.7.84
Redesdale EHF (A)	11.7.84

High Mowthorpe EHF (A)	11.7.84
Bridgets EHF (A)	17.7.84
ADAS Unit, NAC, Stoneleigh (A, AS, L, V)	19.7.84
Slough Laboratory (AS)	1.8.84
Worplesdon Laboratory (AS)	1.8.84

- NOTES:
- 1) Meetings were held with HQ groups of all ADAS Services.
 - 2) Discussions were undertaken with some MAFF Under Secretaries and all Chief Regional Officers.
 - 3) Where possible meetings were held with Local Trade Union representatives during visits to Regions and Wales.
 - 4) During each visit to the Regions and Wales an evening meeting was held with the Regional Heads of Services.

CODE:

- A - Agriculture Service
- AS - Agricultural Science Service
- L - Land and Water Service
- V - Veterinary Service

ORGANISATIONS AND INDIVIDUALS CONTRIBUTING WRITTEN EVIDENCE

- Agricultural and Allied Workers National Trade Group
 Agricultural and Food Research Council
 Agricultural Training Board
- * Mr D B Allison
 Association of County Councils
 Association of District Councils
 Bacon and Meat Manufacturers Association
 Mr M Banwell
 Mr R Bawcki
 Beechams Foods
 British Agrochemicals Association
 British Institute of Agricultural Consultants
 British Leather Federation
 British Veterinary Association
 Mr W B Cartmell
 Chief Regional Officers, MAFF
- * Mr A J Collard
 Committee of Vice-Chancellors and Principals of the Universities
 of the UK
 Council for the Protection of Rural England
 Council of the Scottish Agricultural Colleges
 Country Landowners Association
 Countryside Commission
 Crown Chemical Company
 Department of Agriculture for Scotland
 Dr F H Dodd
 Ecology Party
 Eggs Authority
 Sir Charles Evans
 Farm and Food Society
 Farmers Union of Wales
 Farming and Wildlife Advisory Group
- * Mr J B Finney
 Food From Britain
 Food Manufacturers Association
 Dr P Froggatt
- * Mr R M Gamble
 Mr A Green

- * Mr C Groom
 - Mr P S Hamer
 - Home Grown Cereals Authority
 - Mr H V Hughes
 - Mr B E Humphrey
 - Imperial Chemical Industries PLC
 - Institute of Biology
 - Institute of Professional Civil Servants
 - Institution of Water Engineers and Scientists
- * Mr J E E Jenkins
 - Dr H Kay
 - Landowners Group
 - Laurence Gould Consultants
 - Mr J D Ludlam
 - Mr E Maddison
 - Prof L Martin
 - Meat and Livestock Commission
- * Mr R R Menneer
 - Milk Marketing Board
- * Mr I B Munro
 - Mushroom Growers Association
 - National Farmers Union
 - National Farmers Union Cornwall County Branch
 - National Farmers Union Cumbria County Branch
 - National Farmers Union East Sussex County Branch
 - National Farmers Union Hampshire County Branch
 - National Farmers Union Watercress Branch
 - National Federation of Meat Traders
 - National Institute of Agricultural Botany
 - Natural Environment Research Council
 - Nature Conservancy Council
- * Mr V C Nielson
 - Prof J Nix
- * Mr R Heddyn Owen
 - Dr E S Page
 - Prof E M Patterson
 - Phosyn Chemicals Ltd
- * Mr B H Powell
 - Prof R J Roberts
 - Royal Agricultural Society of England
 - Royal College of Veterinary Surgeons
 - Royal Institution of Chartered Surveyors

Mr J Surgey
Mrs R M Tittensor
United Kingdom Agricultural Supply Trade Association Ltd
Dr B C L Weedon
* Mr J M Weekes
Welsh Office

British Missions Abroad:

Mr J J Beale	Dublin
Mr I L Blackley	The Hague/Brussels
Miss S E Brown	Washington
Mr P S Collicott	Canberra
Mr R Crawshaw	Wellington
Mr D B A Evans	Rome
Mr S Sadowski	Copenhagen
Mr J C Suich	Bonn
Miss V K Timms	Paris
Mr D Thomadakis	Athens

* Denotes Members of ADAS

MEETINGS HELD WITH OUTSIDE ORGANISATIONS AND INDIVIDUALS

Regional Panel - Eastern Region	28.2.84
Council of Civil Service Unions	18.4.84/22.6.84
Principals of Scottish Agricultural Colleges	2.5.84
Department of Agriculture for Scotland	3.5.84
Welsh Office Agriculture Department	30.4.84/4.6.84/16.7.84
Agriculture and Food Research Council Directors	7.6.84
Council for Development in Agriculture - ACOT Republic of Ireland	11.6.84
Mr O Colborn	12.6.84
Cotswold Cereal Group	13.6.84
Nature Conservancy Council	19.6.84
Mushroom Growers Association	25.6.84
British Institute of Agricultural Consultants	25.6.84
Nottinghamshire NFU	26.6.84
Professor R J Harrison, Chairman of Farm Animal Welfare Council	4.7.84
English Tourist Board	16.7.84
Regional Panel - South Eastern Region	17.7.84
Mr G Paterson	17.7.84
Country Landowners Association	18.7.84
Royal Agricultural Society of England	19.7.84
UKF Fertilisers	18.7.84
Agricultural Training Board	20.7.84
National Farmers Union	20.7.84
British Council	25.7.84
Natural Environment Research Council	26.7.84
Association of District Councils	27.7.84
The Society for the Responsible Use of Resources in Agriculture and on the Land	28.7.84
Dr K Dexter	28.7.84
Agricultural and Allied Workers National Trade Group	30.7.84
Department of Agriculture Northern Ireland	31.7.84
Meat and Livestock Commission	23.8.84
Countryside Commission	10.9.84

CURRENT ORGANISATION AND FUNCTIONS OF ADAS

Figure 1 is a diagram of the structure of ADAS and its component services.

AGRICULTURE SERVICE

1. Qualified agriculturists and husbandry specialists, technical support staff, Horticultural Marketing Inspectors and industrial staff make up the Agricultural Service. The largest single group is that of the Agricultural Advisory Officers who are in regular contact with farmers and provide the main front-line input to advisory and development work. Members of this group are also stationed at the twelve Experimental Husbandry Farms (EHFs) and eight Experimental Husbandry Stations (EHSs).
2. Regional and National specialists in various disciplines provide back-up support to local advisers and, on occasions, advice to farmers direct. They also participate fully in investigational and development work and interact with staff at EHF's and EHSs. Extensive collaboration is maintained by these specialists with other organisations involved in agriculture who carry out work of importance to the industry.
3. The provision of socio-economic advice is of increasing importance and this is carried out by special interest advisers within divisions, supported by regional specialists. Horticultural Marketing Inspectors are responsible for enforcement of the EEC Quality Standards for fruit and vegetables, some work for the Intervention Board for Agricultural Produce (IBAP) and the collection of prices for Agricultural Market Reports.
4. Small groups of officers are stationed in the Extension Development Unit, Reading where they are responsible for studying the impact of advisory techniques and developing future strategies and at the National Agriculture Centre, Stoneleigh

where they participate fully in all activities of the NAC.

VETERINARY SERVICE

5. The State Veterinary Service (SVS) developed from the original Department set up to control rinderpest in 1865, and was incorporated into ADAS when it was formed in 1971.

6. The major functions of the Veterinary Service include the control and eradication of notifiable diseases; the operation of national disease control programmes; the investigation of new animal diseases and of zoonoses (ie those diseases of animals transmissible to man); control of the import and export of animals and animal products, meat hygiene and consumer protection work; the welfare of animals on the farm, in transit, in markets and in slaughterhouses; and the licensing of medicines and vaccines. Another important role is international disease surveillance, in order to guard against the introduction of exotic animal diseases such as foot-and-mouth disease, swine fever and rabies, from other countries. The SVS also co-operates with private veterinary surgeons, who are responsible for treatment of animals on the farm, in the investigation of disease and production problems in livestock. Four and a half thousand private practitioners are appointed as part-time Local Veterinary Inspectors to perform statutory animal disease control duties on behalf of, and under the direction of, the SVS.

7. The field staff, who are responsible for the implementation of statutory controls in England, Wales and Scotland, are supported in England and Wales by 23 Veterinary Investigation Centres. These centres provide a laboratory diagnostic service to the veterinary practitioners and through them an investigation, advisory and consultancy service on animal diseases to the livestock industry. There are separate laboratory arrangements in Scotland.

8. The Central Veterinary Laboratory at Weybridge, with its 11 departments, and the smaller laboratory at Lasswade, provide specialist diagnostic facilities and carry out a wide range of service work and Research and Development. The Cattle Breeding Centre at Shinfield provides a commercial artificial insemination service for cattle and pigs and carries out Research and Development on these species.

AGRICULTURAL SCIENCE SERVICE

9. The Service consists of staff based at Regional Laboratories and in a number of Central Laboratories. It is organised into Chemistry and Biology Divisions within which are further sub-divisions into Disciplines.

10. The Chemistry Division comprises Soil Science, Nutrition Chemistry and Analytical Chemistry which operate regionally and the Pest Control Chemistry and Pesticide Registration Departments at the Central Laboratories. In addition there are four small out-stationed HQ Units, dealing with Aerial Photography, Farm Waste, Feed Evaluation and Pesticide Residues. In the Regions the major function is support of Agriculture Service advisers with follow-up advice and promotion and R and D in support of such work. The analysis of samples for IBAP is also of major importance.

11. The Biology Division is represented at Harpenden, Slough, Tolworth and Worplesdon Central Laboratories. Within these laboratories the Division includes the Storage Pests and the Mammals and Birds Departments. The work of both departments is aimed at preventing losses to the agricultural industry caused by invertebrate pests in storage and mammals and birds, respectively.

12. There are two regionally based Disciplines - Wildlife and Storage Biology and Microbiology. The former provides advice on agricultural problems caused by vertebrate pests in crops and storage, and insect and mite pests of stored food and

animal houses, together with advice on environmental and wildlife implications of the use of agricultural chemicals. It also works with Land and Water Service on wildlife conservation and with Veterinary Service on badger control related to bovine tuberculosis. The latter is concerned with dairy hygiene and microbiological problems in processing, preservation and storage of farm and horticultural products and animal feedingstuffs, as well as with treatment and disposal of farm effluent.

13. Entomology and Plant Pathology Disciplines work at Central Laboratories and in the Regions where they are mainly concerned with advice and promotion for invertebrate pests and plant diseases together with any necessary R and D.

14. Finally, the Plant Health and Seeds Inspectorate act in a regulatory and inspectorial capacity under plant health legislation.

LAND AND WATER SERVICE

15. This is a service with a wide range of professional disciplines including surveyors, architects, engineers and geographers. It is organised into an HQ, Regional and Divisional structure together with a number of specialist units - Farm Buildings Group, Field Drainage Experimental Unit, River and Coastal Engineers, Resource Planning Group, Ergonomics and Work Study Unit and Cartographic Section. These provide a scientific backing to LAWS and the industry as a whole.

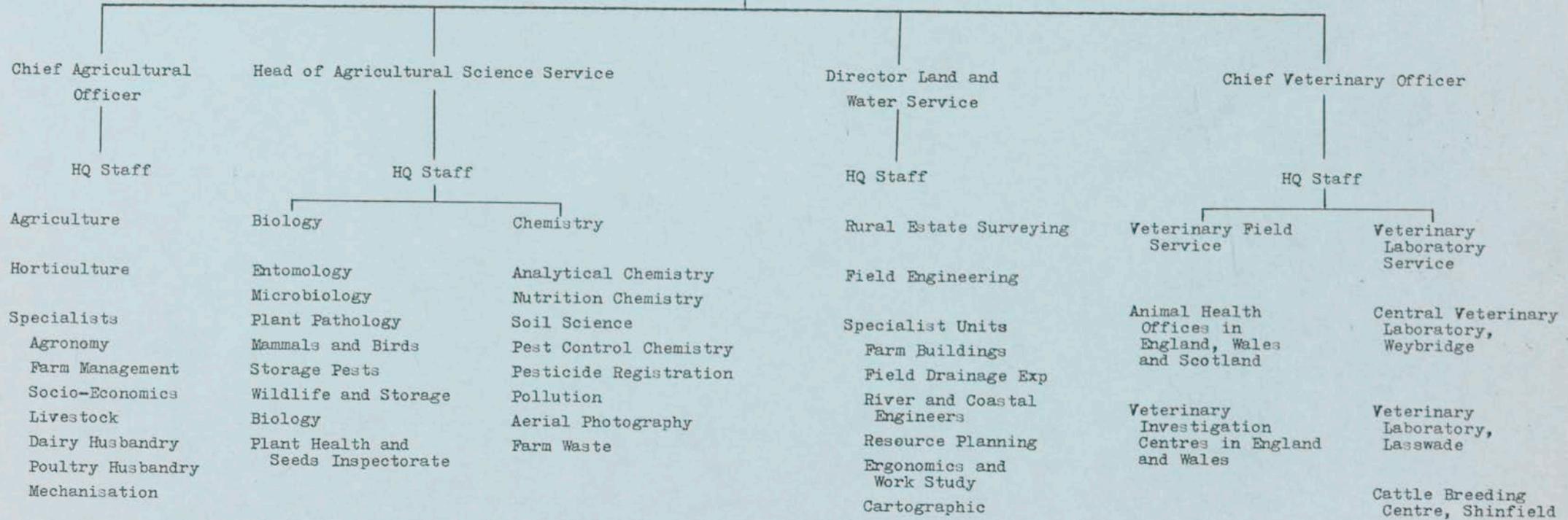
16. The Service is primarily concerned with capital investment in the infra-structure of agriculture and the efficient use of land as a resource. It advises MAFF, other Government Departments, Local Authorities and the agricultural industry generally, including contractors and consultants. The work ranges from major land use issues, such as new airports, major capital investment in flood protection, such as the Thames Barrier, to individual farm

investments. It is also the lead service on conservation matters, seeking to co-ordinate the inputs of specialists both within LAWS and elsewhere in ADAS and to provide outside bodies with a specific contact point.

17. The responsibility for all programmes of capital works on EHF's, EHSs and other Ministry property rests with Land and Water Service.

DIRECTOR GENERAL ADAS

Administration Support to:
 Central Labs
 Experimental Husbandry Centres
 HQs
 Liaison with MAFF Divisions
 Cross-Service Liaison



INFORMATION TECHNOLOGY IN ADAS

1. Introduction - Recent developments in information technology (IT) give the possibility of rendering ADAS more efficient and more effective both in its service to the agricultural industry at large and in the conduct of its internal affairs. About 5,000 farming businesses already have IT facilities and within 10 years the number is expected to reach 50,000. The agricultural supply and service industries are also investing in such equipment. ADAS has the opportunity both to interact and cooperate with this latter group to provide a range of valuable and efficient services to farmers, growers and others in the industry which will supplement or replace those provided "manually". It also has the opportunity of giving a more efficient service to MAFF.

2. Background - There is a long history of automatic data processing in the Ministry but as the range of available computer types has extended the different kinds of opportunity for employing them have been recognised. MAFF like most other organisations has had to keep under continual review its whole strategy for computing and information technology. Current thinking recognises a need for widely spread and individually targetted microcomputers; minicomputers at strategically sited centres distributed around the country, and a central bureau using both mainframe and minicomputers. Current strategy is for the whole to be connected in a network so as to allow direct access from many sites to the most appropriate machine for a particular job, and to allow for the extensive traffic of information between the various parts of the Ministry. This general strategy is being progressively implemented by a careful investigation of each type of user requirement and the design and installation of the facilities required to meet them. ADAS has been involved in all of this and has thought a great deal about the potential impact of information technology on its three principal

functions (statutory, advisory, R & D). It has successfully pioneered developments in several areas but it is now timely for a major new effort to be made.

3. Opportunities - ADAS is quintessentially an information trading organisation. It generates, collects, digests and passes on huge volumes of information. In certain of its functions the customer is the farmer, or a member of one of the support professions/industries. In others it is collecting information for statutory or regulatory purposes and the "customer" is a policy or executive arm of MAFF. Both types of customer require reliable data that have been carefully vetted, collated and stored in a conveniently accessible form. The customers also require to manipulate the data or to have it manipulated and interpreted for them.

4. Whilst the satisfaction of ADAS' customer requirements will continue to require human intervention at various stages, there will be an increasing fraction that can be met by providing for the customer to have direct access either to a computer database or to an integrated package which comprises both data and a guide to enable the customer to answer his own questions or to solve his own problems. With an interactive computer programme he will feed in data relating to his own circumstances, the computer will extract relevant pieces of information from the database, perform any necessary calculations and then offer up solutions. To those unfamiliar with computers this may all sound fanciful or futuristic; to the cognoscenti it is a present reality albeit in limited situations.

5. What is required to make such facilities generally available to all those in the agricultural industry who could make good use of them is for a major effort to be devoted to the compilation of the databases and the accompanying packages of software. This is not a task for ADAS alone. Other research and development agencies like AFRC will have an important part to play especially in the provision of new data. From a

different standpoint, there are commercial companies already involved and planning to expand the provision of hardware and other services. However, there is a distinct and separate role for ADAS and the following paragraphs spell out what that role is. There is also a continuing possibility for cooperation between private and public sectors, a possibility which ADAS has exploited in the past and should continue to exploit.

6. Integrated commodity packages and support services - ADAS generates and collects a great deal of detailed information from its laboratory and field work. This includes data on soils, fertilizers, spray chemicals, crops, livestock, buildings, machinery, pests and diseases, veterinary medicines, and so on. Most of this is the result of objective study and its unbiased nature makes it extremely valuable. However, what makes the ADAS advisory service of even greater value is the fact that it can also interpret and use the data in an unbiased fashion. To provide a full and necessary service via a computer requires not simply the assembly of the data but the construction of software packages to enable the customer to arrive at his own solutions to problems. In principle this presents no difficulty but it adds very significantly to the effort required to provide such a service.

7. A rough estimate has been made of the effort needed. The whole farming scene has been examined on a commodity/primary enterprise basis and the opportunity for generating some 130 desirable packages identified. These comprise Arable Crops (30), Horticulture (50), Livestock (20), Mechanisation (15), Farm Business/Socio Economics (15). To complete the construction of such a set would consume of the order of 350 man years of effort. Furthermore, to meet the anticipated market requirements it would be necessary to complete the work over a period of no more than 5 years. However, it would be fairly straightforward to assign different priority ratings based on anticipated demand so that the most important items could be created within the first one to two years.

8. There will be a growing commitment to update and maintain these integrated commodity packages and support services. During the initial five year period the staff requirement will peak because of the overlapping of the creation and maintenance work. However, the ultimate maintenance requirement is reckoned to be for about 80 persons and so there will need to be a permanent re-deployment of this number of staff. The main burden of this work will fall to multidisciplinary teams of existing staff drawn from the specialist disciplines such as agronomy, dairy husbandry, nutrition chemistry, etc. These people will need to dedicate themselves full-time to this work and consequently it will be necessary to withdraw them from their present duties. However difficult this proves to be in terms of the curtailment of present services, the creation of the database/software packages must be accorded a high priority at this time. Fortunately the development during recent years of special interest groups among the general agricultural/horticultural advisory officers has provided a resource which is available to plug the gap which will be created by the withdrawal of the discipline and commodity specialists.

9. Included in the estimates for setting up and maintaining the databases are 10 computer specialists to guide the construction and to develop the software systems. These posts will be found from staff savings elsewhere in ADAS.

10. There will be a requirement for an extra capital expenditure on computer and peripheral equipment over and above that which is already planned. It will not be possible to give a firm estimate of the cost of this until the study referred to in paragraph 14 has been carried out but it is anticipated that it will be of the order of £7.5m.

11. Customer access - Whilst the computer network and its associated databases and integrated software packages will be used by ADAS advisers to enable them the more effectively and efficiently to discharge their advisory and other duties, it is envisaged that farmers, agricultural suppliers, contractors and trade associations, professional practices and specialist consultants will increasingly want to gain direct access to the system from their own offices. There are several ways in which this access could be made available, for example via a viewdata terminal or a microcomputer, and they make possible an extremely convenient and simple way of invoicing the user for the service he obtains. Furthermore given that the system is designed to handle a large number of customers there is the possibility of each obtaining a convenient and valuable service at a modest cost, yet the total volume of revenue earning business could soon climb to £1m per annum and subsequently become self-financing.

12. Marketing of information - There is a growing realisation in our society that information no less than tangible commodities like land, labour and capital is a valuable, tradeable resource. ADAS should grasp the opportunity which this awakening realisation offers. It should investigate carefully what the customer wants by way of information and seek to provide and charge for it. This is a philosophy that should apply to the whole of ADAS advisory work but the IT approach offers the special advantages of giving a customer immediate access to what he wants and of enabling him to choose exactly the information which he requires and is prepared to pay for.

13. Of course, several organisations in the private sector have already recognised the possibility of trading information to the agricultural industry. ADAS need not be in direct competition with them for there is considerable scope for joint ventures. The current involvement with Prestel is a case in point.

14. Further study - The outline of opportunities given above is the result of a preliminary study carried out during the course of my overall review of ADAS. Before embarking on the course of action which is recommended it will be necessary to conduct a detailed data flow analysis within the Service to provide reliable criteria for planning and investment purposes. Terms of reference for this analysis and study are being drawn up.

PRIME MINISTER

MISC 106

Thank you - I wonder if we have not missed some possible economies
mt

MISC 106 begins its work next week. You might like to look at some of the papers. The Chief Secretary's minute, MISC 106(84)1 indicates that savings of

2063

3336

5202

are needed. This means that the Chief Secretary has to secure about 70 per cent of the sums still in dispute if he is to get back to base line.

A glance at the other papers will indicate how difficult are some of the options under consideration:-

i) Social Security.

Treasury is seeking cuts in housing benefit and widows' benefit. They also propose either a delay in the uprating or no uprating for unpledged benefits.

ii) Defence.

Chief Secretary is seeking cuts of £1150m in 1987-88.

iii) Energy.

Chief Secretary is proposing increases in real gas prices of 4 per cent a year and a rise in the rate of return for the electricity industry from the present 1½ per cent to 4½ per cent.

iv) Agriculture.

Treasury are seeking to cut grants to 10 per cent, to halve agricultural research and to cover all

SECRET

Note: Spide to Richard
Broadbent who will
get CVT to reply to
Mr Jopling, asking
Summary and conclusions of
report to be circulated to
MISC 106

MR TURNBULL

10 October 1984

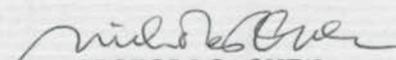
MISC 106: AGRICULTURE AND ADAS

12
AT
10/10

An item of MAFF expenditure which could escape the attention of MISC 106 is ADAS. ADAS has been the subject of an internal MAFF review by Professor Bell. Professor Bell's remit invites him to consider, inter alia, extending charging for ADAS services. I have not seen his report but I understand that he concludes by inviting agricultural Ministers to consider this option seriously.

It would be a pity if the report were not considered by MISC 106. We may be talking about £30 million in 1986-87 and 1987-88. The report has been circulated to the Chief Secretary, not to the Prime Minister and other colleagues.

Might I suggest that the Prime Minister asks to see the report so that MISC 106 members can see it before Tuesday, when agriculture is considered? The note could be hung on the self-congratulatory note which Mr Jopling's office sent to David Barclay on 27 September 1984.


NICHOLAS OWEN

SECRET

188/9

1. NO

NO

2. *for aquatics*



Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

Dobbe pl. Abtām.

N.O

From the Ministers Private Office

David Barclay Esq
Prime Minister's Office
10 Downing Street
London SW1

*Requested
3/10/84*

*received
3/10*

27 September 1984

Dear David

ACARD REPORT: NEW OPPORTUNITIES IN MANUFACTURING

With your letter of 6 August you drew my Minister's attention to this ACARD report and were also good enough to enclose a draft of the Government's response.

My Minister has an interest in this Report and the Government's response, not least because of the major importance he attaches to the application of new and advanced technology to the food manufacturing industry. In our recent response to the ACARD Report on The Food Industry and Technology we spelt out the action the Government is taking to encourage greater application of technology in this field. My Minister is content that the general tenor of the response to the present Report is in harmony with the line taken there.

Mr Jopling was particularly interested to see the reference in the Report to the effectiveness and success of the ADAS consultancy and advisory service and is sure that the Prime Minister will be interested too. The productivity of agriculture has been brought about both by an awareness in the industry of the importance of new technology and by the efforts of a highly qualified ADAS advisory service to ensure a speedy transfer of the technology from the research bench to everyday agricultural practice. The Report says "The remarkable achievements in agriculture demonstrate the value of the agricultural research and product development, the effective arrangements for technology transfer and the trained workforce." My Minister feels that he could not have put it better himself!

In considering any comparisons between agriculture and manufacturing industry, the very different structures of the two sectors are absolutely fundamental. The ACARD Report Table 5.1 shows clearly that agriculture comprises a large number (over a quarter of a million) of

/small enterprises,

small enterprises, employing on average 2.3 people each. No individual enterprise is able to carry out its own R and D, nor can it be expected to stay in touch with research developments in a field in which technology changes so rapidly. It is essential that the results of the R and D for agriculture are quickly transferred to all farmers and growers to ensure that we obtain the full benefits.

In paragraph 5.5 the ACARD Report makes the point that the importance of manufacturing industry to the UK warrants it having, inter alia, arrangements for technology transfer as effective as those for agriculture. If the productive efficiency of British manufacturing could be moved towards that achieved by the agricultural industry we should indeed have achieved much that the Government is aiming for.

*Yours ever
C I Llewelyn*

C I LLEWELYN
Private Secretary



Treasury Chambers, Parliament Street, SW1P 3AG

CONFIDENTIAL

Ivor Llewelyn, Esq.,
Private Secretary to the
Minister of Agriculture, Fisheries and Food,
Whitehall Place,
LONDON, SW1A 2HH

10th October, 1984.

Dear Ivor

REPORT OF A STUDY OF ADAS

The Chief Secretary was grateful for your Minister's letter of 9th October enclosing a copy of Professor Bell's report, to which he will be replying in full shortly. In view of the relevance of the report to forthcoming discussions in MISC 106 he feels it would be helpful to circulate immediately the concluding section of the Report (paragraphs 64-80) to the members of MISC 106. Perhaps you could let me know if there would be any problem in circulating something before the weekend?

will request if required

2. I am copying this letter to Janet Lewis-Jones in the Lord President's Office and to Andrew Turnbull at No.10.

Yours sincerely
Richard Broadbent

RICHARD BROADBENT
Private Secretary

11 OCT 1984



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Prime Minister
Not resolved except for
ECGD which is being
pursued bilaterally.

mt 9/10

JU355

PRIME MINISTER

I was grateful for the discussions which you initiated last week on my Department's PES position. I am writing to set out the basis on which I believe that Peter Rees and I are agreed that we should now proceed.

2 We have now agreed the following baseline:

<u>1985/86</u>	<u>1986/87</u>	<u>1987/88</u>
£millions	£millions	£millions
✓ 884.5	809.6	734.2

This baseline excludes regional expenditure and any local authority - relevant current expenditure; and will need to be adjusted to take account of the revised wage and salary assumption for PES agreed by the Cabinet and the detailed manpower targets when they are agreed with the Chief Secretary (I have agreed in general to a 3% manpower cut by 1 April 1988 subject to consideration of phasing and the need to bid for new staff for the takeover of the Radio Investigation Service, for the Companies Registration Office, and for the new scheme of regional incentives). On this basis, I understand that my programme will be regarded as "agreed" for the purposes of the operations of MISC 106. I accept that, as with all such agreed programmes, the Chancellor and Chief Secretary reserve the right

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to make further proposals should MISC 106 fail to identify the savings we need to keep within the agreed totals.

3 Peter Rees also has further points which he wishes to put to me in respect of the ECGD programme in 1986-7 or 1987-8. He and I will pursue this bilaterally, outside the operations of MISC 106.

4 I am copying this minute to Nigel Lawson and to Peter Rees.

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NT

9 October 1984

DEPARTMENT OF TRADE & INDUSTRY

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Treasury Chambers, Parliament Street, SW1P 3AG

G K Sandiford Esq
Private Secretary to the
Secretary of State for Northern Ireland
Northern Ireland Office
Whitehall
London SW1A 2AZ

5 October 1984

Dear Private Secretary,

I enclose a note of the Chief Secretary's meeting with your Secretary of State on 1 October. I should be grateful if you could ensure that this is circulated on a strict need to know basis.

2 As the minutes record the Chief Secretary and your Secretary of State agreed at their bilateral discussion that the next step in relation to public expenditure should be further work on needs assessment in Northern Ireland with the aim of providing the evidence for a comprehensive discussion of the overall position in next year's Survey. In parallel with those discussions Neil Ward wrote (his letter to 1 October) to Andrew Turnbull about separate but not unrelated matters of the level of financial support for Northern Ireland.

3 I am copying this letter to Andrew Turnbull.

Yours sincerely,
Paul Teffer
R J BROADBENT

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9 OCT 1984



COMMUNICATIONS

DEPARTMENT OF TRADE & INDUSTRY

ow

NB/M AT 8/10

010/109

CONFIDENTIAL



Treasury Chambers, Parliament Street, SW1P 3AG

G K Sandiford Esq
Private Secretary to the
Secretary of State for Northern Ireland
Northern Ireland Office
Whitehall
London SW1A 2AZ

5 October 1984

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3 I am copying this letter to Andrew Turnbull.

Yours sincerely,
Paul Teffer
R J BROADBENT

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CONFIDENTIAL

NOTE OF THE CHIEF SECRETARY'S MEETING WITH THE SECRETARY OF STATE FOR NORTHERN IRELAND AND THE MINISTER OF STATE ON OCTOBER 1 1984

Those present:

Chief Secretary
Mr A N Ridley
Mr G W Watson
Mr P R C Gray
Mr W J E Norton
Miss C Evans
Mr R Broadbent

Secretary of State
Minister of State
Dr W H Quigley
Mr S G Norris
Mr I M Burns
Mr P J Small

MANPOWER TARGETS

The Chief Secretary welcomed the Secretary of State. He suggested that manpower targets be taken first. The Secretary of State said that he would be coming forward shortly with proposals to increase prison staffing and it was agreed therefore that these grades should be excluded from the discussion. The Chief Secretary accepted his offer of a reduction of 10 in Home Civil Service posts in the Northern Ireland Office to be achieved by measures to increase efficiency including the implementation of staff inspection reports.

2. Turning to Northern Ireland Civil Service posts in the NIO the Chief Secretary accepted the reduction of 30 offered, but noted that the NICS group had been exempt from the central scrutiny and reductions to which other UK departments had been subjected in the period 1979-1983. Accordingly he thought that a further reduction of some 65 posts would be reasonable.

In response it was pointed out that although these posts had not formed part of published manpower totals they had been subject to scrutiny by Northern Ireland Ministers and as a result manning was very tight. The Treasury had already registered its interest in NICS staff inspections which formed part of the scrutiny process. Following a discussion agreement was reached on a reduction of 50.

LOCAL AUTHORITY UNALLOCATED MARGIN

3. The Secretary of State said that he felt strongly that the principle of comparability formed an indispensable tool of the Government of Northern Ireland. Changes in public expenditure were monitored closely by the Northern Ireland Assembly but in the past the unallocated margin had appeared to be a minor item which might go unnoticed in the province. However, now that this had become a major and identifiable figure in the PEWP it was impossible to defend treating Northern Ireland differently from Scotland.

4. The Chief Secretary said that the principle was the same as in previous years. The unallocated margin was necessary because of the government's limited control of expenditure by local authorities in GB. Since this expenditure was under central Government control in Northern Ireland the need for unallocated provision did not arise.

5. The Secretary of State said that although Northern Ireland did not have the same local government structure the pressures on spending eg on major items such as teachers' and firemen's salaries were the same as in GB. Without receiving a share of unallocated provision Northern Ireland Departments had to meet these pressures by making cuts in other programmes. This meant that Northern Ireland was being penalised for the limited success in controlling local government expenditure in GB.

6. The Chief Secretary asked for clarification of the figure of £6m in respect of unallocated provision in 1986-7. It

was explained that this was ^{derived from} the amount included in the 1984 White Paper. The figure which would be published in next year's PEWP had not yet been decided - the figure of £6m was not a firm bid but simply an indication of the effect on that year based on last year's figures.

NORTHERN IRELAND BLOCK

7. The Secretary of State reiterated the importance of the principle of comparability which enabled public expenditure totals to be settled largely without controversy and to be defended on the grounds that people in Northern Ireland were getting broadly the same treatment as in GB. While he could not object to the principle of a needs assessment study he was concerned at the practicalities of implementing reductions if over provision was identified. There was a public expectation that public expenditure in Northern Ireland would increase broadly in line with the total in GB and deviations from this trend would be very difficult to explain. As far as the current Survey was concerned he was not prepared to accept a reduction on the basis of an assessment which in his view underestimated the needs of Northern Ireland. If it were proposed to seek a reduction "on account" pending completion of the study he could equally well press for an increase on the same basis.

8. The Chief Secretary said that there was a need to distinguish between the principle of having a study, and the practicalities of responding to its findings. The question of relative standards of provision amongst the territories would not go away and there was considerable merit in examining the evidence objectively without the pressures which had arisen during devolution. The objective was to move towards broad parity between provision in England and the territories and he was convinced that the proposed further study would prove worthwhile. The Treasury had an open mind on the outcome - the results might show under or over provision - but it was important to establish the scale of discrepancy and identify areas of agreement and of dispute, as a basis for discussion

in next year's Survey. The further study should therefore have a deadline of June 1985. As to the proposed reduction of £50m the Treasury was confident that work done so far gave convincing evidence of over provision well in excess of this figure; but he would not press this if the Secretary of State would agree to withdraw his bid for a share of the unallocated margin. The Secretary of State agreed to this on the understanding that the unallocated margin question could be reconsidered in the context of the exercise to codify the rules on comparability of local government expenditure.

SUMMARY OF CONCLUSIONS

9. It was agreed that:

i. The NIO's 1.4.1988 manpower targets should be reduced, in respect of the HCS element by 10 to 176, and in respect of the NICS element (excluding the prison service) by 50 to 1260.

ii. Additional bids in respect of a Northern Ireland consequential of the unallocated margin should be dropped, on the understanding that the question would be further studied in the context of codification of the block ground-rules.

iii. Northern Ireland would participate in further work on needs assessment. The modalities to be discussed in the first place between officials.

H M TREASURY
3 October 1984

10 OCT 1984

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file

NOTE FOR THE RECORD

DTI: Expenditure Programme

Before the meeting between the Prime Minister, the Chancellor of the Exchequer and the Chief Secretary, the net addition to base line for DTI's main programme, excluding regional policy was:

+115 +110 +21

At the meeting Mr. Tebbit offered further savings of:

10 43 50

In her personal minute of 4 October the Prime Minister asked him to extend these savings to:

13.4 53 60

Mr. Tebbit's Private Office (Ruth Thompson) 'phoned today to say that he had accepted this proposal. The agreed position, in relation to base line is therefore:

+101.6 +57 -39

In addition Mr. Tebbit will pursue savings on ECGD bilaterally with the Chief Secretary.

I advised Ruth Thompson that the next stage was for Mr. Tebbit to reply to the Prime Minister signifying his agreement to her proposals, and copying his letter to the Chief Secretary. Meanwhile I have informed Sir Robert Armstrong's that the way is now clear for Mr. Tebbit to serve on MISC 106.

AT

Subject



cc/RTA
Lee DA 11
cc Master
JPS

10 DOWNING STREET

THE PRIME MINISTER

Personal Minute

No. M 11/84

SECRETARY OF STATE FOR TRADE AND INDUSTRY

Thank you for your minute of today. I took the opportunity of telling the Chancellor and Chief Secretary after Cabinet what you had said and this minute follows discussion with them.

We all recognise that the Chief Secretary's proposals have caused you acute difficulty and that you have gone as far as you feel you can towards meeting them. I know too that you understand the pressures on the Chancellor and the Chief Secretary and the importance of the public expenditure exercise for everything we are trying to do as a Government. We are all genuinely grateful for the constructive way you have looked at your programme and done your best to help.

In the light of that, and of the desire of all of us that we should have the benefit of your weight and influence on Willie Whitelaw's Committee, I have agreed with the Chancellor and the Chief Secretary that, if you will agree to make further reductions, over and above those you offered last night, of the £3.4 million which was suggested for year one and £10 million in each of years two and three, they will regard your main programme as being in the "agreed"

category for the purposes of the operations of the Lord President's Committee. Of course, the Chancellor and the Chief Secretary have to reserve the right to make further proposals, both in respect of your Departmental programmes and your nationalised industries, if the Lord President's Committee fails to identify the savings we need to keep within the agreed totals; but all the agreements so far reached with colleagues are subject to that reservation.

We concentrated on your main programme yesterday evening and the Chief Secretary tells me that he has a suggestion to make to you about your ECGD programme, which could save useful sums, particularly in 1986-87 and 1987-88. However, he has said that he would be happy to pursue this with you bilaterally, outside the operations of the Lord President's Committee.

I hope that it will be acceptable to you to proceed on this basis and that you will agree to serve on Willie Whitelaw's Committee.

Margaret Thatcher

4 October 1984



JU316A

PRIME MINISTER

You asked me to consider whether there is anything else I can offer to the Chief Secretary in the reduction of my Department's expenditure. I have looked again at whether I can go further.

2 Let me be clear about what the Chief Secretary is asking me to do. I have already made the strongest efforts to reduce expenditure, including a number of cuts which will be very unpopular. I have decided to end the small firm loan guarantee scheme; I have volunteered a moratorium on RDGs; I have given up the materials initiative; and I have made other painful cuts. In consequence I have provided from within my PES for launch aid for the A320 and the V2500, and for over a third of the extra costs of regional policy in the short-run, resulting solely from changes in economic assumptions. Given these steps already agreed, it is common ground that the ^{only} way I can make deeper cuts is by reducing still further the spend on support for industrial research and development. It is also common ground that my headroom in these areas, after allowing for existing commitments, is limited. In round terms, it is £193 million in 1986/87 and £285 million in 1987/88. I volunteered yesterday evening, in the hope that this would enable me to come to the agreement with the Chief Secretary, reductions of £43 million and £50 million. This

a RYA
Public expenditure file
Please classify SECRET

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SECRET



SECRET

represents 22 and 18 per cent of my total uncommitted spend in this category.

3 The Chief Secretary has remained firm that he is looking for reductions in these years of £147 million and £249 million. This would leave me with just £46 million and £40 million for each year. The change in direction of our policies would be striking and potentially very damaging. Between 1980/81 and this year, support for science and technology has grown from £170m to £369m.

The Chief Secretary would have it fall by 1987/88 to £165m. In practice it would mean I should have to wind up, almost at once, our support for industrial research and development. I could not take in new applications, and should simply have to end schemes which are widely welcomed by industrialists, and to whose expansion we are committed in the Manifesto. We should be abandoning our ability to exert further influence on industry's research and development. I could not pretend we were doing this because I believed it correct. It would have to be recognised that the decision was forced on us by lack of cash. This, on top of all the other decisions to cut I have accepted, would leave us defenceless against criticism. Yet that is what the Chief Secretary is demanding.

4 I find this all the more humiliating because, at the same time that I am being asked to abandon policy to which we have all - including yourself - properly drawn attention and from which we

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SECRET

have derived credit, I am also being refused the authority to manage my Department in one singular way I have made clear to you I regard as necessary. I have no doubt that this, and the addition to my Ministerial team of an eighth Minister at a time when I believe it should be reduced, will be contrasted with the policy I am being asked to accept of denying assistance for industrial research and development. I would not know how to defend such a sense of priorities.

NT

N T

4 October 1984

Department of Trade & Industry

Of course if settlement is a matter of £5-£10 million a year in years two and three and the £3.4 million in year one which we discussed last night, I would find some way to achieve it. However if I am to be treated like a salsami sausage by Peter — or indeed as an anvil on which MAFF expenditure might be hammered — then I have no choice but to resist.

N

Subject

cc Hager

SUMMARY OF A MEETING TO DISCUSS THE EXPENDITURE PROGRAMME
OF DEPARTMENT OF INDUSTRY: 10 DOWNING STREET: 3 OCTOBER
AT 1830 HOURS

Present: Prime Minister
 Chancellor of the Exchequer
 Secretary of State for Trade
 and Industry
 Chief Secretary
 Mr. Butler
 Mr. Turnbull

The Prime Minister said she wished the Secretary of State for Trade and Industry to serve on Lord Whitelaw's group to examine those departmental programmes where agreement had not been reached with the Treasury. This would only be possible if the Secretary of State had himself settled his programme with the Chief Secretary. E(A) had reached agreement that morning on expenditure under regional policy. What was at issue was DTI's main line programme excluding regional policy and excluding support for nationalised industries.

The Secretary of State for Trade and Industry said baseline for this expenditure was:

	£ million		
	1985-86	1986-87	1987-88
1)	783	752	773

In discussion with the Chief Secretary there had been agreement that reduced requirements, savings offered and additional bids accepted had left the programme as follows:

	Net addition to baseline		
2)	+115	+110	+21

In addition the Chief Secretary was seeking further changes which would modify the position as follows:

	Net changes from baseline		
3)	+ 82	- 37	-228
leaving 4)	Gap between SS/TI and CST (difference between lines 2 and 3)		
	33	147	249

The Secretary of State for Trade and Industry said he could not achieve cuts of the extent sought by the Treasury. This would leave his programme for support of industrial R & D with no more than was adequate to cover existing commitments. It would mean accepting no new applications after Christmas. This would represent a major change in the Government's support for new technology which would be inconsistent with the Manifesto and which, given the changes on regional policy, he could not defend.

The Chancellor argued that, with rising profits and lower Corporation Tax, industry should be prepared to take responsibility for financing more of its own research.

After some discussion the Secretary of State for Trade and Industry said he would undertake to find additional savings of:

5)	10	43	50
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which would produce a position in relation to baseline of

6)	+105	+67	-29
----	------	-----	-----

and new programme totals of:

7) 888 819 744

If E(A) decisions on regional policy were taken into account the Department's total programme moved from a baseline of

8) 1227 1184 1215 to

9) 1297 1284 1092

producing changes of

10) +70 +100 -123

The Chancellor suggested that if the Secretary of State for Trade and Industry could find further savings of £3.4 million in 1985-86, the excess of baseline would be £101.6 million or the amount attributable to the decision to offer launch aid to airbus and V2500. This would enable the Secretary of State for Trade and Industry to say that with the exception of this item which stemmed from a collective decision, he had absorbed all the Department's additional bids. The Secretary of State for Trade and Industry said he was prepared to accept this as part of a settlement on all three years.

The Chief Secretary said he could accept an increase over baseline in 1985-86 in view of the extent to which the programme was already committed. The Secretary of State for Trade and Industry's offer in years 2 and 3 would not be sufficient when taken with what could be achieved on other programmes for the planning total to be held. There would inevitably be a comparison with the savings made on industrial support with those offered on agricultural support.

The discussion then moved to the proposal, agreed with the Secretary of State for Employment that the Redundancy Fund rebate to employers should be reduced from 41 to 35 per cent. The Secretary of State for Trade and Industry said he was prepared to accept this proposal despite its adverse consequences particularly for smaller employers who were not topping up the statutory redundancy payments. He commented that the benefit would be short-lived as a lower payment would bring forward a time when the Fund was moved into surplus. At this point contributions would have to be cut.

Summing up the discussion, the Prime Minister said it had not been possible to agree figures for the DTI programme in years 2 and 3 and agreement on year 1 was provisional on a settlement of the rest. She invited the Secretary of State for Trade and Industry to consider whether he could offer further savings. Meanwhile those present should reflect on the position overnight.

The meeting ended at 2000 hours.

AT

3 October 1984

JKRAHE

Ref. A084/2622

PRIME MINISTER

Public Service Pay and Expenditure in 1985-86

C(84) 26

Flag A

BACKGROUND

The Government has distinguished in its public expenditure planning between increases in pay and increases in the prices of other inputs, and has set an explicit separate 'pay assumption' or 'pay factor'. It is necessary, whatever the system of public expenditure planning, to promulgate to Departments by about December pay assumptions for the preparation of the subsequent year's Supply Estimates. Under cash planning it has become the practice to decide and announce the assumption in September or October.

2. The pay assumptions in recent years have been as follows:

1982-83	4 per cent
1983-84	3½ per cent
1984-85	3 per cent

In all years, these 'pay factors' have been lower than the assumed increase in the price of other inputs and thus, on the face of things, have implied a reduction in the average real value of public service pay. In practice, public service pay settlements have typically been about one or two percentage points higher than the pay assumption. The extra cost has been found by such measures as administrative economies and staff reductions greater than previously planned.

3. The pay assumption usually applies to all central Government pay, including the Civil Service, the armed forces, and the National Health Service (though in some recent years the Defence cash limit has subsequently been adjusted to accommodate the recommendations of the Armed Forces Pay Review Body). It also applies to the universities, but not to local government or the nationalised industries. It is applied to planned manpower levels, so that savings from planned reductions in staff numbers are not available to finance higher pay settlements.

4. In his memorandum C(84) 26, the Chief Secretary, Treasury proposes to follow this broad pattern, apart from one significant departure. He proposes that there should be a separate pay assumption for 1985-86; that it should be set at 3 per cent; and that it should cover the public services other than local government. Since the published cash plans for 1985-86 were based on a general uplift factor, applying to pay and prices alike, of 4 per cent, a pay factor of 3 per cent will reduce the public expenditure baseline by some £200 million a year. The Chief Secretary in effect proposes to claw this back from departmental programmes and so ease the problem of containing the total of programmes within the published figures.

5. The departure from previous years is that the Chief Secretary proposes that there should be no formal announcement of the pay factor in advance of the Autumn Statement. He suggests that the pay factor should be regarded as a routine part of the public expenditure planning machinery, and no more deserving of a special announcement than any other part of the machinery.

MAIN ISSUES

6. The main issues before the Cabinet are as follows:

- (i) Should there be a separate pay assumption?
- (ii) What should it be?
- (iii) If it is less than 4 per cent, should the resulting reduction in the public expenditure baseline be treated as the Chief Secretary proposes?
- (iv) Should there be a special announcement regarding the pay factor?

A Separate Pay Assumption

7. In practice, questions (i) and (ii) seem likely to be discussed together. If there is to be a separate pay assumption, it is not easy to see an alternative to the proposed 3 per cent. Since 1979-80 most public service groups have received lower settlements and increases in earnings than the averages in both the public trading sector and the private sector. Although the

1984-85 pay round is at an early stage, there is little sign that settlements will be lower than the 5 $\frac{1}{4}$ to 5 $\frac{1}{2}$ per cent which is the likely outcome of the 1983-84 round. To set a lower pay assumption than last year's 3 per cent would be regarded as unrealistic (and perhaps provocative). It might well therefore be ineffective; if so, it would probably increase the threat to the public expenditure planning totals from excessive pay increases.

8. On the other hand, there is no doubt that a reduction in the level of pay settlements in the economy remains highly desirable. To set a higher pay factor than last year would give very much the wrong signal. It therefore seems likely that any Ministers who may consider 3 per cent unrealistic will argue against setting a separate pay assumption, at least at this stage, rather than argue for a different figure.

The Case Against a Separate Pay Assumption

9. The following main points may be made against a separate pay assumption:

(a) The logic of cash planning is that managers are given a budget which they are free to spend to the best advantage, in the light, among other things, of movements in relative prices. There is no more reason to distinguish between the prices of labour and of other inputs than to distinguish between any other categories of goods and services. The Chief Secretary himself appears to accept this to some extent, since paragraph 6 of C(84) 26 implies that his aim will be to ensure that departmental running costs do not rise by more than the general uplift factor of 4 per cent, and that he will not be seeking to distinguish between labour and other inputs.

(b) A separate pay assumption shows the employers' negotiating hand and may 'paint the Government into a corner' because the pressure in successive years is always to reduce it. The aim should be to dispense with it.

The Case For a Separate Pay Assumption

10. The following points may be made in favour of a separate assumption:

(a) There is a difference between labour and other inputs. For example, it is usually more difficult to vary staff numbers than the use of other factors of production.

(b) The existing expenditure plans in effect provide for pay increases of 4 per cent in 1985-86. This generates excess provision by comparison with the level of pay settlements which the Government would like to see.

Especially given the likely difficulties of the current Public Expenditure Survey, it would be wrong to forgo the savings that would result from a lower pay assumption.

Public Expenditure Treatment

11. I understand that some Ministers may be briefed to object to the Chief Secretary's proposal to reduce the baseline of those programmes which are affected by the choice of pay assumption. It must be conceded that the pay out-turn in the public services next year is likely to be greater than 3 per cent. This will mean a further squeeze on departmental programmes. If (as in the case of the NHS Review Body Groups this year) the excess is too large to be offset by efficiency savings, there is likely to be a call on the Contingency Reserve. The public expenditure saving of £200 million arising from the choice of a 3 per cent pay assumption is therefore arguably bogus. Even so, however, it is probably right to accept the Chief Secretary's proposal. The extra pressure to squeeze more efficiency from departmental programmes does no harm; and, although the Chief Secretary would not wish to concede at this stage that pay awards well in excess of the pay assumption may have to be financed in part from the Reserve, he will no doubt have the possibility in mind in determining the appropriate level for next year's Reserve.

Announcements

12. The arguments against making a separate announcement of the pay assumption are set out in paragraph 7 of C(84) 26. But there are two points that the Cabinet will wish to probe:

(a) It has been assumed in discussions in previous years that the Cabinet's decision on the pay assumption will leak, because so many people in Departments have to know about it for their work on the Public Expenditure Survey. Is there not a risk that, if there is a leak, the Government will still get the 'unhelpful headlines' which the Chief Secretary mentions, and even more misunderstanding and misrepresentation than in previous years?

(b) It is not clear that it will be possible - or even wise - to refuse to comment before the Autumn Statement, as the Chief Secretary appears to envisage. Apart from the likelihood of a leak, there is a meeting between senior Ministers and representatives of the local authority employers on 22 October to discuss the prospects for the current pay round. There is likely to be some discussion of the pay factor: indeed, the meeting would probably be less helpful to the Government than it could be if Ministers were unable to say that the public expenditure plans for 1985-86 will be based on a pay assumption of 3 per cent. It is one thing to refuse to single out the pay assumption for special mention; another to refuse even to discuss it publicly before the Autumn Statement.

HANDLING

13. You will wish to ask the Chief Secretary, Treasury to introduce his memorandum. The Chancellor of the Exchequer may wish to amplify it by outlining the economic background and prospects for the current pay round. The Home Secretary and the Secretaries of State for Education and Science, Defence, Scotland, Environment and Social Services will have views on the implications for pay negotiations in the services for which they are responsible.

The Secretary of State for Employment will wish to comment more generally. Others of your colleagues may also wish to speak, either from the stand-point of their departmental programme or more generally.

CONCLUSIONS

14. You will wish the Cabinet to reach conclusions on the following:

(i) Should there be a separate pay assumption of 3 per cent for 1985-86, applying to all public services other than the local authorities?

(ii) Should the public expenditure baseline for programmes affected by the decision be reduced accordingly?

(iii) Should the Government's decision, unlike previous years, not be the subject of a special announcement? And if there is to be no special announcement, should the Government positively refuse to make its intentions known before the Autumn Statement?

If there is to be an announcement, should it be made formally by the Treasury or informally by No. 10?

RTA

ROBERT ARMSTRONG

3 October 1984



Ref. A084/2641

PRIME MINISTER

Public Expenditure Survey 1984

(C(84) 29)

BACKGROUND

A This year's White Paper on the Government's Expenditure Plans (Cmnd. 9143) gave planning totals of £132.1 billion for 1985-86 and £136.7 billion for 1986-87; after agreed adjustments (mainly due to the reduction in this year's Budget on the National Insurance Surcharge) these produced baseline figures for the 1984 Public Expenditure Survey of £131.7 billion and £136.3 billion. The baseline figure for 1987-88 was £139.0 billion: this was derived from the 1986-87 baseline by uplifting all programmes, with the main exception of expenditure on the Falkland Islands, by 2½ per cent.

B 2. At the beginning of July the Chief Secretary, Treasury reported to the Cabinet, in his memorandum C(84) 18, that bids from Departments, net of reduced requirements, exceeded the baseline figures by £5.0 billion in 1985-86, £5.8 billion in 1986-87, and £8.4 billion in 1987-88. He proposed that the baseline figures for 1985-86 and 1986-87 should be maintained; and that the baseline for 1987-88 should be increased to £140.4 billion. This figure resulted from using an uplift factor of 3 per cent rather than 2½ per cent. The Chief Secretary also proposed that the reserve should be £3 billion in 1985-86, £4 billion in 1986-87 and £5 billion in 1987-88.

C 3. The Cabinet approved these proposals; invited the Chief Secretary to pursue bilateral discussions of expenditure programmes with the Ministers responsible; and invited him to report again when he had completed those discussions (CC(84) 25th Conclusions, Minute 5).

D 4. In his memorandum C(84) 29 the Chief Secretary reports on the current position. Although I understand that the detailed figures are constantly changing, the general picture is clear



E enough. Even on the assumption that the objective agreed by E(A) on 3 July (E(A) (84) 17th Meeting) of reducing nationalised industry External Financing Limits below the baseline by £250 million in 1985-86, £500 million in 1986-87, and £1 billion in 1987-88 is achieved - and the Chief Secretary says that he is a long way from this - agreed changes and outstanding bids from Departments amount to about £1.75 billion in 1985-86, £2.1 billion in 1986-87, and £3.4 billion in 1987-88. Few programmes have been agreed; and there are particularly large bids for Defence, the Foreign and Commonwealth Office, Export Credits, Housing, Health, and Social Security.

5. The Chief Secretary therefore proposes that a small Ministerial Group, on the lines of the Ministerial Group on Public Expenditure (MISC 99) last year, should be set up.

HANDLING AND CONCLUSIONS

6. There is no need for an extended discussion which would probably be unhelpful. You have already agreed that a Ministerial Group should be set up (Mr Turnbull's minute of 1 October recording its composition is attached for ease of reference), and those involved have already been approached informally. It would be preferable (and consistent with past practice) to avoid telling the Cabinet who are to be the members as this is your decision and not theirs.

7. I therefore suggest that you might invite the Chief Secretary, Treasury briefly to report whether there are any last-minute developments since this memorandum was written. You might announce your decision to set up a Ministerial Group under the chairmanship of the Lord President of the Council. It would be helpful for the work of the Group if you could:

- (a) remind your colleagues that the Cabinet has already agreed that the aim of this year's Public Expenditure Survey should be to hold to the baseline figures proposed by the Chief Secretary in July; and
- (b) ask all Ministers concerned to give the highest priority to the work of the Group and to instruct their Private Offices and Departments accordingly.

Attached to brief



F 8. There has already been extensive speculation in the media about the establishment of a 'Star Chamber'. You will no doubt wish to avoid any extended statement on what is a perfectly normal part of the annual Public Expenditure Survey. But there seems to be no objection to confirming, in response to enquiries, that a Ministerial Group has been set up to make recommendations to the Cabinet. This was done at a similar stage last year (CC(83) 30th Conclusions, Minute 4).

approved by ROBERT ARMSTRONG
and signed in his absence.

Lindsay Wilson

3 October 1984

CONFIDENTIAL



10 DOWNING STREET

CABINET OFFICE	
A	7407
1 OCT 1984	
FILING INSTRUCTION	
FILE No.

From the Private Secretary

cc - M. Gregson
H. Buckley

SIR ROBERT ARMSTRONG
CABINET OFFICE

Public Expenditure Survey 1984: Small Ministerial Group

The Prime Minister has seen your minute of 28 September reference A084/2599. She wishes the composition of the Group to be

Lord President of the Council (Chairman)
Home Secretary
Secretary of State for Scotland
Lord Privy Seal
Secretary of State for Trade and Industry
Chief Secretary, Treasury

She would like the Secretary of State for Trade and Industry to be a member but this would be conditional upon agreement being reached between him and the Chief Secretary on the outstanding differences on his Departmental programme. A meeting has been arranged between him, the Prime Minister, the Chancellor and the Chief Secretary for Wednesday afternoon in an effort to achieve this.

She is content for you to approach members of the Group informally before Thursday in order that an early start can be made on scheduling the work of the Group. This can include the Secretary of State for Trade and Industry who is aware that his membership of the Group is conditional upon resolution of the outstanding differences.

AT

Andrew Turnbull

1 October 1984

CONFIDENTIAL

Prime Minister

File

1

You should be aware of this before Cabinet. If you do not like it, we should warn the Chancellor before Cabinet

MR TURNBULL

2 October 1984

PUBLIC EXPENDITURE: DES

No - we did this last year. We cannot add further to FERB 2.10.

The Chief Secretary and Keith Joseph have this afternoon agreed to a level of DES spending that will be thoroughly satisfactory to the Treasury. We expect that news of this settlement will be brought to Thursday's Cabinet. The Prime Minister should, however, be warned that the package includes cuts in student grants. *is proposed is equivalent to an increase*

The proposal is to abolish the minimum award, to steepen the parental contribution scales and to make richer parents liable to pay a small amount towards fees. This will affect parents as follows:

Parental Income (£)*	Contribution on present policy (£)	New Proposals: Increase in Contribution (£)
8000	0	0
10000	291	0
12000	617	57
14000	950	124
16000	1283	241
18000	1617	407
20000	1680	725
22000	1680	725

Because of the way that the student grant is calculated, parents with two or three children will not lose twice or three times as much as those with one child; indeed, many of them will lose no more than single child families. And the DES propose to add a special relief to ensure that no family with more than one student loses too heavily, although the details of the scheme have yet to be worked out.

* 'Parental Income' = 'Residual Income' after allowance is made for various financial burdens.

The package will save £39 million in 1985/6, rising to £61 million in 1987/8.

No one can pretend that the proposals will delight the Government's supporters. But they probably constitute the only practicable means of achieving the reductions that the Chancellor desperately needs. Most of the expenditure nominally assigned to the DES is in fact already committed through the Rate Support Grant which Cabinet settled some time ago. This leaves the Treasury with little room for manoeuvre; and they have seen no way of meeting their targets without either making inroads into science or cutting the student grant. Given the delicate condition of science funding, Keith Joseph has opted for cuts in the grant level.

We reluctantly recommend that the Prime Minister should accept the Treasury/DES proposals.

Ol Letwin.

OLIVER LETWIN

45

Public Expenditure

100



SECRET



Prime Minister ④
There is some interesting material in Annexes C & D on experience in other countries.

AT 6
4/10

Treasury Chambers, Parliament Street, SW1P 3AG

A Turnbull Esq
10 Downing Street

2 October 1984

Dear Andrew

PUBLIC EXPENDITURE

As requested in your letter of 28 September to David Peretz, I attach a draft speaking note and briefing for the Prime Minister's use at Cabinet on 4 October.

On public expenditure in the current year, the Chief Secretary proposes to introduce the topic on the line of the speaking note at Annex A. Annex B provides a speaking note for the Prime Minister to bring this topic to a conclusion.

For the future years, the Chief Secretary will introduce his paper in full. Annex C provides a speaking note for the Prime Minister (or Treasury Minister's use as necessary) on experience in other countries. Annex D sets out the background in more detail.

The conclusion of this discussion would be an appropriate point for the Prime Minister to warn of the need to exercise care in responding to Party Conference motions. Annex E provides a speaking note. Annex F provides background notes on the motions to be debated at the Conference which have potentially serious public expenditure implications. The Chief Secretary believes that energy, defence and agriculture are the three debates where public expenditure objectives are most at risk. Experience last year in the field of energy prices for example underlines the need to minimise premature public speculation.

I am sending a copy of this letter to David Peretz in the Chancellor's Office.

Yours sincerely
Richard Broadbent

RICHARD BROADBENT

SECRET

PUBLIC EXPENDITURE 1984-85

Chief Secretary's introductory speaking note

The public expenditure situation is very serious - both this year and in the prospect for future years.

On this year, it has been clear for some months that there are many substantial claims on the Reserve. The main factors are the miners' strike and overspending by local authorities, both current and capital. But there are other demands, for example pay in the National Health Service and the effects of changes in interest rates. There is no doubt that the press and the City are aware that our plans are likely to be exceeded; but they have yet to realise the extent of the problem. [not for the minutes: The Treasury's latest assessment suggests that the planning total will be exceeded by over £1 billion.]

PUBLIC EXPENDITURE 1984-85

Prime Minister's speaking note

In 1983 we agreed an across-the-board package of cash-limit cuts when it became apparent early in the year that our plans were likely to be exceeded. This year we have had no cash limit cuts; and we have ruled out a moratorium on local authority capital expenditure. But we cannot allow expenditure to run away, unrestrained. I do not need to tell you of the damage to our whole strategy if we fail to control public expenditure.

I am therefore asking each spending Minister to do your utmost to restrain expenditure this year. In the first place this means ensuring that existing cash plans are not exceeded. Savings must be sought to offset extra demands on programmes. This must also apply - as it often has not in the past - for demand-led programmes, where there may be little discretion over meeting the extra demand. The presumption must always be of no net increase in programmes, and the rules for access to the public expenditure Reserve must be strictly interpreted and applied. Secondly, I would ask each Minister to review his programme with a view to generating further savings this year. I am not suggesting going back on commitments, or making cuts which would be excessively disruptive or store up trouble for future years. But I am asking that everything should be done to realise savings that can be identified. This will mean bringing forward efficiency schemes, pushing for greater and quicker asset and land disposals, looking for increases in charges, as well as postponing new expenditure measures or delaying projects.

I hope that if you all go back to your Departments and set in hand measures of this kind it may be possible to achieve savings that would bring the prospective outturn this year much closer to the expenditure planning total.

PUBLIC EXPENDITURE 1985/86 - 1987/88

Speaking note on experience in European countries for use if necessary

For future years the prospect is one of acute difficulty. But

we are far from alone in our difficulties with public expenditure. France, Germany, the Netherlands, Italy, Spain - indeed the United States itself - are all grappling with the difficulties of keeping public expenditure in check: and some of these countries - including a number with socialist governments - have not shrunk from measures which we are often told would be quite impossible here. The French, Dutch and Belgian governments have all reduced unemployment benefit. Pension increases were delayed in Germany last year and this. Family allowances in Italy for higher income earners are being progressively withdrawn. The Spanish government is trying to rationalise its social security system, with a view to reducing the Budget deficit.

BACKGROUND NOTE: AUSTERITY MEASURES IN OTHER COUNTRIESa) United States

1. The Administration remains committed to cutting discretionary domestic programmes. The Government-appointed Greenspan Commission reported in January 1983 on ways of closing the deficits projected in the social security funds. Largely following its recommendations, Congress, in May 1983, agreed to cuts in planned expenditure and increases in social security contributions, together worth around \$165 billion over 7 years. Cost of living adjustments to social security pensions were delayed for 6 months, benefits for those who retire early were reduced and benefits for those with relatively high incomes will be taxed.

2. There is also serious concern over the escalation of health costs. The Administration has made a number of proposals including lowering its contribution if States' spending on medicare exceeds target, and "capping" the fees of medical practitioners under the scheme. The 1984 Deficit Reduction Act will cut \$15 billion from entitlement programmes between FY 1984-87 with most of the savings concentrated in the medicare programme.

b) Japan

3. Concern has been expressed over the rise in the number of the elderly expected in the coming years. Partly as a result of these pressures the Government intends to reduce pensions. Unemployment benefit was cut from 1 August 1984 by shortening the entitlement period and excluding bonus earnings from the calculation.

4. Insured workers have to meet 10% of health costs from October 1984. In addition, health care insurance premiums are now levied on a substantially larger portion of taxable income. Another aim of the Government is to eliminate the budget's current account deficit by 1990.

c) Germany

5. The Government delayed some pension increases by 6 months in 1983 and 1984. Unemployment benefit for those without children was reduced by an average 2 percentage points of previous wages on 1 January 1984. No further reductions in social benefits are expected in 1985.

6. On the health side board and lodging charges for hospital patients were introduced from 1 January 1983 for the first 14 days of their stay. Drugs for common ailments such as colds and flu are no longer available under sickness insurance. Prescription charges were increased by one-third on 1 January 1983.

7. The 1985 Budget includes proposals to decrease industrial subsidies from 5.6% to 5.2% of 1985 Federal Government expenditure. The plan is apparently to decrease this progressively to 4% by 1988.

d) France

8. The social security fund has moved into surplus since 1983 after large deficits in 1981 and 1982, as a result of increased taxes and contributions and some economies in spending. The unemployment benefit scheme, which was running into deficit, was renegotiated by the Government, trade unions and employers in early 1984. The main features of the new scheme, which came into effect on 1 April, were a reduction of maximum level of benefit and shortened entitlement periods. A board and lodging charge (now Fr 21 per day) for hospital patients was also introduced from 1 April 1983.

9. The 1985 draft Budget presented to the Parliament on 12 September, pledged to reduce taxation by 1% of GDP. Nominal state expenditure is forecast to grow by 6% against nominal GDP growth of 7½%. The increase in general operating expenditure will be limited to 4½% in nominal terms while capital expenditure will rise by 6½%. No cuts in social welfare benefits were announced in the Budget. The Budget also revealed that the number of state employees is to be cut by 5450 through non-replacement and the rise in subsidies to the public sector is to be restricted to 3% in nominal terms.

10. At the same time that the 1985 draft Budget was presented the Council of Ministers also decided upon some significant measures relating to energy pricing, intended to promote the use of electricity and make full use of France's nuclear generating capacity. In future electricity prices will be increased at 1% below the inflation rate. Gas prices will be increased sufficiently in 1984 and 1985 to help reduce Gaz de France's severe losses. Thereafter, price increases will be in line with inflation. Petrol prices will be increased by 2% faster than inflation in 1984 and 1985. Coal prices will continue to be set in line with international prices. The additional petrol tax revenue will help to pay for the cuts in direct taxes announced in the draft 1985 budget in accordance with President Mitterand's pledge to reduce taxes by 1% of GDP.

e) Italy

11. In recent budgets family allowances for higher income earners have been progressively withdrawn and the availability of old age and invalidity pensions have been reduced. Prescription charges have been introduced for drugs unless they are essential or for emergency treatment.

12. The 1985 Budget was presented to Parliament on 1 October. The aim of the Budget measures is to reduce the PSBR from the 1984 level of 15.7% of GDP to 14.3% in 1985. To do this Mr Gorla, the Treasury Minister, is hoping to reduce total public expenditure by about 3% of the estimated 1984 outturn. The savings are targeted at three main areas. First, and foremost, transfers to the nationalised industries are to be reduced significantly. Second, health expenditure is to be reduced and, specifically, prescription charges are to be increased (although savings have not been defined). Third, expenditure on pensions is to be reduced, especially invalid pensions which make up the bulk of spending on pensions, but as yet the savings have not been defined.

f) Spain

13. The Government is working on a comprehensive reform of the social security system. It hopes to rationalise the structure and size of the benefits and thereby try to reduce the budget deficit. No announcements regarding the reforms are expected until 1986 at the earliest. During talks between the Government and the non-communist trade union organisations over 1985 wage settlements, the Government is reported to have made two concessions: no drastic cut in the budget deficit and delay in the social security review.

14. As a result of the 1984 Budget deficit running well above target the Government introduced a package of measures in June 1984 in an attempt to hold back the rise in public expenditure. Among these measures was the introduction of cash limits on government departments.

15. Press reports suggest that the 1985 Budget (to be announced within the next 10 days) will contain very few measures to restrain public spending. The two most significant initiatives are reported to be the restructuring of the shipbuilding industry, at a cost of 8000 jobs (savings unknown) and the closure, from 1 January 1985, of 1176 kilometres of passenger track which is expected to yield the equivalent of around £36 million in savings in the next financial year.

g) Belgium

16. In March 1984 the Government proposed a series of tough measures to reduce the cost of the social programmes. These included a common basic unemployment benefit with dependents' supplement, and a reduction in benefits for non-heads of families unemployed for over two years. In addition, it is proposed that family allowance will not be paid until the month following a birth. Limits will be imposed on the amount of total benefits an individual may receive and on indexed invalidity benefits. Higher rates paid to benefit recipients are to be restricted to those with no other income. These proposals are currently being considered by Parliament.

17. Prescription charges were increased on a sliding scale in the 1984 budget, but no increases have been proposed for 1985.

h) Netherlands

18. Unemployment, disablement and the minimum benefit levels were cut by 3% from 1 January 1984 and the bi-annual indexation of all benefits was suspended. There was a further 3% reduction in unemployment and disability benefits from July for those recipients whose previous salaries were above the minimum daily wage. The 1985 budget proposes further rate reductions in the above benefits.

i) Denmark

19. In the 1984 Budget the Government reduced some unemployment benefits and cut child benefits for high income earners with the overall aim of securing budget balance for individual schemes. In addition, social security benefits (excluding pensions) were de-indexed until 1987 and flat rate increases only will be paid.

j) Australia

20. An assets test has been introduced for age (ie, retirement) pensions, operative from March 1985. This test supplements the incomes test which already applies.

PARTY CONFERENCE MOTIONS

Speaking note for the Prime Minister

We must all be very careful at the Party Conference next week to say nothing which will worsen the situation, and intensify the pressures for higher public spending. There are, as usual, many motions down requiring us to take action which would be very expensive indeed. We must not shrink from squarely rejecting these, and if necessary basing our rejection explicitly on public expenditure considerations, in order to bring home to the Party the seriousness of our commitment to control public expenditure.

or pre-empt options for reductions whether in central or local government or the nationalised industries.

CONSERVATIVE PARTY CONFERENCE:POTENTIALLY SENSITIVE ISSUESTUESDAY OCTOBER 9THSOCIAL SECURITY. Reply Speaker Mr Newton (?)

Pressures to - increase real value of state pension
- maintain intact the second state earnings - related pension scheme (SERPS).

LAW AND ORDER. Reply speaker Mr Brothan

Requests for undertakings on spending on law and order or, in particular, police pay.

*ENERGY. Reply speaker Mr Walker

Pledges on the financing and investment of the coal industry, and coal prices.

WEDNESDAY OCTOBER 10TH*DEFENCE. Reply speaker Mr Heseltine

Pledges on spending on or the scale of the defence programme after 1986/7, when the NATO 3% commitment ends.

DRUG ABUSE. Reply speaker Mr Clarke

Pledges to increase policy NHS or Customs & Excise manpower to curb the drug problem.

HEALTH. Reply speaker Mr Fowler

New commitments on public spending levels in the longer term, or to preserve the present pattern and structure of services, including ancillary ones.

LOCAL GOVERNMENT. Reply speaker Lord Bellwin

Predictions about future spending rate levels after the abolition of the metropolitan councils.

THURSDAY OCTOBER 11TH*FOOD AND FARMING. Reply speaker Mr Jopling

Commitments to long-term maintenance of present objectives, grants etc., or maintenance of 'parity' with assistance to Agriculture elsewhere in the Community.

EMPLOYMENT. Reply speaker Mr King

Commitments to more and more generous schemes to help the jobless.

HOUSES AND LAND. Reply speaker Mr Gow

Promises of more generous subsidies or schemes to encourage sales of council houses and flats.

FRIDAY OCTOBER 12TH

EDUCATION. Reply speaker Sir K Joseph

Pressure for more spending to raise educational standards or to increase output of those qualified in key skills.

Agenda of the Conference

Chairman: DAME PAMELA HUNTER, D.B.E.

TUESDAY, 9th OCTOBER

First session: 9.30 a.m.–12.30 p.m.

- 1 Religious Service (*see page 30*)
- 2 Official welcome by the Worshipful the Mayor of Brighton, Cllr. John Blackman
- 3 Chairman's opening remarks
- 4 Adoption of the Annual Report (*see page 112*)
- 5 Debate on SOCIAL SECURITY

MOTION NO. 829.

MR MICHAEL JACK (*on behalf of the Southport Conservative Association*)
to move:

"This Conference, recognising the growing proportion of the population of pensionable age, calls upon Her Majesty's Government to develop further its social policies to ensure that those who have given a life time service to society can look forward to retirement free from economic and material worry."

Reply Speaker: DR. RHODES BOYSON, M.P., *Minister for Social Security*

- 6 Debate on LAW AND ORDER

MOTION NO. 493.

MR W. COATES (*on behalf of the Meriden Conservative Association*)
to move:

"That this Conference believes the Government must reconsider the whole problem of organised violence and intimidation and calls on her Majesty's Government to implement in full their manifesto promises on violence, law and order."

Reply Speaker: RT HON. LEON BRITTAN, Q.C., M.P., *Secretary of State for the Home Department*

- 7 The Chairman of the Party Organisation
MR. JOHN SELWYN GUMMER, M.P.

Second Session: 2.30–5.30 p.m.

- 8 Debate on ENERGY

MOTION NO. 284.

MR D. W. RIDGE (*on behalf of Newark Conservative Association*) *to move:*

"This Conference calls upon Her Majesty's Government to embark upon a vigorous programme to restore the pride and confidence of all those working within the coal industry; and to ensure the mining community is given every

assistance to change and adapt itself to modern needs, and thereby obtain the benefits of becoming strong and self-sufficient."

Reply Speaker: RT HON. PETER WALKER, M.B.E., M.P., *Secretary of State for Energy*

9 Debate on CONSERVING THE ENVIRONMENT

MOTION NO. 307.

MR MICHAEL WILLIS (*on behalf of Brentwood and Ongar Conservative Association*) to move:

"This Conference calls on the Government to conserve the environment by all practical means, including the reduction of known sources of pollution and vigorous defence of the Green Belt."

Reply Speaker: THE HON. WILLIAM WALDEGRAVE, M.P., *Parliamentary Under Secretary of State, Department of the Environment*

10 Debate on PUBLIC RELATIONS

MOTION NO. 745.

MR R. D. APPLETON (*on behalf of Stockton North Conservative Association*) to move:

"This Conference urges the Government to smarten its public relations, to ascertain Conservative views and reactions on the ground and to explain its policies lucidly to the whole country."

Reply Speaker: RT HON. VISCOUNT WHITELAW OF PENRITH, C.H., M.C., *Lord President of the Council and Leader of the House of Lords*

WEDNESDAY, 10th OCTOBER

Third session: 9.30 a.m.—12.30 p.m.

11 Debate on RATES

MOTION NO. 644.

MR N. CUTTS (*on behalf of the Rushcliffe Conservative Association*) to move:

"This Conference welcomes the rate capping legislation but urges her Majesty's Government to make positive steps towards the abolition of the domestic rating system, replacing it eventually with a system of local taxation which bears more fairly on a wider spread of the population."

Reply Speaker: RT HON. PATRICK JENKIN, M.P., *Secretary of State for the Environment*

12 Debate on DEFENCE

MOTION NO. 50.

MRS ANGELA BROWNING (*on behalf of the Tiverton Conservative Association*) to move:

"This Conference urges Her Majesty's Government to continue its realistic defence policy and strong support of NATO. The Conference is equally supportive of the Government's initiatives to encourage détente between East and West."

Reply Speaker: RT HON. MICHAEL HESELTINE, M.P., *Secretary of State for Defence*

13 Debate on DRUG ABUSE

MOTION NO. 65.

MR J. D. ATKINSON (*on behalf of Pudsey Conservative Association*) to move:

"That this Conference requests Her Majesty's Government to take immediate steps to eliminate drug and solvent abuse—with particular emphasis on harsher sentences for 'pushers'."

Reply Speaker: RT HON. KENNETH CLARKE, Q.C., M.P., *Minister for Health, Department of Health and Social Security*

Fourth Session: 2.30–5.30 p.m.

14 Debate on ECONOMY AND TAXATION

MOTION NO. 81.

MR SIMON H. HOY (*on behalf of the Guildford Conservative Association*) to move:

"This Conference believes that low inflation and tight public expenditure provide far the best foundation for the expansion of jobs and prosperity and urges the Government both to adhere to these basic policies and to reinforce them with all possible measures in order to reform the labour market and ease the transition for those who have to move jobs."

Reply Speaker: RT HON. NIGEL LAWSON, M.P., *Chancellor of the Exchequer*

15 Debate on HEALTH

MOTION NO. 437.

MR IAIN McCRONE (*on behalf of the North East Fife Conservative Association*) to move:

"This Conference welcomes the increased expenditure by H.M. Government on health and urges that every effort is made to ensure that Health Authorities and Boards provide the most cost effective ancillary service consistent with the best interests of patient care."

Reply Speaker: RT HON. NORMAN FOWLER, M.P., *Secretary of State for Social Services*

16 Debate on LOCAL GOVERNMENT

MOTION NO. 576.

CLLR BRIAN MOGFORD (*on behalf of the Birmingham, Edgbaston Conservative Association*) to move:

"This Conference congratulates her Majesty's Government in their persistent action to abolish the Metropolitan County Councils and re-affirms its belief that their abolition will improve standards of accountability of elected representatives to their electorate; that it will reduce the duplication caused by two tier local government in urban regions; will provide a greater degree of choice to residents therein and thereby help to contain rate rises to both residents and job-providing business enterprises."

Reply Speaker: LORD BELLWIN, *Minister for Local Government, Department of the Environment.*

THURSDAY, 11th OCTOBER

Fifth Session: 9.30 a.m.–12.30 p.m.

17 Debate on FOOD AND FARMING

MOTION NO. 365.

MR PETER TALBOT (*on behalf of North Norfolk Conservative Association*)
to move:

"While acknowledging the need for economies in the soaring cost of the Common Agricultural Policy, this Conference urges Her Majesty's Government to ensure that the British farmer is treated fairly in comparison with his European equivalent, and that United Kingdom policies directly supporting our agriculture are maintained."

Reply Speaker: RT HON. MICHAEL JOPLING, M.P., *Minister of Agriculture, Fisheries & Food*

18 Debate on EMPLOYMENT

MOTION NO. 215.

MRS SALLY WILLIAMS (*on behalf of the Ceredigion & Pembroke North Conservative Association*) *to move:*

"This Conference believes that, whilst this government has made a positive contribution to assist the unemployed to find work, there is still a gap between help available and the needs of those unemployed."

Reply Speaker: RT HON. TOM KING, M.P., *Secretary of State for Employment*

19 Debate on HOMES AND LAND

MOTION NO. 459.

MR JOHN WYLIE (*on behalf of the Fulham Conservative Association*) *to move:*

"That this Conference congratulates H.M. Government on the success of its measures to expand home ownership among Council and Housing Association tenants and now urges the Government to develop further policies to bring the benefits of home ownership to tenants of those Council-owned properties which are less suitable for outright sale (such as those on older, flatted estates or in high rise blocks), in partnership with independent Housing Associations and other organisations."

Reply Speaker: MR IAN GOW, T.D., M.P., *Minister for Housing and Construction, Department of the Environment*

Sixth Session: 2.30–5.30 p.m.

20 Debate on FREE ENTERPRISE AND INDUSTRY

MOTION NO. 398.

MR RAYMOND ROBERTSON (*on behalf of the Scottish Conservative & Unionist Association*) *to move:*

"This Conference, believing that industry in private ownership is a fundamental part of a free society, calls upon H.M. Government to make known its long term plans for the privatisation of the nationalised industries."

Reply Speaker: RT HON. NORMAN TEBBIT, M.P., *Secretary of State for Trade and Industry*

21 Debate on OVERSEAS AFFAIRS

MOTION NO. 705.

SIR DONALD WALTERS (*on behalf of the Cardiff North Conservative Association*) to move:

"That this Conference strongly supports Her Majesty's Government's initiative to reduce tension between the Communist Bloc and the Free World to secure balanced and verifiable disarmament and thereby to free resources for the promotion of wealth throughout the world."

Reply Speaker: RT HON. SIR GEOFFREY HOWE, Q.C., M.P., *Secretary of State for Foreign and Commonwealth Affairs.*

22 Debate on a BALLOTTED MOTION (*see enclosed ballot paper*)

FRIDAY, 12th OCTOBER

Seventh Session: 9.30 a.m.—12.00 noon

23 Debate on a BALLOTTED MOTION (*see enclosed ballot paper*)

24 Debate on EDUCATION

MOTION NO. 136.

CLLR F. ALLGOOD, J.P. (*on behalf of the Fareham Conservative Association*) to move:

"This Conference approves the Secretary of State's initiative to raise standards in education and asks that more should be done to ensure that young people are equipped with skills and knowledge that are of relevance to modern Britain."

Reply Speaker: RT HON. SIR KEITH JOSEPH, Bt, M.P., *Secretary of State for Education and Science*

Eighth Session: 2.15—3.20 p.m.

25 Financial appeal and collection in aid of Party funds

26 Address by

RT HON. MRS MARGARET THATCHER, F.R.S., M.P.

The Prime Minister and Leader of the Conservative and Unionist Party

Chairman: COL SIR ALASTAIR GRAESSER, D.S.O., O.B.E., M.C., T.D., J.P., D.L. President of the National Union of Conservative and Unionist Associations

The National Anthem

■ 3 OCT 1984

0 1 2 3 4
5 6 7 8 9



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PRIME MINISTER

2 October 1984

YOUR PES MEETING WITH MR TEBBIT ON 3 OCTOBER 1984

Treasury are asking simply for DTI to get back to baseline. Other spending Ministers are faced with much more severe economies. If Mr Tebbit is to be credible as an active member of the "Star Chamber", he should volunteer much more - as he can well afford to do. You could remind him at the outset of this Government's determination to deregulate and to free up markets. That should reduce the functions of DTI, their intervention expenditure, and the Department's head count.

We have identified five major areas for saving:

1. Regional Policy

50
Our separate brief recommends that total expenditure (in cash) on Regional Assistance should be held to £300m per annum over the 3 years 1985/86 to 1987/88. This would eliminate separate expenditure on land and buildings and on Regional Selective Assistance.

2. Non-Regional Assistance to Industry

This embraces general industrial R&D, costing around £300m per annum, and other forms of Selective Assistance

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costing £80-90m per annum. Keith Joseph managed on far lower sums: £102m and £49m respectively in 1980/81. We think you should tell Norman to get back to these levels quickly. Industry doesn't need this form of Supplementary Benefit. We suggest £50m (cash) per annum for Ministers to use as "Selective Assistance to Individual Industries, Firms and Undertakings". We could do more to exploit economies of scale in basic pre-competitive research within the EC.

3. Export Promotion and Trade Co-operation

Although not large in absolute terms, this expenditure has grown by a fat 50 per cent since 1980/81 - from £20m to £30m. We suggest it should be trimmed back to £25m, £20m and £15m over the 3 years.

4. Regulation of Domestic Trade and Industry and Consumer Protection

The same comments apply. It can, in our view, be cut down to a level £20m per annum from £30m plus.

5. Central and Miscellaneous Services

At over £140m, these look ridiculously high. They have more than doubled since 1979/80, and continue to show cash increases even on the baseline. The merger of the

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Departments of Trade and Industry has not merely procured no economy - it has cost more. We think you should persuade Mr Tebbit to reduce these costs - and the manpower which gives rise to them - by at least 5 per cent compound over the next 3 years. Cash figures of £130m, £120m and £110m look reasonable.

Summary of Savings

These are counted from the expenditure baseline (Summary Table Annex 1, attached to Peter Rees' letter of 2 August.)

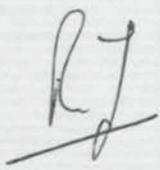
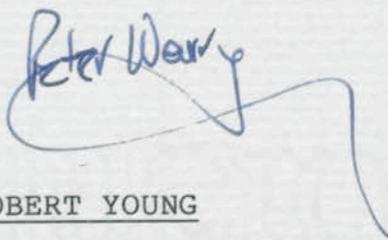
	<u>1985/86</u>	<u>1986-87</u>	<u>1987-88</u>
Regional Policy	175	163	175
Selective Assistance to			
Industry	45	31	33
General Industrial R&D	45	154	212
Export Promotion/Trade			
Co-operation	10	11	12
Regulation	11	12	13
Central and Miscellaneous			
Services	<u>15</u>	<u>29</u>	<u>45</u>
	<u>291</u>	<u>400</u>	<u>490</u>

Other Avenues

The expenditure headings which you will debate with Mr Tebbit are not the whole of the story. There is more yet

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to be squandered by the DTI nationalised industries. British Steel will be the most demanding, and British Shipbuilders could yet deliver a nasty surprise. This prospect should give you more than enough ammunition to press Mr Tebbit for more and faster asset sales. How about speeding up the disposal of Land Rover and Leyland Truck and Bus? And the war shipyards? And the shares which HMG still has in British Aerospace?

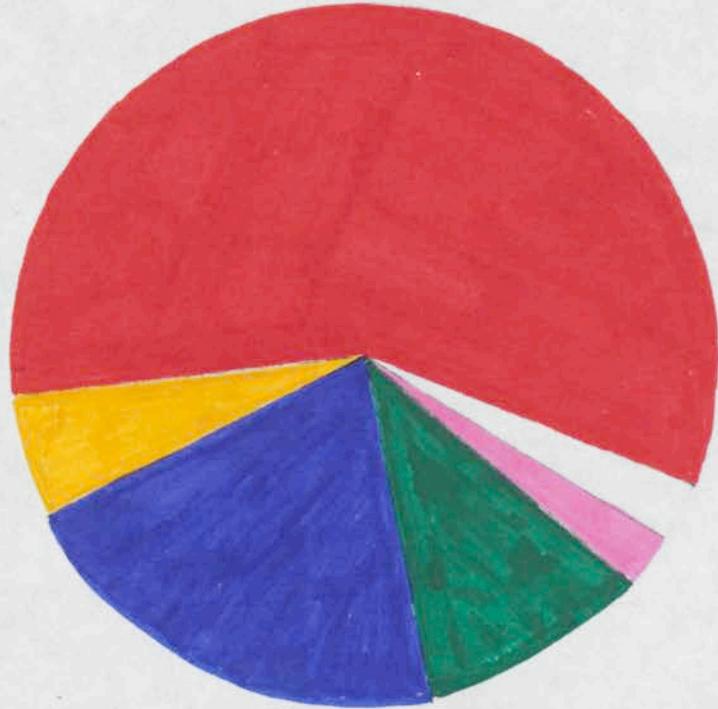
 

JOHN REDWOOD/PETER WARRY/ROBERT YOUNG

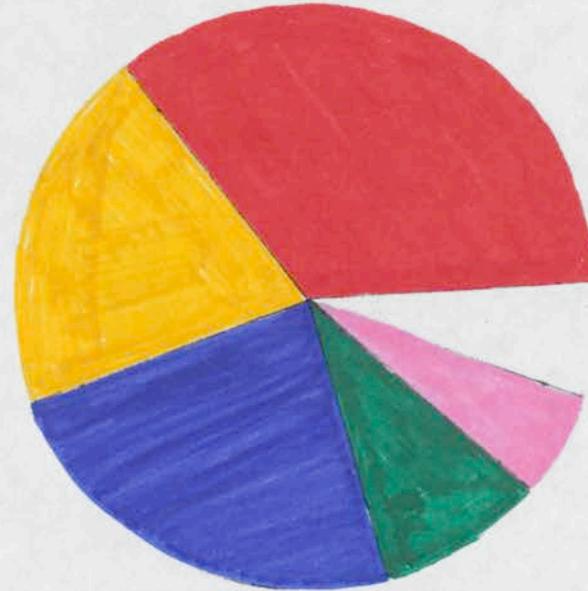
CHART 3

MAJOR COMPONENTS OF DTI SPEND

1980/81



1984/85



1987/88
PES BID



- NATIONALISED INDUSTRIES INCLUDING BL
- SCIENTIFIC & TECHNOLOGICAL SUPPORT
- REGIONAL SUPPORT
- OTHER INDUSTRIAL SUPPORT
- TRADE REGULATION & EXPORT PROMOTION
- CENTRAL & MISCELLANEOUS SERVICES

SECRET

Prime Minister ①

This is the note the Treasury promised. I suggest that at the 2:30pm meeting you concentrate on general philosophy and turn to figures after E(R.I)

AT 2/10

PUBLIC EXPENDITURE SURVEY 1984: TRADE AND INDUSTRY

The purpose of the meeting is to settle Mr Tebbit's expenditure programmes on a basis that enables him to serve as a member of the Star Chamber.

2 The main aim is to secure large savings in DTI's mainline programme of industrial support. These are needed not only to help secure the overall planning totals agreed by Cabinet but also to enhance the Star Chamber's authority to demand savings from others - particularly on agricultural subsidies. While large reductions in agricultural and industrial subsidies might be thought to involve a change in policy, they would not breach pledges in the manifesto or elsewhere.

3 Mr Tebbit's proposals on regional policy are to be discussed by E(A) earlier in the day. The savings he proposes fall short of those sought by Treasury Ministers by about £80 million in a full year. This underlines the need for savings in his non-regional spending.

4 The outstanding points on the provision for Mr Tebbit's nationalised industries concern the Post Office and British Steel and should be capable of settlement in bilateral correspondence.

5 The agenda for the Prime Minister's meeting is, therefore:

- i DTI mainline programme excluding regional policy
- see Annex A
- ii ECGD - see Annex B
- iii Redundancy Fund (Where we understand that Mr Tebbit is being advised to oppose a change which would produce savings in the Department of Employment's programme) - see Annex C.

TI's MAINLINE PROGRAMME (excluding regional policy)

	80	143	-73
	£m		
	1985-86	1986-87	1987-88
1. Baseline	783	752	773
<u>Secretary of State's proposal</u>	<u>0</u> 1227.5	<u>1184.2</u>	<u>1215.2</u>
2. Reduced requirements	<u>N</u> - 14	- 25	- 37
3. Further savings offered at bilateral	1297	1284	1185
4. Bids conceded by Chief Secretary	143	139	49
5. Bids not conceded by Chief Secretary	13	25	24
6. Net addition to baseline	+ 115	+110	+ 21

Further changes sought by Chief Secretary (see letter of 27 September)

7. Bids not conceded	- 13	- 25	- 24
8. Further reductions in programmes or increased charges	- 20	-122	-225
9. Net changes from baseline	+ 82	- 37	-228
10. Gap between Secretary of State and CST	33	147	249
		100	200

1. Mr Tebbit maintains that the modest reduced requirements and savings he has offered (lines 2 & 3 above) are the most that are "practicable and realistic".

2. The Chief Secretary has conceded that large savings are not practicable for 1985/86 and has reduced his bid for savings to £20 million. But for later years large savings are practicable from "uncommitted" industrial support - estimated at £243m and £370m in 1986/87 and 1987/88 (see table attached). Higher revenue from charges could also contribute. Both kinds of savings fit in well with the Government's general policies. The Chief Secretary would leave it to Mr Tebbit to decide how to achieve the savings.

1052.
123
1215
1384
123
1264

3. Industrial subsidies may be justified in certain particular cases where it can be shown that market forces cannot operate effectively, eg the Alvey programme. But the Treasury believes that much DTI spending is on intervention in industry which has little effect on what companies actually do and is inconsistent with the broad aims of the Government's economic policy. The Chief Secretary proposed a joint review of the DTI's industrial support schemes in the summer. This would be designed to clarify objectives and test the evidence that actual or expected benefits exceed the cost of the subsidies. Mr Tebbit has not yet agreed and Permanent Secretaries are to discuss ~~it~~ after the survey. Such a review should of course ideally precede not follow further commitments. But the PES timing makes this difficult. The dilemma might be resolved if Mr Tebbit could be persuaded to withdraw his additional bids and offer savings of at least £20m in 1985-86, £75 million in 1986/87 and £150 million in in 1987/88. These figures would still leave two-thirds of DTI's uncommitted current provision to fund this type of spending if the review demonstrated a case.

4. In addition the DTI could increase resources available to them by charging. There may be a case for free or subsidised services to "first time exporters", and a few other cases. But in general the full costs of export promotion and of DTI's regulatory functions could and should be recovered. This is already the policy in other areas (eg prudential supervision and the nuclear inspectorates). Nor is it right, as DTI seem to assume, to charge only "what the market will bear". If firms, eg exporters, will not pay the full cost for DTI services, it generally means:

either that the service is not worth providing;

or that it is being provided inefficiently.

Full-cost charging brings this out and allows the private sector to compete.

POINTS TO MAKE

Mainline DTI Expenditure

5. a. The DTI should contribute adequate savings on its non-regional expenditure, especially as its programme will be over baseline in 1985/86. DTI's good progress on parts of BL and privatisation needs to be followed now by reducing and tightening up interventionist subsidies to the private sector even though they may now be directed at "innovation". Policy changes are involved but not a breach of pledges.
- b. The savings Mr Tebbit has offered so far on non-regional expenditure are inadequate: less than his aggregate bids and small (up to £30 million a year) on a non-regional baseline of nearly £800 million. The savings are of course needed as contribution to overall Cabinet objectives. But also to ensure Mr Tebbit can serve on Star Chamber without weakening its authority in relation to other subsidies, particularly agriculture (which Mr Tebbit himself is believed to favour cutting).
- c. Ask Mr Tebbit for proposals and look for the following:
- i. drop additional bids (see paragraph 4 a. above);
 - ii. savings of £20m in 1985/86 and, not less than £75m and £150m in 1986/87 and 1987/88 by a combination of reductions in industrial support and charging;
 - iii. seek Mr Tebbit's undertaking to support a sensible formulation of a joint review of his industrial support which Permanent Secretaries are to discuss after the survey. The review would be "without prejudice" and it could be taken into account in the 1985 Survey.

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GRANT GIVING SUB-PROGRAMMES WHERE REDUCTIONS ARE BEING SOUGHT: BASELINE AND COMMITMENTS

	£ million			
	1985-86 in June 1984	1985-86 in Sept 1984	1986-87	1987-88
1. Selective Assistance to Individual Industries				
- Baseline	94.7	94.7	80.9	82.9
- Commitments	81.7	91.8	59.9	43.9
- Committed: (%) of Baseline	(86)	(97)	(74)	(53)
2. General Industrial R & D				
- Baseline	295.3	295.3	304.4	312.0
- Commitments	225.3	279.2	136.0	45.0
- Committed: (%) of Baseline	(76)	(95)	(45)	(15)
3. Aircraft & Aeroengine General R & D				
- Baseline	35.4	35.4	36.3	37.2
- Commitments	3.4	35.7	3.3	4.2
- Committed: (%) of Baseline	(10)	(100)	(9)	(11)
4. Space				
- Baseline	67.7	67.7	69.0	70.7
- Commitments	68.5	67.1	49.0	40.6
- Committed: (%) of Baseline	(101)	(99)	(71)	(57)
5. Future Industrial Support				
- Baseline	2.7	2.7	1.0	1.0
- Commitments	0	0	0	0
- Committed: (%) of Baseline	-	-	-	-
6. Total				
- Baseline	495.8	495.8	491.6	503.8
- Commitments	378.9	473.8	248.2	133.7
- Uncommitted	116.9	22.0	243.4	370.1
- Committed (%) of Baseline	(76)	(96)	(50)	(27)

	£m		
	1985-86	1986-87	1987-88
Expenditure baseline	29.9	-159.3	-163.2
Reduced requirements	-21.0	-	- 0.2
Additional bids (conceded by CST)	+307.4	+319.4	+187.1
Savings agreed in bilateral (transfer of refinance)	- 76.5	- 19.7	- 18.1
Net addition to baseline	209.9	299.7	168.8
Further saving sought by CST (switch from \$ finance)	- 1.8	-12.5	-33.9
CST net change from baseline	208.1	287.2	134.9

Export subsidies (interest make-up) are paid to the banks to bridge the gap between their current cost of funds and the fixed Consensus interest rates charged to the buyer of UK capital goods. The cost of these subsidies rises rapidly over the Survey period (by some £800 million in total) reflecting higher forecast sterling and, especially, US dollar interest rates. There is thus a strong case for discouraging the use of US dollar finance. Loading the interest rate for new US dollar loans to give the same subsidies as on sterling loans would produce savings without completely withdrawing support for a major trading currency. The size of the saving would vary with relative interest rates. On present forecasts it would save £34 million in 1987-88. The loading could be regularly reviewed in the light of prevailing market rates. This is the only way of controlling rising costs under the present arrangements (since Consensus rates reflect international agreements. Mr Tebbit has offered no other real savings on ECGD's programme). The saving from the transfer of refinance is entirely painless.

Points to make

(i) Ask Mr Tebbit to accept the loading of interest rates for new US dollar loans sufficient to provide savings equivalent to a 100 per cent switch out of dollar finance whilst interest rates remain high. Subsidies to exporters cannot continue on an open-ended basis regardless of cost. The Treasury proposal (the use of loading) is not equivalent to total withdrawal of support for US dollar loans.

(ii) The reduction of subsidies on dollar finance to levels equivalent to those available on sterling finance may lose exports in some markets but the overall effect will be small.

(iii) Experience with less direct methods of controlling the cost eg encouragement to use currencies with lower interest rates has not in practice provided savings. A mandatory change is essential if savings are to be secured.

REDUNDANCY FUND

	1985-86	1986-87	1987-88
Baseline	254	261	268
Estimating increase	90	87	89
Option for Savings	- 37	- 36	- 37

Bid reflects higher forecasts (agreed by Treasury) of the number of payments and unit costs. The option entails cutting Redundancy Fund rebate to employers from 41 to 35 per cent of their statutory payments.

Mr King has agreed with the Chief Secretary to make the savings but has consulted Mr Tebbit because of the industrial implications. Securing the savings should allow the Employment programme to be settled outside the Star Chamber.

Line to take

(a) Company finances are improving, shedding of labour has slowed and perennial arguments against cutting rebate are now much weaker.

(b) Sums involved are tiny compared with benefits to companies from 1984 Budget (£1000m or so); and even smaller as a proportion of total redundancy costs (firms typically pay out more than their statutory requirement).

(c) Companies will eventually benefit from a lower rate of contribution to balance the Fund.

Note: A cut to anything other than 35 per cent would need main legislation as would exemption for small firms.



10 DOWNING STREET

From the Private Secretary

SIR ROBERT ARMSTRONG
CABINET OFFICE

Public Expenditure Survey 1984: Small Ministerial Group

The Prime Minister has seen your minute of 28 September reference A084/2599. She wishes the composition of the Group to be

Lord President of the Council (Chairman)
Home Secretary
Secretary of State for Scotland
Lord Privy Seal
Secretary of State for Trade and Industry
Chief Secretary, Treasury

She would like the Secretary of State for Trade and Industry to be a member but this would be conditional upon agreement being reached between him and the Chief Secretary on the outstanding differences on his Departmental programme. A meeting has been arranged between him, the Prime Minister, the Chancellor and the Chief Secretary for Wednesday afternoon in an effort to achieve this.

She is content for you to approach members of the Group informally before Thursday in order that an early start can be made on scheduling the work of the Group. This can include the Secretary of State for Trade and Industry who is aware that his membership of the Group is conditional upon resolution of the outstanding differences.

Andrew Turnbull

1 October 1984

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10 DOWNING STREET

From the Private Secretary

1 October 1984

Public Expenditure Survey

The Prime Minister has seen the Chief Secretary's minute of 27 September and is content for the paper attached to it to be circulated for the 4 October Cabinet meeting. This should be done 24 hours in advance, with appropriate handling instructions.

I am copying this letter to Richard Hatfield (Cabinet Office).

Andrew Turnbull

Richard Broadbent, Esq.,
Chief Secretary's Office.



10 DOWNING STREET

Pune Minuti (2)

I have arranged for you to
see Mr Tebbitt on his own
on Wednesday 2.30 - 3.00 pm
with a quadrilateral with
CL (G) and CST at 18.15 pm
after E (NI)

Treasury have sent on
the attached correspondence.
No need to go into the
detailed figuring as a
specific brief will come over
on Tuesday night.

AT

28/9

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cc Mr Scholar
Mr Monck
Mr Lovell
Mrs Case
Mr R H Wilson
Mr Bent
Mr White
Mr King
Mr Gray
Mr Yeo

Treasury Chambers, Parliament Street, SW1P 3AG

Mr Felstead
Mr D Jones

Rt Hon Norman Tebbit MP
Secretary of State for Trade and Industry
Department of Trade and Industry
1 Victoria Street
LONDON SW1H 0ET

2 August 1984

Norman Tebbit

PUBLIC EXPENDITURE SURVEY 1984 - DTI AND ECGD

Following Cabinet on 5 July, I am writing to propose an agenda for our bilateral meeting in September on your departmental programmes.

The attached table set out the key figures for DTI and ECGD and I suggest we should use them as the basis for our discussion. I hope that any revisions that may be needed as a result, for example, of revised economic assumptions can be agreed between officials so that revised tables can be circulated before we meet.

For each department, I suggest that having dealt with a reduced requirement we should start our discussion with your bids for additional expenditure. However, as I made clear in Cabinet, the overall position is extremely tight and I will be able to agree to additions only in exceptional cases. Elsewhere it must be a question of reordering priorities within existing programmes.

Of the bids you have put forward, I accept that the cost of the recent launch aid contracts have to be met and that the additions for shipbuilding are largely the result of interest rate movements and the performance of British Shipbuilders. I appreciate also that there will need to be payments to British Telecom for civil defence services, although how large they should be and who should make them has still to be settled. For ECGD, I accept that the bulk of the increase on interest support relates to existing commitments and is thus, effectively irresistible. It will be all the more important for us to look carefully at the scope for altering the terms for new business.

Against this background, the main focus of our meeting must be to consider the scope for savings. I should make clear at the

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outset that in order to hold the expenditure totals to the figures agreed by Cabinet, I must press you to avoid any increase over the baseline for 1985-86 and to make substantial net savings in the later years leaving aside your expenditure on regional policy.

We have agreed already to secure substantial net savings from the changes in regional policy. These will derive from the Scottish and Welsh Offices as well as your own department. We shall be discussing how best to proceed in this field in E(A) in the near future and until decisions on the details are reached we cannot estimate how the savings will be distributed between programmes and among departments. I suggest therefore that we should not discuss these regional policy questions at our bilateral but should leave them to be settled in the separate regional policy discussions. It is crucial, however, that the savings are brought into account in time for the Autumn Statement. Moreover, I should wish to discuss with you at our bilateral the scope for reducing expenditure during the transitional period for example by a moratorium on RDGs or stricter criteria for regional selective assistance.

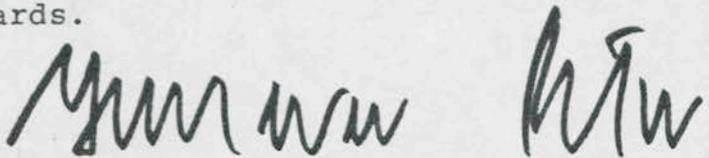
Turning to the rest of your programme, the table of possible reductions indicates the main areas where savings might be made. They might include reductions in the expenditure not yet committed over a wide range of your assistance schemes as well as the introduction (or increase) of charges where this would be appropriate. Naturally, if you would prefer to find savings in other ways I would be happy to consider your proposals.

We may also need to take into account the implications for your programme of the arrangements agreed by E(A) earlier this year requiring offsets to domestic programmes where Community expenditure rises faster than has been allowed for. However, in the first instance this is for discussion by officials.

I envisage bringing forward proposals on the provision for pay in 1985-86 in mid-September. If, as in earlier years, we decide to set a figure below that implicit in the present baseline and to remove the difference from programmes, that exercise can proceed in parallel with the bilateral discussions.

Finally we need to discuss manpower numbers in your department. I understand that you are not yet in a position to take a final decision on privatising the Warren Spring Laboratory or hiving off the Patent Office. I must press you, therefore, for further efficiency savings with the aim of reducing your 1 April 1988 target by 3 per cent (leaving aside the manpower implications of whatever is decided on regional policy). I hope that further contracting-out can play a major part in this. For ECGD, I am content that the manpower baseline agreed last year should remain until final decisions on the Matthews Report have been taken.

I am sending copies of this letter to Jim Prior, George Younger, and Nicholas Edwards.



PETER REES

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Summary Table

EXPORT CREDITS GUARANTEE DEPARTMENT

A. Expenditure Baseline

£ million

	1984-85	1985-86	1986-87	1987-88
Refinancing of fixed rate Export Credits	18.5	26.7	3.9	4.0
Cost Escalation Guarantees	8.3	-	1.3	1.4
Interest Support Costs	130.3	0.7	-168.5	-172.7
Mixed Credit Matching Facility	1.5	2.5	4.0	4.1
Total	158.6	29.9	-159.3	-163.2

B. Expenditure: Reduced Requirements

Refinance		-38.5	-12.8	-15.5
Cost Escalation Guarantees		-1.6	-	-0.1
Mixed Credits		-	-	-0.1
Total		-40.1	-12.8	-15.7

C. Expenditure: Additional Bids

Interest Support Costs		177.5	201.0	142.3
TTC/FES		5.0	5.0	5.0
Total		182.5	206.0	147.3

D. Expenditure - Options for Reductions

Transfer of refinance		32.0	-	-
Withdrawal of Mixed Credits Matching Facility		2.0	3.5	3.5
Switch from US dollar to sterling financing				
(i) ECGD proposed option		0.4	2.6	7.2
(ii) Treasury alternative		1.6	10.4	28.8
Total (ECGD option)		34.4	6.1	10.7
Total (Treasury alternative)		35.6	13.9	32.3

E. Running Costs

Running Costs	30.0	37.0
(Percentage increase	5	23)

F. Manpower

	1.4.84	1.4.85	1.4.86	1.4.87	1.4.88
Baseline	1840	1840	1835	1835	1830

DEPARTMENT OF TRADE AND
INDUSTRY

A. Expenditure Baseline

£ million

	1984-85	1985-86	1986-87	1987-88
*Total to nearest million (excluding local authority relevant current expenditure and external financing of nationalised industries)	1291	1227	1184	1215

Includes Regional development grants of

385	380	370	379
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*Subprogramme details at Annex 1

B. Expenditure: Reduced Requirements

£ million

	1985-86	1986-87	1987-88
Total reduced requirements	-14.0	-24.8	-36.9

C. Expenditure: Additional Bids

*Regional development grants	26.0	112.0	143.0
Selective assistance to individual industries	11.0	17.0	20.0
General industrial R & D	2.0	7.0	4.0
Regulation of domestic trade and consumer protection	0.0	0.8	0.0
Finance for Rolls Royce Ltd	28.5	21.8	0.0
Other aircraft and aeroengine projects	72.1	79.7	21.8
Refinancing of home shipbuilding lending	4.0	3.0	5.6
Interest support costs	15.8	21.3	17.4
Assistance to the shipbuilding industry	5.1	4.0	0.0
Assistance to the steel industry	4.8	4.2	2.0
Other central and miscellaneous services	1.0	0.0	0.0
Civil defence	24.0	24.0	24.0

Total additional bids	194.3	294.8	237.8
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Further bid

Support for films	2.0	2.0	2.0
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* Additional bids for regional development grants will be handled in the separate discussions about regional policy.

D. Expenditure: Options for Reductions

Provision of land and buildings	}	45	50	70
Selective assistance to individual industries				
Promotion of tourism	}	76	100	150
General industrial R&D				
Aircraft and aeroengine general R&D	}	35	30	35
Space				
Export promotion and trade co-operation	}			
Regulation of domestic trade and consumer protection				
Total reductions		156	180	255

E. Manpower

	1.4.85	1.4.86	1.4.87	1.4.88
Baseline	12800	12700	12700	12700
Reduced requirements (including savings to offset additional bids)	-	-	-	-
Additional bids	-	-	-	-
Options for reductions p.a.	-	127	127	127
Revised baseline	12800	12573	12446	12319

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Summary Table: Annex 1

**DEPARTMENT OF TRADE AND
INDUSTRY**

Expenditure Baseline: Subprogrammes

	£ million			
	1984-85	1985-86	1986-87	1987-88
Regional development grants	385.0	380.0	370.0	379.3
Provision of land and buildings	28.8	30.1	31.0	31.7
Selective assistance to industry in assisted areas	63.8	64.5	61.6	63.1
Other regional support	2.1	0.8	0.8	0.8
Selective assistance to individual industries firms and undertakings	94.4	94.7	80.9	82.9
Promotion of tourism	33.7	35.2	36.1	37.0
Other support services	5.9	3.4	3.5	3.6
Future industrial support	0.5	2.7	1.0	1.0
General industrial R&D	283.4	295.3	304.4	312.0
Aircraft and aeroengine general R and D	34.4	35.4	36.3	37.2
Space	65.0	67.7	69.0	70.7
Concorde development and production	1.0	1.4	-0.3	-0.3
Finance for Rolls Royce Ltd	0.4	-19.5	-15.8	-16.2
Other aircraft and aeroengine projects and assistance	20.8	17.2	20.3	20.8
Refinancing of home shipbuilding lending	-23.0	-24.0	-19.0	-19.5
Interest support costs	10.7	-3.5	-19.5	-20.0
Assistance to the shipbuilding industry	31.7	18.1	2.4	2.4
Assistance to the steel industry	53.1	19.4	7.3	7.5
Export promotion and trade co-operation	28.6	29.9	30.9	31.6
Regulation of domestic trade and consumer protection:-				
i. Central Government expenditure	27.8	31.3	32.0	32.8
ii. Local authority capital expenditure	1.9	2.0	2.1	2.1
Other central and miscellaneous services	140.6	145.4	149.2	154.7
<hr/>				
Total to nearest million (excluding local authority relevant current expenditure and external financing of nationalised industries)	1291	1227	1184	1215

Expenditure: Reduced Requirements

	£ million		
	1985-86	1986-87	1987-88
Provision of land and buildings	-3.0	0.0	0.0
Selective assistance to individual industries	-9.0	-24.8	-24.0
Future industrial support	-2.0	0.0	0.0
Finance for Rolls Royce Ltd	0.0	0.0	-10.7
Assistance to the shipbuilding industry	0.0	0.0	-2.2
<hr/>			
Total reduced requirements	-14.0	-24.8	-36.9

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RECORD OF A MEETING IN THE CHIEF SECRETARY'S OFFICE AT 3 PM ON
WEDNESDAY, 5 SEPTEMBER 1984

Present:

Chief Secretary
Mr A H Lovell
Mr P Mountfield (for part)
Mr M C Scholar
Ms E Conn
Mr E A Yeo
Mrs L E Bennett (for part)
Mr A N Ridley
Mr E J W Gieve

Department of Trade & Industry

Secretary of State
Sir Brian Hayes
Sir Anthony Rawlinson
Mr J Gill (ECGD) (for part)
Mr A C Russell
Mr H V B Brown

EXPORT CREDITS GUARANTEE DEPARTMENT BILATERAL

1. Additional bids and reduced requirements

The Chief Secretary accepted all the bids and reductions except that for Tender to Contract/Forward Exchange Supplement. He noted that most of the bids were inescapable and that the largest of them, for interest support costs, was due to higher Treasury interest rate assumptions.

He said that, in aggregate, he could not secure lower figures than £100 million above baseline in 1985-86, and £150 million above baseline in 1986-87. He envisaged a saving of £50 million on the baseline in 1987-88. His proposals were in the form of a package and savings that would become available on regional policy simply had to be utilised against the large bids for launch aid and for shipbuilding.

On manpower, the Secretary of State said he agreed to meet the requirement of a 3 per cent reduction by April 1988 but there were certain caveats. The manpower implications of the changes in regional policy would need to be considered in due course. Second, if the Scrutiny recommended additional staff for the Radio Interference Service, something must be done. Third, the needs of the Companies Registration Office, as identified by the current studies, would have to be met. Fourth, consideration would need to be given to the phasing of the reduction.

The Chief Secretary accepted that these caveats involved special areas where the precise manpower requirements would have to be considered by the Department and the Treasury in due course.

2. Regional assistance

The Secretary of State said that decisions on the new regional grant scheme would need to be taken with colleagues from the territorial departments but that he hoped they would accept his general approach. To provide a contribution towards savings in 1985-86 however, he had decided that he must be prepared to have a moratorium of 4 months' duration. There were alternative ways in which such a moratorium might be wound down, and these would be for the experts to work out, but he envisaged that the moratorium would be in place for two years to the end of 1986-87. He also said that his overall package utilised the savings which would become available on certain assumptions about the new regional policy. On this basis the estimates for regional expenditure by the DTI would be:

	£ million		
	1985-86	1986-87	1987-88
Present baseline	444.5	431.6	442.4
Proposed baseline	429.5	471.6	371.0
	<u>-15.0</u>	<u>+40.0</u>	<u>-71.4</u>

The Chief Secretary said that the expected savings on regional policy changes could not be pre-empted to offset increases elsewhere, and that in any event the actual figures would have to be decided in E(A) Committee. He would need to have fuller details of the proposal, and his officials would need to examine it. The Secretary of State said that the savings on what would have been attributed to DTI spend on the old RDG system, were more than sufficient to pay for launch aid.

3. Reduced requirements

The Chief Secretary said that he accepted the offered 'reduced requirements' in full, viz 1985-86, £-14.0; 1986-87, £-24.8m; 1987-88, £-36.9m.

4. Bids already conceded

The Chief Secretary said that he had conceded five additional bids in his bidding letter, viz

	£ million		
	1985-86	1986-87	1987-88
Finance for Rolls Royce Ltd	28.5	21.8	-
Other aircraft and aero-engine projects	73.1	80.7	22.3
Refinancing of home shipbuilding lending	4.0	3.0	5.6
Interest support costs	24.5	27.7	19.7
Assistance to the shipbuilding industry	5.1	4.0	-
	<u>135.2</u>	<u>137.2</u>	<u>47.6</u>

5. Assistance to the steel industry

The Chief Secretary said that it was inappropriate to include contingency provisions for later years in the Survey and that the bids for the later years should be withdrawn. He was prepared to accept the bid of £4.8 million in 1985-86. The Secretary of State accepted.

6. Other central and miscellaneous services

The Secretary of State said that although the stimulation of inward investment was generally a commercial matter, Government encouragement was sometimes necessary. The Chief Secretary accepted the bid of £1.0 million in 1985-86.

7. Civil Defence

The Secretary of State said he was unwilling to bear the projected heavy Civil Defence expenditures on his programme. Civil Defence provisions of this order should be for the Home Office, not the DTI.

The Chief Secretary said he had been informed of the background to the matter and the sizeable expenditures concerned. He proposed that the three bids be deleted but asked that the DTI should scrutinise the detail of the present claim, reduce it to a realistic level, and sort out which Department would be the appropriate one to take responsibility. The Treasury was prepared to see the eventual justified cost as a charge against the Reserve, but only on the basis that it was under the firm control of a specific Minister.

8. Support for films

The Chief Secretary said he understood the DTI was prepared to find £0.5 million in each of the Survey years. In view of that, he would concede the balance of £1.5 million in each year.

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9. General industrial R and D
 10. Aircraft and aeroengine general R and D
 11. Space

The Secretary of State said that taking 1986-87, the options for reductions proposed by the Treasury for these sub-programmes were some 25 per cent of the aggregate expenditure. He said the option cuts proposed by the Treasury were so severe that they would not only mean changes of policy but, effectively, the abandonment of the programmes.

12. Provision of land and buildings

The Chief Secretary said that he understood the existing provisions were based on a 12 months' supply of vacant stock and a vacancy rate of 15 per cent, and that such margins were out of line with the private sector.

The Secretary of State said that the Treasury's options for reductions were so large that he would be very exposed if he accepted them. He did however agree that some savings could be made here (£7m, £10m, £10m.) It would be important to ensure that the same programmes of his territorial colleagues should be cut the same extent. He would also like officials to explore the possibility of the EIEC being able to raise finance with the private sector.

The Chief Secretary accepted the savings subject to the provisos put by the Secretary of State.

13. Selective assistance to individual industries

The Chief Secretary expressed concern at the sizeable additional bids in this programme and said that, in his quest for reductions, he had expected that savings should be possible from the relatively uncommitted expenditures, particularly in later years.

The Secretary of State said that the programme of assistance was a matter of both policy and contractual commitment. To get back to the baseline would mean stopping new offers of aid, and postponing others. A moratorium of some kind would probably be illegal. He considered it would be difficult to persuade colleagues that the Small Firms Loans Guarantee Scheme should be closed in December. There would be a renewal of the agitation when the procedures were tightened earlier in the year.

General

The Secretary of State said that he could not find savings to offset the major bids on his aggregate programme. To do so would mean breaking contracts and Manifesto commitments. His Department had however found minor savings and, as part of a package, he could offer:

	£ million		
	1985-86	1986-87	1987-88
Provision of land and buildings	- 7.0	-10.0	-10.0
Space	- 3.0	- 5.0	- 7.0
Launch Aid	- 5.0	+ 5.0	
Other	- 0.2	+ 0.2	
Mergers and Monopolies Commission	- 0.1		
Insolvency Service	-	-	- 0.5
Companies Registration Office		- 0.7	- 0.8
Patent Office	- 0.9	-	- 0.5
Iron and Steel	-	- 3.0	- 1.7
Textiles	- 6.5	- 1.5	+ 4.0
Insurance Supervision	-	- 2.0	- 2.0
Support for films	- 0.5	- 0.5	- 0.5
Vote 4		-0.1	
Other savings/re-phasing	- 3.3	-15.3	+2.2
	-26.5	-32.9	-16.8

NOTE. The final details of these figures were provided by DTI officials after the meeting. Further adjustments were made to reflect the treatment of the additional bids for Steel in the later two years, producing figures of £28.7m and £14.8m respectively.

The Secretary of State said:

- (a) he was willing for his officials to discuss with Treasury colleagues procedures for controlling selective financial assistance through limits on the volume of offers and perhaps on the terms of payments where this was practicable. But whether this would satisfy the conditions which needed to be met for cash limiting to work remained to be seen, and what was possible in terms of expenditure control given sufficient end-year flexibility, might not be acceptable in relation to cash limit precedents.
- (b) that it was now for points of detail to be cleared up by officials. He wished his proposals to be seen as a package; it went as far as he could to meet the immediate and the wider concerns of the Treasury.

Conclusions

The Chief Secretary thanked the Secretary of State for his offers. Officials would need to consider the package and its detail, not only to ensure full understanding of the composition of the new figures but also their wider consequences for the future.

HM TREASURY
Parliament Street
LONDON, SW1P 3AG

21st ~~1984~~ September 1984

Distribution: Those present

DEPARTMENT OF TRADE AND INDUSTRY BILATERAL

1. General

The Secretary of State said he understood the Chief Secretary's concerns, described in the bidding letter, and his Department would play its part in reducing public expenditure. However, the DTT's spending had declined substantially in recent years; further substantial reductions were impossible, and the present large additional bids were the inevitable results of past policy decisions. The Secretary of State provided several diagrams which showed the changing composition of DTT's programmes. He said that further substantial reductions would require the breaking of contractual commitments and renegeing on Manifesto commitments.

The Secretary of State made three particular points:

- (a) The Treasury preferred not to anticipate the provisions necessary for programmes like launch aid. Additional bids were therefore inevitable once decisions were taken.
- (b) Additional bids had been made for regional development grants but the scheme was shortly to be reviewed in EA Committee. It was however clear that the only way to contain spending in 1985-86 would be to institute a moratorium on regional grants, and he was prepared to face that solution.
- (c) He was totally unwilling to accept responsibility for the heavy anticipated expenditures to the privatised British Telecom in respect of Civil Defence.

2. TTC/FES

The Chief Secretary suggested that the facility should be withdrawn. The Secretary of State responded that it offered useful support for UK exporters tendering in foreign currency at modest cost. He proposed that it should be retained but in view of the heavy losses incurred since it was introduced that it should be transferred from ECGD's trading account to public expenditure. Mr Gill also referred to PAC criticism of the propriety of the facility's inclusion on the department's trading account. The Chief Secretary proposed that ECGD should continue to carry TTC/FES on the trading account for at least 1985-86 with the tacit understanding that if the facility was continuing to make heavy losses the department could re-submit its bid to transfer it to public expenditure from 1986-87. In exchange he was prepared to accept the retention of the mixed credits matching facility which involved similar levels of expenditure. The Secretary of State agreed.

3. Transfer of refinance

The Chief Secretary said he would like to take up the option of transferring further refinance to the banks, whilst acknowledging that the public expenditure savings achieved would be cosmetic. It was agreed that officials should take this forward.

4. Switch from US dollar to sterling finance

(i) The Chief Secretary said that because of the high cost of US dollars, the growth of US dollar fixed rate export finance should be discouraged by loading the fixed interest rate for dollar financing. The Secretary of State pointed out that the assumed consequent savings in interest support expenditure were based on current economic assumptions which forecast that dollar interest rates would continue to be significantly higher than those for sterling; the position might well reverse. The Chief

Secretary replied that if the relative sterling and dollar interest rates did not develop as forecast it would be possible instead to discourage the use of sterling finance. It was agreed that officials should continue the work already in hand on ways of discouraging the use of dollar financing, and should report back to Ministers in time for the next round of public expenditure discussions.

The Chief Secretary said that the Economic Secretary had recently written to the Minister for Trade about ECGD's liability to take out loans in US dollars. It was agreed that there should be further discussion between officials before any talks with the banks about implementing the removal of ECGD's take-out provisions from new lending in dollars. It might be necessary to bring the issue back to Ministers for decision. The Chief Secretary said that this could have implications for the volume of dollar finance, and asked that the matter be pursued quickly so that the consequent public expenditure implications could be assessed in time for the Autumn Statement.

5. Manpower and Running Costs

It was agreed that discussion of ECGD's manpower requirements and running costs should be deferred until final decisions on the Matthews Report had been taken.

28 SEP 1984

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5 6 7 8 9



DEPARTMENT OF TRADE AND INDUSTRY
 1-19 VICTORIA STREET
 LONDON SW1H 0ET 5422
 TELEPHONE DIRECT LINE 01-215
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Secretary of State for Trade and Industry

The Rt Hon Peter Rees QC MP
 Chief Secretary to the Treasury
 HM Treasury
 Parliament Street
 London SW1

CHIEF SECRETARIES	
13 SEP 1984	
Ms Conn	
PPS, FST, EST, MST	
Sir Peter Middleton	
Mr Bailey, Mr Byatt	
Mr Monck, Mr Lobell	

September 1984

Mr Scholar, Mr AW Russell
 Mr Bostock, Mr Gordon
 Mr Gray, Mr NJ King
 Mr RH Wilson, Mr Best
 Ms Low, Mr Yeo
 Mr Felstead, Mrs Gannon
 Mr Stuart, Mr Ridley, Mr Lord

R Peter.

PUBLIC EXPENDITURE SURVEY. DEPARTMENT OF TRADE AND INDUSTRY

Thank you for your letter of 14 September.

2 I am afraid that I do not regard your proposals as realistic. The savings you require for 1985/86 cannot be achieved even if we had a moratorium on all new SFI and Section 8 cases. As for the later years any substantial cuts would require both a moratorium now and a complete reversal of the policy set out in the Manifesto.

3 I do not believe you are giving credit for the savings I intend to make, let alone for the substantial revenue which my Department's work on privatisation will bring to the Exchequer. Let me set out how I see the position. The effect of the regional policy changes which I hope will be agreed at E(A), together with the moratorium, is to yield savings on what would otherwise have been counted against expenditure currently incurred by DTI of £123m in 1985/86, £117m in 1986/87 and £240m in 1987/88. I explained at our meeting on 5 September that I believed new money should be provided by the Treasury to cover the costs of the collective decision to offer Rolls Royce and British Aerospace launch aid. Nevertheless, you will see that these savings on what would have otherwise been spent on regional assistance more than cover for the cost of launch aid and make a significant saving below the Department's total baseline in 1987/88.

4 For the bids which I put forward as a consequence of reordering of priorities, I had already offered direct offsetting savings. The only remaining bids are those for steel and shipbuilding, which I cannot avoid. These are partly covered by the balance of savings on regional policy. The other savings I volunteered on 5 September would more than make up the difference.

5 I would hope that our resumed discussions can be based on what is practicable and realistic, and I believe you will then find that I have already gone to the limit in endeavouring to help you.

Norman Tebbit

NORMAN TEBBIT

JH3AXX



Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Norman Tebbit MP
 Secretary of State for Trade and Industry
 Department of Trade and Industry
 1 Victoria Street
 London SW1 6RB

14 September 1984

Stan Norman

**PUBLIC EXPENDITURE SURVEY:
 DEPARTMENT OF TRADE AND INDUSTRY**

I gather our offices have agreed a time on 25 September for us to continue our discussion of your Departmental Public Expenditure programme. I hope you will find it helpful in advance of that if I set out the position we reached on 5 September and the difference between us.

2 Taking your programme as a whole, including regional policy, you proposed a net change on the baseline of:

1985-86	1986-87	1987-88
+ £100m	+ £150m	-£50m

While we need to keep track of both elements of the programme, I am sure we need for operational reasons to disentangle the expenditure on regional assistance, which we shall be considering in E(A), and the rest of your programme on which we have to try to reach a bilateral agreement.

3 On the regional side, I was most grateful for your agreement at the meeting that there should be a moratorium on regional development grants in 1985-86. While that does worsen our problem in the later years, it is an essential contribution to reducing expenditure in 1985-86. However, taking that with the changes to regional policy that you were envisaging on 5 September, the net change from the baseline for regional policy would, I understand, be as follows:

	1985-86	1986-87	1987-88
DIT programmes	-15	+40	-71
GB as a whole	- 5	+64	-48

As you will know that still falls some way short of the savings Nigel and I are seeking. I understand that officials will report very shortly on a number of options for the future of regional policy and we will obviously have to take the issues forward in E(A).

4 Your proposals on the rest of your programme are summarized in Annex A.

5 Compared with your original bid for:

+166m +£167m +£62m

your proposals produce a net increase from your baseline for non-regional expenditure of:

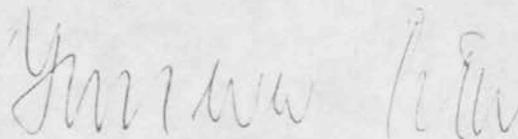
+£115m +£110m +£21m

Almost half of the difference between these two is of course the result of my agreement that your additional bid for Civil Defence, and Assistance to the Steel Industry (for the later 2 years only), could be set on one side. In effect, therefore, you have reduced your demands for extra provision by only

-£27m -£29m -£15m

6 I fully understand the difficulties you would face in going beyond that and I would not press it on you if I could find more palatable ways of achieving the objectives agreed by Cabinet. But we face much greater difficulty this year than last in holding to our plans. We have already agreed an increase of some £1 billion for local authority current provision. Our EC contribution seems set to be around £300 million higher than provided for. The increase in interest rates has boosted, for example, ECGD's requirements by a further £300 million. Then there are the pressures on the social security front - where we face bids of £ billions. And all that is before we begin to consider the various policy bids that colleagues have put forward, all of which no doubt are highly desirable in their own terms.

7 In these circumstances, we must look not only for savings in regional policy of the order we have proposed but also for substantial savings on your discretionary grants and other support for private industry. Painful though it will be to make such reductions, they will be very much in line with our general economic and industrial policy. We have always been suspicious of the value for money of Government intervention in this field, a suspicion that the Prime Minister reiterated in the Summer. I must, therefore, look to you for the kind of overall savings that I proposed in my letter of 2 August. To help negotiations I am willing to reduce my initial bid to match the savings you have offered but, as Annex B shows, I must still press you for a significant net reduction from your baseline in the first two years and a large reduction in the final year.



PETER REES

Position at meeting on 5 September 1984

ADDITIONAL BIDS		£ million		
		85-86	86-87	87-88
Selective Assistance to individual industries	not agreed	+11.0	+17.0	+20.0
General industrial R&D	not agreed	+ 2.0	+ 7.0	+ 4.0
Regulation of domestic trade and consumer protection	not agreed	+ 0.0	+ 0.8	0.0
Finance for Rolls Royce Ltd	agreed	+28.5	+21.8	0.0
Other aircraft & aeroengine projects	agreed	+ 73.1	+ 80.7	+ 22.3
Refinancing of home ship-building lending	agreed	+ 4.0	+ 3.0	+ 5.6
Interest support costs	agreed	+ 24.5	+ 27.7	+ 19.7
Assistance to the shipbuilding industry	agreed	+ 5.1	+ 4.0	0.0
Assistance to the steel industry	agreed in part	+4.8	-	-
Other central & miscellaneous services	agreed	+1.0	-	-
Civil Defence	withdrawn	-	-	-
Support for films	agreed in part	+1.5	+1.5	+1.5
Total excluding RDG's		+156	+164	+73

SUMMARY OF DTI POSITION

Reduced requirements		-14	-25	-37
Additional bids		+156	+164	+73
Further savings		-27	-29	-15
TOTAL	Signature	+115	+110	+21

Suzzy called:
you don't need
to worry about
the statement. 😊

Position at meeting on 5 September 1984

ADDITIONAL BIDS		<u>£ million</u>		
		85-86	86-87	87-88
Selective Assistance to individual industries	not agreed	+11.0	+17.0	+20.0
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Other central & miscellaneous services	agreed	+1.0	-	-
Civil Defence	withdrawn	-	-	-
Support for films	agreed in part	+1.5	+1.5	+1.5
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SUMMARY OF DTI POSITION

Reduced requirements		-14	-25	-37
Additional bids		+156	+164	+73
Further savings		-27	-29	-15
Net change from baseline excluding regional expenditure charges.	TOTAL	+115	+110	+21

£ million

	1985-86	1986-87	1987-88
1. <u>DTI proposals at bilateral</u> (incl. regional expenditure)	+100	+150	-50
<hr/>			
2. <u>DTI position</u> (excl. regional expenditure changes)			
Original proposal	+166	+167	+62
Proposals at bilateral (see Annex A)	+115	+110	+21
Difference	51	57	41
<hr/>			
Comprising:			
Bids set to one side (Civil Defence & Steel)	(24)	(28)	(26)
Savings offered	(27)	(29)	(15)
<hr/>			
3. <u>CST's revised options for reductions</u>			
Original options	-166	-180	-255
*CST's concession	+27	+29	+15
Reductions still required	-139	-151	-240
<hr/>			
<u>Contribution</u>			
DTI savings offered	-27	-29	-15
Other savings required	-112	-122	-225
<hr/>			
4. <u>Net change to DTI's baseline</u>			
DTI reduced requirements	-14	-25	-37
Additional bids conceded	+143	+139	+49
CST's revised options for reductions	-139	-151	-240
Net change	-10	-37	-228

*equivalent to DTI savings offered

CONFIDENTIAL

cc:PPS



FST
EST
MST
Sir P Middleton
Mr Bailey
Mr Monck
Mr Scholar
Mr P Gray

Treasury Chambers, Parliament Street, SW1P 3AG

Mr Lovell
Ms Conn
Mr Ridley
Mr Lord

Rt Hon Norman Tebbit MP
Secretary of State
Department of Trade and Industry
1 Victoria Street
London SW1

27 September 1984

Norman Tebbit

PES 1984 - DEPARTMENT OF TRADE AND INDUSTRY

At the conclusion of our short discussion on 25 September on your PES programmes I said I would let you have a letter setting out my understanding of our respective positions. This should help to focus any further discussions on the ... main issues. The figures are set out in Annex A attached to this letter.

2 I accept, of course, that we need to take account of both regional and other industrial expenditure. As a matter of procedure, however, we have to discuss regional policy throughout Great Britain at E(A) next week while we have to settle on the rest of your budget through the normal Survey process.

3 I very much welcome the direction of your proposals on regional policy and your agreement to a moratorium on RDGs in 1985-86. Even so the framework you are proposing produces smaller savings in the later years than Nigel and I will propose to E(A).

4 However, even if we achieved all we are asking in the regional policy field, we would still need to secure substantial savings on the rest of your budget in order to hold to the expenditure totals agreed by Cabinet.

CONFIDENTIAL

5 In the light of your comments on the practicability of my earlier proposals I have reconsidered what would be possible. I had hoped to explore this with you at our meeting on the basis of the latest figures for "committed" expenditure which your officials gave to mine on Monday. I quite understand why you decided that it was not worth crawling over the figures. I am attaching them to this ...letter (Annex B) so that you can see the basis on which I am making my specific proposals.

6 I accept that the scale of reductions I first proposed for 1985-86 cannot be regarded as practicable. I still think however that there is some room for cutting back here and there. Clearly you will be the best judge of where this is feasible, but I understand that the character of "commitment" in respect of expenditure for aircraft and aero-engine general R & D is much less contractually based than some of the other expenditure. I would have thought that the spend on this item offers considerable scope for reduction. It may be too that there is some scope for increasing revenue in 1985-86 by increasing the charges for the services provided in the promotion of exports and tourism. With these factors in mind, and taking account of the savings you have already offered for 1985-86, I am prepared to reduce substantially my bid for that year from a reduction of £139 million to a reduction of £20 million. I accept that even this much reduced proposal will be difficult for you, but I believe that it is practicable and realistic and it would be a welcome contribution to easing our general financial problems next year.

7 In the next two years the level of commitments falls quite substantially: in 1986-87 uncommitted spending on the selected items totals £243 million, and in 1987-88 it rises to £370 million. I am proposing therefore, much more substantial savings in these years. They would imply cutting back on grant giving programmes, but I suggest they should also include introducing or raising charges.

8 I accept, of course, that savings of this order imply a significant shift in policy. But a shift away from discretionary subsidies and towards reducing distortions in the market seems very much in line with our determination to improve the use of our resources and wider economic strategy. Similarly it seems entirely consistent with our wider approach that we should charge companies for the services Government provides. This allows competition with the private sector and gives an indication of the value of the service.

9 Naturally I would be happy to discuss these proposals with you should you think it worthwhile.



PETER REES

ANNEX A

<u>DTI position</u>	£m		
	1985-86	1986-87	1987-88
Reduced requirements	-14	-25	-37
Further savings made in bilateral	-27	-29	-15
Bids conceded by CST	143	139	49
Bids not conceded by CST	<u>13</u>	<u>25</u>	<u>24</u>
Net change from baseline excluding regional expenditure changes	<u>115</u>	<u>110</u>	<u>21</u>
 <u>CST position</u>			
Reductions in programmes or increased charges	-20	-122	-225
Bids not conceded	<u>-13</u>	<u>-25</u>	<u>-24</u>
	<u>-33</u>	<u>-147</u>	<u>-249</u>
CST net change from baseline excluding regional expenditure changes	<u>82</u>	<u>-37</u>	<u>-228</u>

744
 348

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GRANT GIVING SUB-PROGRAMMES WHERE REDUCTIONS ARE BEING SOUGHT: BASELINE AND COMMITMENTS

	£ million			
	1985-86 in June 1984	1985-86 in Sept 1984	1986-87	1987-88
1. Selective Assistance to Individual Industries				
- Baseline	94.7	94.7	80.9	82.9
- Commitments	81.7	91.8	59.9	43.9
- Committed: (%) of Baseline	(86)	(97)	(74)	(53)
2. General Industrial R & D				
- Baseline	295.3	295.3	304.4	312.0
- Commitments	225.3	279.2	136.0	45.0
- Committed: (%) of Baseline	(76)	(95)	(45)	(15)
3. Aircraft & Aeroengine General R & D				
- Baseline	35.4	35.4	36.3	37.2
- Commitments	3.4	35.7	3.3	4.2
- Committed: (%) of Baseline	(10)	(100)	(9)	(11)
4. Space				
- Baseline	67.7	67.7	69.0	70.7
- Commitments	68.5	67.1	49.0	40.6
- Committed: (%) of Baseline	(101)	(99)	(71)	(57)
5. Future Industrial Support				
- Baseline	2.7	2.7	1.0	1.0
- Commitments	0	0	0	0
- Committed: (%) of Baseline	-	-	-	-
6. Total - Baseline	488.8	495.8	491.6	503.8
- Commitments	378.9	473.8	248.2	133.7
- Uncommitted	109.9	22.0	243.4	370.1
- Committed (%) of Baseline	(77)	(96)	(50)	(27)

1984 PUBLIC EXPENDITURE SURVEY: DEFENCE

Note of a meeting held in HM Treasury at 9.00am on Friday 28 September 1984

Those present:	<u>HMT</u>	<u>MOD</u>
	Chief Secretary	Secretary of State for Defence
	Mr P J Kitcatt	Sir Clive Whitmore
	Mr M Scholar	Mr N Bevan
	Mr I P Wilson	
	Mr F Martin	
	Mr R Broadbent	
	Mr A N Ridley	

The Chief Secretary suggested that the agenda should be that proposed in his letter of 2 August, using the table attached to that letter.

Efficiency Savings

2. The Chief Secretary invited the Secretary of State's views on the efficiency savings suggested in his 2 August letter. The Secretary of State replied that the savings requested for 1987-88 were not credible either in terms of domestic politics or vis-a-vis NATO, particularly against the background of US Government and Congressional pressure, exemplified in the Nunn/Cohen amendment. In combination with the rejection of his additional bids for inflation adjustment in 1987-88 and for 2% growth in that year, the proposed efficiency reductions would mean a reduction in provision for the defence programme of the order of 4 per cent. He was willing to defend, against House of Commons Defence Committee and other criticism, the present standstill in provision for 1986-77. But he could not defend a substantial reduction in programme provision in the subsequent year. The issue was thus essentially one of principle.

Falklands Provision for 1987-88

3. The Chief Secretary asked whether it would be possible to reduce the bid of £300 million for Falklands provision in 1987-88. The Secretary of State reminded the Chief Secretary of the existing agreement that Falklands costs would be met as an addition to the defence programme and emphasised that the figure was realistic and designed only to meet expected Falklands expenditure. He was, however, happy for Treasury and MOD officials to examine the figure further to

/ see

see if there was any scope for savings at the margin, and he would also be willing to review the figure subsequently should revised planning assumptions about the level of Falklands forces be agreed. On that basis the Chief Secretary indicated that he was willing to accept the bid.

Inflation Adjustment for 1985-86

4. The Chief Secretary also indicated that he was willing to accept in principle the bid for inflation adjustment in 1985-86, subject to the examination by officials of the appropriate figure in the light of the latest inflation forecast. The Secretary of State welcomed this agreement. It was pointed out that, if Cabinet agreed the Chief Secretary's proposal for a 3% pay assumption for 1985-86, this would reduce the baseline for the calculation of the bid. It was agreed that the bid should be calculated after taking account of clawback for the pay assumption.

Additional VAT Payments

5. The Chief Secretary recognised that there was an element of rough justice in asking departments to absorb the increased cost of the Budget change in VAT on building alterations. With the exception of one small concession for church-maintained schools, other departments were absorbing this additional cost and the Chief Secretary hoped that MOD would be willing to do likewise. The Secretary of State said that in these circumstances he would be willing to absorb the additional costs. He further explained that one component of the additional bid related to research and development work now contracted out to the Royal Ordnance Factories. He hoped that it would be possible for this to be refunded under the mechanism provided by Section 11 of the Finance Act 1984, and the Chief Secretary agreed that the Treasury would examine this possibility.

Extra Cost of Review Body Awards

6. The Secretary of State explained that he attached importance to this bid. The sum represented nearly 1% of the defence budget, and additional cash had been made available in past years to meet the real terms growth commitment. The Chief Secretary pointed out that no such adjustment had been made in the 1983 Survey, and that, given his acceptance of the bid for inflation compensation in 1985-86, additional cash for the pay awards was not necessary to met the 3%

/ real

3% real growth objective. To accept both bids would in effect mean double-counting. Moreover, there was no Manifesto or other public commitment to provide extra cash to meet the costs of such awards, which were no different from any other price change. Since the defence provision after 1985-86 had been agreed in the 1983 Survey on a strictly cash basis, the presumption must be that all price changes would be absorbed. However, the Secretary of State suggested that the terms of the 1983 Survey agreement were that the cash provision for defence would be increased sufficient to meet the "real requirement": increased cash to offset the cost of the pay awards was necessary to maintain the real value of the defence budget. The Chief Secretary pointed out that this argument could not be applied to the years after 1985-86. Moreover, the question of efficiency savings was also relevant in this context: these would enable the "real requirement" to be met without additional cash inputs. He hoped therefore that the Secretary of State would be willing to drop this additional bid.

Inflation Compensation and Real Growth in 1987-88

7. The Secretary of State said that he might be prepared to drop for the present the bid for additional cash in 1987-88 with respect to inflation compensation, provided there was an agreement, similar to that in the 1983 Survey, which would enable future adjustment of the baseline in the light of any changes in inflation assumptions. The Chief Secretary asked what would be the position on the bid for 2% growth in 1987-88 in those circumstances. The Secretary of State acknowledged that there was no commitment to real growth after 1985-86, although there would, he suggested, be very great pressure to achieve some growth. He would not insist on pressing the bid this year, provided that the cash provision for 1987-88 was arrived at on a realistic basis. That in turn would require that the request for efficiency reductions in the baseline should be dropped. It was the Secretary of State's aim to achieve efficiency savings: he needed them to defend the standstill in cash provision for 1986-87 and to accommodate the effects, for example, of sterling depreciation on such things as Trident costs. But he could not motivate his department to achieve such savings if the cash was simply lost to the Treasury. The Chief Secretary pointed out that the efficiency reductions he was asking for built up at a rate of only 1% a year; the department had

/ had

had the benefit of previous efficiency improvements and, in the light of the overall objectives for public expenditure agreed by Cabinet, it was not unreasonable to ask that these benefits should now be shared.

Manpower

8. The Chief Secretary asked whether, in the light of the position outlined in the Secretary of State's letter of 25 June, he was able to offer a firm figure for reductions by 1 April 1988. The Secretary of State emphasised his support for civil service manpower reductions: indeed his concern was that across the board the Government was not doing enough. He was planning substantial reductions below his present manpower baseline: over recent months savings had been identified which would enable the Department to reduce its total to 174,700 by 1 April 1985, and he would have no difficulty at all in achieving a figure well below 170,000 by 1 April 1988. Indeed, he was hoping to achieve reductions of over 4% a year. However, he was unwilling to offer firm figures at this stage. He feared that if he did so, it would simply remove the pressure on other departments to find their proper share of the overall target. The Chief Secretary emphasised that he would not allow that outcome: at the same time it was very difficult for him to press other colleagues for savings if he could not show that the Ministry of Defence was making its contribution.

9. The Secretary of State indicated that he might be willing to provide firm figures for manpower reductions provided there could be some accommodation on his additional bids with respect to inflation compensation in 1987-88 and the extra cost of Review Body awards. The Chief Secretary noted the proposition, but feared that the expenditure totals implied could not be reconciled with the overall objectives agreed by Cabinet on 5 July. He would like to reach an accommodation and would write to the Secretary of State setting out the areas of disagreement and those of potential agreement. The Secretary of State welcomed this, and hoped that it might be possible for the Chief Secretary to propose a quantified package.

cc. Those Present

PPS

Mr Bailey

Mr Gray

Mr Lord

ESTIMATES 1984' = CMND 9227

lead to an annual saving of £2 million in 1983/84 and subsequent years.

CIVILIAN MANPOWER

230. Reduction in the number of civilians employed by the MOD has been a continual process since the unified Department was created in 1964, as the graph at Figure 5 shows. The number of UK-based civilians in the Department has been reduced by 47,700 to 200,000 between 1979 and 1 April 1984, a reduction of nearly 20%. The Ministry of Defence, which comprises one-third of the Civil Service, has contributed nearly one-half of the total Civil Service reductions over this period. Numbers of locally-engaged civilians serving overseas have fallen by 4,700, a reduction of over 12%. The majority of reductions have been achieved without recourse to redundancies, by improving efficiency, general streamlining, privatisation (including contracting-out) and dropping or curtailing functions.

231. Some examples of savings measures already achieved or in hand are as follows:

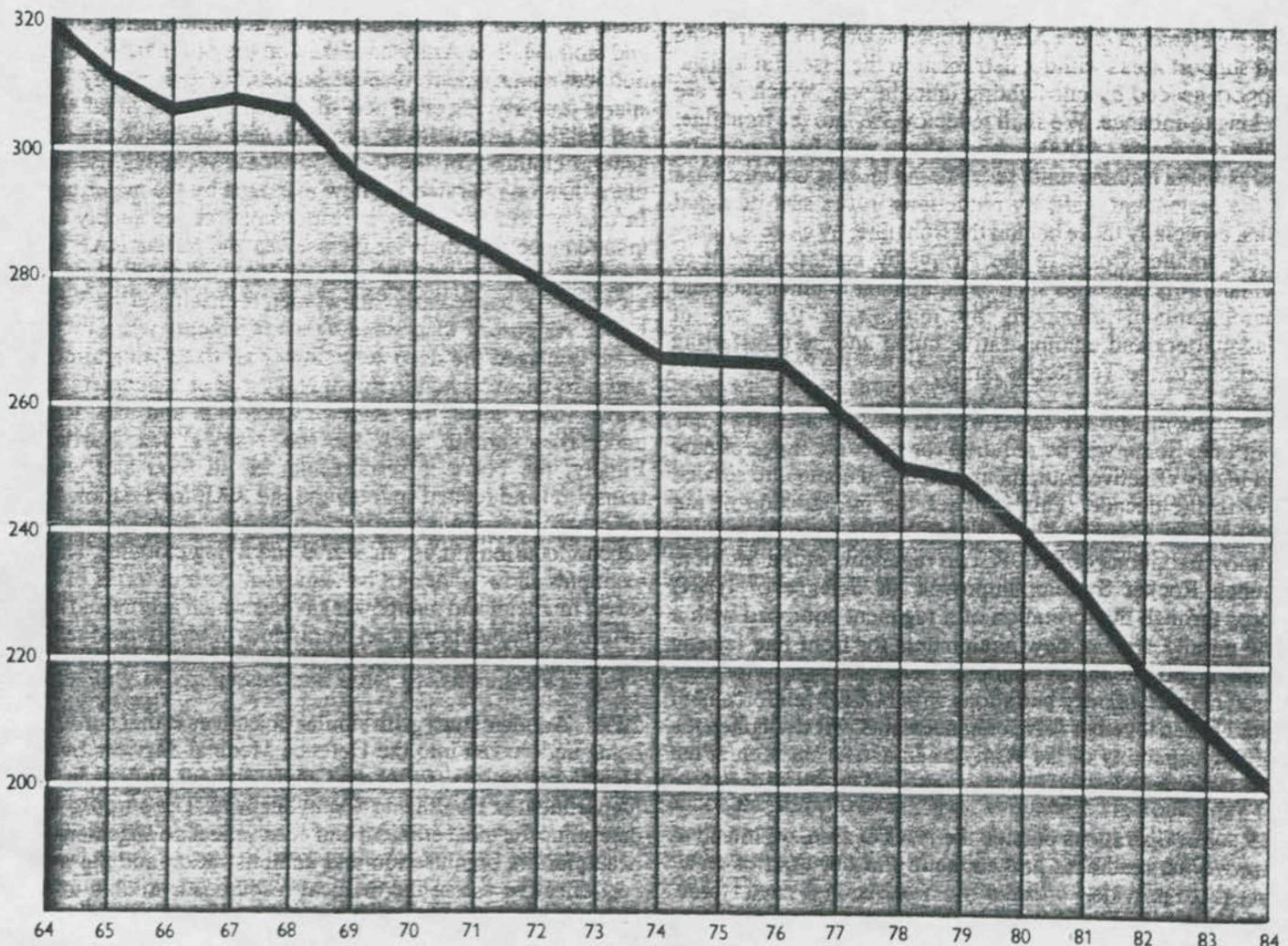
- contracting-out of cleaning and catering at Ministry of Defence establishments is now producing an annual saving of £12 million.
- the introduction of a comprehensive Royal Navy stores inventory system in 1983 should

- the use of improved computer technology in Service pay systems should lead to staff savings amounting to £11 million a year.

232. A whole range of studies and re-organisation now in hand will ensure that the momentum is maintained. For example, a restructuring of the Quality Assurance area of the Procurement Executive, taken together with the increasing development of quality control by defence contractors themselves, will enable the number of personnel employed on these tasks to be reduced substantially.

233. The Department's forward plans, taking account of the privatisation of the Royal Ordnance Factories which will transfer some 18,500 posts outside the Civil Service, assume a total civilian manpower provision of not more than 179,000 by the end of the 1984/85 financial year and not more than 170,000 by 1 April 1988, in line with the Government's target for the Civil Service as a whole. The aim will be to achieve a rate of rundown which significantly betters this target.

Figure 5 The Reduction in Ministry of Defence Civilian Manpower 1964-84

**Note:**

All years have been broadly adjusted to reflect changes in Government Departmental organisation which have affected the Ministry of Defence.



u MASTER SET

10 DOWNING STREET

From the Private Secretary

28 September 1984

Dea Dano.

PUBLIC EXPENDITURE

The following action points emerged from the discussion the Chancellor and the Chief Secretary had with the Prime Minister this afternoon.

- (i) The Treasury would prepare a speaking note for the Prime Minister to use at Cabinet on Thursday. This would have three elements: first, the Prime Minister would tell colleagues that, having rejected the Chief Secretary's proposal for a moratorium on local authority capital expenditure, they should do everything within their power to minimise expenditure in 1984-5. They should go through their programmes carefully to see what savings could be made. This would represent, in effect, an appeal to colleagues to do what they could on a voluntary basis. Secondly, the Prime Minister should warn colleagues that the future position on public expenditure was extremely difficult and that they should exercise great care in responding to Conference motions. No commitments to future expenditure should be given, nor should hopes be raised. Finally, there should be notes on what the French and other Governments were doing to restrain public expenditure. These should arrive by Wednesday evening.
- (ii) It was agreed that a special effort should be made to settle Mr. Tebbit's programme early to enable him to take his place as a member of the Star Chamber. A meeting has been arranged after E(NI) on Wednesday between the Prime Minister, Mr. Tebbit, the Chancellor and the Chief Secretary. The Chief Secretary's office have already sent over some of the papers relating to the bilateral. The Treasury should prepare a specific brief on the line to take, to reach here by close of play on Tuesday.

(iii) The Prime Minister wondered whether it was right to make the Autumn Statement on 13 November when this was the final day of the debate on The Queen's Speech. The Treasury should investigate the precedents for making a major economic announcement on the same day as the Economic Debate and should consult the Chief Whip about the likely reaction of the Opposition. The Chancellor should minute the Prime Minister on the outcome of these investigations.

BH
I am sending a copy of this letter to Richard Broadbent (HM Treasury).

*Yours sincerely
Andrew*

(ANDREW TURNBULL)

David Peretz, Esq.,
HM Treasury.

file JR



10 DOWNING STREET

From the Private Secretary

28 September 1984

Dear Richard,

PUBLIC SERVICE PAY AND EXPENDITURE IN 1985-6

The Prime Minister is content for the Chief Secretary to circulate the paper attached to Paul Pegler's letter to me of 27 September. She agrees that the pay assumption for 1985-6 should be set at 3 per cent.

*Yours sincerely
Andrew Turnbull*

(ANDREW TURNBULL)

Richard Broadbent, Esq.,
HM Treasury.

JR



Prime Minister ①

Agree I let RTA know that you are hoping to "dear" Mr Tebbit so that he can join the group? *Yes*

Agree RTA to approach members informally before Thursday? *Yes*

AT 28/9 *Yes*

Ref. A084/2599

PRIME MINISTER

Public Expenditure Survey 1984: Small Ministerial Group

You indicated to the Cabinet on 5 July (CC(84) 25th Conclusions, Minute 5) that it was probable that you would establish a small Ministerial 'Star Chamber' Group, like MISC 99 last year, to consider and make recommendations to the Cabinet on expenditure programmes which cannot be agreed bilaterally between the relevant spending Ministers and the Chief Secretary, Treasury. As I reported to you in my minute of 24 September, both the number of such programmes and the issues at stake are likely to be greater than last year. We shall therefore need to set up a Ministerial Group. This minute seeks your instructions on the membership.

in Pt 27

2. The membership of MISC 99 was as follows:

- Lord President of the Council (Chairman) ✓
- Secretary of State for Scotland ✓
- Lord Privy Seal ✓
- Secretary of State for Trade and Industry
- Chancellor of the Duchy of Lancaster (Lord Cockfield)
- Chief Secretary, Treasury

*assuming he has reached agreement *not**

Non-departmental Ministers

3. I take it that you will wish the Lord President of the Council to be Chairman, as you indicated to the Cabinet on 5 July; and that you will also wish the Lord Privy Seal to be a member.

Yes
Yes

4. The other non-departmental members of the Cabinet are the Chancellor of the Duchy of Lancaster and the Minister without Portfolio. On the whole, my feeling is that they have been too recently appointed to the Cabinet for it to be appropriate to invite them to be members of the Group this year. Moreover, such groups generally work more effectively if the number of their members is kept small.



Departmental Ministers

5. Among departmental Ministers I would suggest:

Agreed
The Home Secretary: I understand that he is very near agreement bilaterally with the Chief Secretary; and that even if complete agreement is not reached the sums at issue are small; and

Agreed
The Secretary of State for Scotland: unlike last year, there may be an issue between him and the Chief Secretary about the application of the so-called Goschen formula (which relates expenditure under the control of the Secretary of State to expenditure on corresponding English programmes); but I do not think that this is a serious objection to his being a member of the Group.

6. I understand that there are substantial differences between the Secretary of State for Trade and Industry and the Chief Secretary, particularly regarding 1986-87 and 1987-88; and that it is unlikely that agreement will be reached bilaterally. This is not a conclusive objection to membership: it would be possible for the Secretary of State to 'cross the floor' when his programmes were discussed by the Group. Nevertheless, it seems to me that it would be difficult for the Group to be accepted as impartial by other spending Ministers if he were a member.

Recommendation

7. I therefore recommend the following membership:

Lord President of the Council (Chairman)

Home Secretary

Secretary of State for Scotland

Lord Privy Seal

Chief Secretary, Treasury

with DTI, agreement has been reached
As last year, the Group would be known as the Ministerial Group on Public Expenditure.

8. The natural occasion for you to tell your colleagues of the establishment of the Group would be at the meeting of the

CONFIDENTIAL



Cabinet on Thursday 4 October. I should, however, be grateful for your authority informally to approach the Chairman and members of the Group before then. This would enable preparations to be put in hand for the Group to begin work on 15 October, immediately after the Party Conference.

RA

ROBERT ARMSTRONG

28 September 1984

CONQUEROR

CONFIDENTIAL

CONFIDENTIAL

27 September 1984

MR TURNBULL

THE PAY FACTOR FOR NEXT YEAR

We support the Chief Secretary's proposal for a 3 per cent increase in the public service pay bill next year. A pay factor of 4 per cent was assumed when originally setting the expenditure plans for 1985-86. Cutting it to 3 per cent saves around £200 million.

There is one trick to look out for. Spending Ministers may argue that these are just crude across-the-board cuts and should count towards the cuts they are negotiating individually with the Chief Secretary. The Treasury want these savings on top of those they are negotiating bilaterally with departments. Spending Ministers must not be allowed to win the argument - the public spending position is too serious.

David Willetts

DAVID WILLETTS

CONFIDENTIAL

PRIME MINISTER

MEETING WITH THE CHANCELLOR AND CHIEF SECRETARY

(i) Public Expenditure in 1984/85

When Cabinet colleagues declined to support a moratorium on local government capital expenditure, the Chief Secretary was given leave to bring forward other proposals which would eliminate the overshoot in 1984/85. He has considered the possibilities but, apart from some limited savings and increased asset sales he has not identified any that colleagues would be likely to accept. He is therefore recommending that the Government acquiesce in a substantial overspend this year. If this is to be accepted, a special effort will be needed to explain it.

(ii) Public Expenditure Survey

The Chief Secretary has reported on the state of play following his bilaterals. He has made little progress and a great deal remains to be done. At the same time there are the difficulties of scheduling on which Sir Robert Armstrong has already reported to you.

The Chief Secretary recommends bringing forward the Economic Cabinet to next Thursday so that Lord Whitelaw's group can make an early start. You will need to discuss with him and the Chancellor the composition of the group. Mr. Tebbit is likely to be still in dispute and may therefore be disqualified. This would leave the choice between Minister without Portfolio, Chancellor of the Duchy, Lord Privy Seal, Home Secretary and Secretary of State for Scotland. The Chief Secretary seeks your approval to the circulation of a Cabinet paper. You will also want to go over with him and the Chancellor some of the very difficult options which will

need to be pursued.

(iii) Pay Factor

The Chief Secretary has circulated a note recommending that the pay factor for 1985/86 be reduced from 4 per cent to 3 per cent. This would save £200 million provided Ministers are not allowed to count the saving in their bilaterals.

The Chief Secretary can leave at this point. He is anxious to get back to his constituency.

(iv) Washington meetings

The Chancellor can report on these, in particular Argentina's agreement with the IMF.

(v) VAT on food

I understand you were unhappy about the terms of a letter drafted by the Treasury. There has been some correspondence between Mr. Jopling and the Chancellor on this. Part of the difficulty stems from the fact that the Treasury presentation begins by repeating your undertaking and then adds the caveat about the tax system not being immutable. This tends to undermine the undertaking. In my view it would be better if they reversed the sequence. The Treasury are of course, anxious to retain some flexibility at the margins of what is defined as food.

AT

27 September, 1984

Prime Minister

Content for CST to circulate the paper attached 24 hours before Cabinet meeting?



FROM; CHIEF SECRETARY
DATE: 27 September 1984

AT
28/9

3

o27/109

PRIME MINISTER

PUBLIC EXPENDITURE SURVEY

After paper to be circulated (not this minute) to Chief Minister only under the secret procedure ref.

You will want to know how the Public Expenditure Survey is going, and to have my assessment of the next steps.

2 As we expected, this year's Survey is proving particularly difficult. Given the range of unavoidable additional bids - local authority current expenditure alone accounts for £1 billion a year - sticking to the agreed public expenditure totals requires sizeable cuts in a number of areas. Hence I am having to press colleagues to make policy changes they regard as deeply unwelcome.

3 I attach tables showing for each year colleagues' original bids and current positions and the figures I have proposed. The Autumn forecast may affect some of the figures; and we cannot yet make a realistic estimate of the net cost of the miner's strike in future years. As they stand I have some negotiating margin, but I need to obtain in 1985-86 about half of what I am asking, even taking into account an increase of £500 million in the forecast proceeds from special sales of assets (not yet reflected in the tables).

4 To close the gap will require a very rigorous approach on all programmes, involving, in particular, substantial reductions in industrial and agricultural support, a rise in NHS charges (but retaining the present exemptions) and a range of savings in social security involving secondary legislation. I should be able to secure some of these savings bilaterally but some, for example industry and agriculture, seem bound to go to the Star Chamber.

Lord Whitehead's Group.

5 Even with these savings there is likely to remain a gap in 1985-86 of around £1 billion which can only be closed in my view by some or all of the following (each of which might produce savings of around £500m in 1985-86):

- a) substantial reductions in the housing programme;
- b) cost savings and some real prices increases in the energy and water industries;
- c) additional savings on social security ~~which would almost certainly require an adjustment to the uprating.~~

6 Our latest estimates of asset sales do not help us for 1986-87 and 1987-88 so the position there is correspondingly tighter. To reach our targets we will need to secure savings in all the areas listed in paras. 4 and 5 and, in addition, make real terms reductions for defence in both years. The difficulties we face this year, as last, reflect in large part the constant increases in social security and that illustrates the need for substantial savings following current reviews.

7 Given the difficulties, the Chancellor and I have therefore been thinking further about the very tight timetable up to the Autumn Statement and BT Impact Day that you saw at the beginning of August.

8 To give Lord Whitelaw's group time to address itself to these very difficult issues, it should, clearly, begin work as soon as possible. Although it would not, I think, make sense to bring forward its starting date from the date we originally identified - 15 October, straight after the Party Conference - we ought to do all we can to make sure it can get down to business properly on the 15th.

SECRET AND PERSONAL

9 On reflection, the Chancellor and I think that it would be better to avoid a Cabinet discussion on public expenditure and the economy on Thursday 18 October, lest it overhang the deliberations of the MISC group earlier in the week. Our preference would be to have this discussion at the 4 October Cabinet (when it is already planned to discuss the question of a pay factor for 1985-86), so that colleagues could have brought home to them the seriousness of the public expenditure prospect, before the MISC group goes into action.

10 The Treasury Autumn forecast will not be complete by then, but enough work will have been done to enable the Chancellor to discuss the current economic prospect as the context for the work of Lord Whitelaw's group. I attach a draft Cabinet paper which could either be circulated just before the meeting, or, if you prefer, handed out and collected up at the Cabinet meeting itself.

11 We shall lose time if the MISC group's papers are not prepared in good time. I hope you will agree to the circulation of some of them - on a highly restricted basis - enough ahead of 15 October to allow the members of the MISC group time to consider them - i.e. in the week beginning 8 October (which is, of course, Party Conference week).

12 As in earlier years, some of the issues we face are unlikely, in my judgement, to be capable of resolution outside meetings under your chairmanship (such as defence, energy prices, social security).

SECRET AND PERSONAL

SECRET AND PERSONAL

13 You may want to discuss the overall position with us early next week. Another issue we might discuss is the membership of the MISC group.

14 I would be grateful to know if you agree with these further thoughts about the timetable; and if you are content with the draft Cabinet paper, whether for circulation 24 hours before next Thursday's Cabinet, or for handing round at the meeting.

15 I am copying this minute to Sir Robert Armstrong.



PETER REES

SECRET AND PERSONAL

1985-86 £m

Department	Baseline	Opening Position		Changes from Baseline	
		Minister	CS1	Minister	CS1
Defence	18,003.0	219.6	43.0	323.6	147.0
FCO-ODA	1,264.0	10.9	-60.5	10.9	-60.5
FCO-other	602.0	46.3	-14.4	46.3	-14.4
EC*	550.0	205.0	205.0	205.0	205.0
IBAP (and prefunded AFF)*	1,304.0	-29.3	-33.3	44.7	44.7
AFF (domestic)	776.0	14.9	-177.4	-1.1	-161.9
Forestry*	56.0	-1.1	-9.1	-3.5	-3.5
Regional Policy (GB)	491.0	108.0	-40.0	-5.0	-40.0
DTI (other)	782.0	166.0	-45.0	112.0	80.0
ECGD	30.0	291.4	206.4	209.5	208.1
Energy	321.0	7.6	-39.6	-7.1	-39.6
Employment	3,158.0	136.4	-327.2	-32.0	-149.0
Transport	2,176.0	51.0	-124.0	-121.0	-292.0
Housing	2,507.0	53.0	-685.0	53.0	-747.0
PSA	-109.0	55.3	0.0	44.5	10.0
DOE other (inc Urban)	931.0	44.1	-173.0	44.1	-78.0
Ordnance Survey*	18.0	2.1	-1.7	-0.2	-0.2
Home Office	1,023.0	49.2	-28.3	2.2	-23.0
LCD	547.0	0.0	-11.6	0.0	-10.0
DES	3,353.0	117.1	-143.0	-4.2	-126.5
OAL	287.0	8.4	-8.6	8.4	-5.0
Health + PSS	13,954.0	476.5	-17.0	297.7	0.0
Social Security	39,410.0	757.0	0.0	532.0	0.0
Superannuation*	1,130.0	-58.5	-58.5	-58.5	-58.5
Scotland	3,904.0	36.1	32.1	36.1	32.1
Wales	1,521.0	13.5	-13.5	7.7	-13.5
N. Ireland	4,213.0	45.6	26.6	45.6	26.6
Inland Revenue	949.0	8.1	0.0	8.1	0.0
CEx Other Depts	853.0	3.6	-32.0	3.6	-32.0
Other Depts.	319.0	20.0	-5.7	20.0	-5.7
LA current*	24,754.0	944.0	944.0	944.0	944.0
NI EFLs (inc RMPS)	1,332.0	-250.0	-250.0	-250.0	-250.0
Reserve*	3,750.0	-750.0	-750.0	-750.0	-750.0
Pay Factor	0.0	0.0	-100.0	0.0	-100.0
Asset sales	-2,000.0	0.0	0.0	0.0	0.0
Adjustments	-488.0	0.0	0.0	0.0	0.0
Change from Survey Baseline	131,671.0	2,801.8	-1,691.3	1,766.4	-1,262.8

*Agreed programmes

1986-87 £m

Department	Baseline	Changes from Baseline			
		Opening Minister	Position CST	Latest Position Minister	Position CST
Defence	18,613.0	182.7	-250.0	182.7	-250.0
FCO-ODA	1,299.0	78.0	-62.7	78.0	-62.7
FCO-other	602.0	65.5	-15.1	65.5	-13.1
EC*	600.0	30.0	30.0	40.0	40.0
IBAP (inc prefunded AFF)*	1,312.0	-15.3	-19.5	80.7	80.7
AFF (domestic)	786.0	8.5	-245.6	15.3	-233.5
Forestry*	57.0	-1.7	-9.7	-4.1	-4.1
Regional Policy (GB)	478.0	157.0	-200.0	64.0	-113.0
DFI (other)	752.0	167.4	-68.0	105.0	-37.0
ECGD	-159.0	324.4	284.6	297.2	287.8
Energy	324.0	7.0	-50.6	-7.6	-50.6
Employment	3,184.0	81.9	-528.2	-90.0	-242.0
Transport	2,258.0	52.5	-115.0	-85.0	-149.0
Housing	2,576.0	398.0	-363.0	637.4	-362.6
PSA	-117.0	11.9	0.0	-2.9	0.0
DOE other (inc Urban)	954.0	96.3	-160.0	96.3	-100.0
Ordnance Survey*	18.0	6.0	-2.6	0.7	0.7
Home Office	1,070.0	49.8	-25.6	1.7	-20.0
LCD	581.0	0.0	-29.3	0.0	-5.0
DES	3,432.0	165.8	-103.0	-3.1	-87.4
OAL	330.0	10.7	-9.9	10.7	-3.0
Health - PSS	14,657.0	640.7	0.0	459.7	0.0
Social Security	41,521.0	940.0	0.0	461.0	0.0
Superannuation*	1,226.0	-55.3	-55.3	-55.3	-55.3
Scotland	4,067.0	20.7	-4.3	20.7	-4.3
Wales	1,589.0	3.1	-15.0	-2.9	-15.0
N. Ireland	4,390.0	34.4	28.4	34.4	28.4
Inland Revenue	974.0	28.0	0.0	28.0	20.0
C.Ex Other Depts.	878.0	4.2	-3.0	4.2	-3.0
Other Depts.	333.0	33.1	-7.6	33.1	-7.6
LA current*	25,182.0	1,048.4	1,048.4	1,048.4	1,048.4
NI EFLs (inc RMPS)	298.0	-500.0	-500.0	-500.0	-500.0
Reserve*	4,750.0	-750.0	-750.0	-750.0	-750.0
Pay Factor	0.0	0.0	-100.0	0.0	-100.0
Asset sales	-2,000.0	0.0	0.0	0.0	0.0
Adjustment	-521.00	0.0	0.0	0.0	0.0
Change from Survey Baseline	136,294.0	3,323.7	-2,301.6	2,263.8	-1,662.2

*Agreed programmes

1987-88 £m

Changes from Baseline

Department	Baseline	Opening Minister	Position CST	Latest Minister	Position CST
Defence	18,617.0	1,046.6	-250.0	1,046.2	-250.0
FCO-ODA	1,320.0	157.3	-63.6	157.3	-63.6
FCO-other	618.0	71.3	-20.1	71.3	-17.8
EC*	615.0	195.0	195.0	215.0	215.0
IBAP(inc prefunded AFF)*	1,344.0	-20.7	-24.6	111.3	111.3
AFF(domestic)	805.0	-9.1	-283.6	-17.5	-270.9
Forestry*	59.0	-1.8	-9.8	-4.2	-4.2
Regional Policy(GB)	489.0	169.0	-200.0	-48.0	-145.0
DII(other)	773.0	62.7	-244.0	11.0	-227.7
ECGD	-163.0	191.9	132.3	160.0	134.9
Energy	332.0	4.7	-67.4	-16.4	-67.4
Employment	3,264.0	33.5	-623.3	-145.0	-279.0
Transport	2,311.0	74.5	-126.0	-42.0	-172.0
Housing	2,641.0	425.0	-486.0	663.5	-486.0
PSA	-120.0	0.8	0.0	-12.9	-5.0
DOE other(inc Urban)	976.0	85.1	-160.0	85.1	-100.0
Ordnance Survey*	19.0	10.2	-3.5	2.5	2.5
Home Office	1,096.0	113.3	-35.2	18.3	-10.0
LCD	595.0	36.0	-38.4	17.0	17.0
DES	3,518.0	180.2	-106.0	-2.2	-91.0
OAL	338.0	18.1	-10.2	15.8	-2.0
Health +PSS	15,024.0	1,066.8	0.0	846.0	0.0
Social Security	42,559.0	2,123.0	0.0	1,498.0	0.0
Superannuation*	1,256.0	37.7	37.7	37.7	37.7
Scotland	4,170.0	36.1	-91.5	36.1	-91.5
Wales	1,629.0	25.6	10.6	11.6	7.6
N.Ireland	4,500.0	61.4	-50.0	61.4	11.4
Inland Revenue	998.0	-8.2	0.0	-8.2	0.0
CEx Other Depts	900.0	27.8	-33.0	27.8	-33.0
Other Depts.	380.0	60.4	-4.5	60.4	-4.5
LA current*	25,577.0	948.0	948.0	948.0	948.0
NI EFLs(inc RMPS)	305.0	-1,000.0	-1,000.0	-1,000.0	-1,000.0
Reserve*	4,868.0	131.2	131.2	131.2	131.2
Pay Factor	0.0	0.0	-100.0	0.0	-100.0
Asset sales*	-2,050.0	50.0	50.0	50.0	50.0
3% Uplift	1,379.0	-1,379.0	-1,379.0	-1,379.0	-1,379.0
Adjustment	-543.0	0.0	0.0	0.0	0.0
Change from Baseline	140,399.0	5,024.4	-3,904.9	3,607.1	-3,133.0

*Agreed programmes

SECRET

DRAFT PAPER BY CHIEF SECRETARY FOR 4 OCTOBER CABINET

1984 PUBLIC EXPENDITURE SURVEY

Cabinet agreed on 5 July to hold the public expenditure planning totals to aggregate figures of £131.7 billion, £136.3 billion and £140.4 billion respectively for the three years 1985-86 to 1987-88. I was invited to report again on the Survey when I had completed discussions with the Ministers responsible on individual expenditure programmes and manpower allocations.

2. I have now had bilateral meetings with colleagues on all the major programmes. Some further meetings have been taking place in the last day or so, on which I can report orally.

3. But I have to report to colleagues that we have made disappointingly little progress on expenditure. The position is summarised in annex A.

4. For departmental expenditure agreements have been reached on only [] programmes, involving net [additions] to the baseline of []. There are major unresolved issues on [the FCO, Agriculture, Trade and Industry, Housing, Education and Social Security departmental programmes.] And we are also a long way from reaching agreements which would yield the savings on baseline of £250 million, £500 million, and £1000 million in nationalised industries' external financing limits endorsed by E(NI) on 3 July.

Agree
sufficiently
imprecise

5. In aggregate, colleagues are still seeking net additions to provision for the non-agreed programmes implying overshoots on the agreed targets [of around £1 $\frac{3}{4}$ billion in 1985-86 rising to £4 billion in 1987-88]. Some of these additions may, in the last resort, prove to be irresistible. But in aggregate expectations must be scaled down -
if the targets are to be met.

6. For this reason I am having to press for programme totals well below present demands, either by withdrawal of bids or option reductions; or, in a number of cases, both.

7. Hence there are major gaps still to bridge. No doubt some further progress could be made in bilateral exchanges. But, given the size of the task and the major issues of political priorities identified in some areas, Cabinet will wish to consider whether the time has come to convene the small group of Ministers under the chairmanship of the Lord President of the Council, envisaged in our 5 July discussion, to look at those areas of expenditure on which it does not prove possible to reach bilateral agreements during the course of this week. I suggest the group should be ready to start work on Monday 15 October, immediately after the Party Conference.

8. On manpower, where I was charged to press for significant reductions in the present plans for 1 April 1988, we have made some progress, and agreements have been reached for some Departments where programme expenditure remains unresolved. To reach our target, however, it will be necessary to agree sizeable further reductions. I hope to make more progress bilaterally, but where that proves impossible I will be obliged to ask the Ministerial group to consider the position.

PES 1984: POSITION REACHED AT 27 SEPTEMBER 1984

CHANGE FROM BASELINE

Department	1985-86		1986-87		1987-88	
	Baseline	Agreed+ Dept Bids	B'line	Agreed+ Dept Bids	B'line	Agreed Dept Bids
(excl LA relevant current and NI EFLs)						
Defence	18003	+323.6	18613	+182.7	18617	+1046.2
FCO-ODA	1264	+10.9	1299	+78.0	1320	+157.3
FCO-Other	602	+46.3	602	+65.5	618	+71.3
EC*	550	+205.0	600	+40.0	615	+215.0
IBAP (inc AFF prefunded)	1304	+44.7	1312	+80.7	+1344	+111.3
AFF (domestic)	776	-1.1	786	+15.3	805	-17.5
Forestry*	56	-3.5	57	-4.1	59	-4.2
Regional Policy (GB)	491	-5.0	478	+64	489	-48.0
DTI (Other)	782	+112.0	752	+105.0	773	+11.0
ECGD	30	+209.5	-159	+297.2	-163	+160.0
Energy	321	-7.1	324	-7.6	332	-16.4
Employment	3158	-32.0	3184	-90.0	3264	-145.0
Transport	2176	-121.0	2258	-85.0	2311	-42.0
Housing	2507	+53.0	2576	+637.4	2641	+663.5
PSA	-109	+44.5	-117	-2.9	-120	-12.9
DOE Other	931	+44.1	954	+96.3	976	+85.1
Ordnance Survey*	18	-0.2	18	+0.7	19	+2.5
Home Office	1023	+2.2	1070	+1.7	1096	+18.3
LCD	547	0	581	0	595	+17.0
DES	3353	-4.2	3432	-3.1	3518	-2.2
OAL	287	+8.4	330	+10.7	338	+15.8
Health and Social Security	13954	+297.7	14657	+459.7	15024	+846.0
Superannuation*	39410	+532.0	41521	+461.0	42559	+1498.0
Scotland	1130	-58.5	1266	-55.3	1256	+37.7
Wales	3904	+36.1	4067	+20.7	4170	+36.1
N Ireland	1521	+7.7	1589	-2.9	1629	+11.6
Inland Revenue	4213	+45.6	4390	+34.4	4500	+61.4
ChX Other	949	+8.1	974	+28.0	998	-8.2
Depts	853	3.6	878	+4.2	900	+27.8
Other Depts	319	20.0	333	+33.1	380	+60.4
LA						
Current*	24754	+944	25182	+1048	25577	+948
NIEFLS (inc RMPS)	1332	-250	298	-500	305	-1000
Reserve*	3750	-750	4750	-750	4868	+131.2
Asset Sales	-2000		-2000		-2050	+50
3% Uplift					1379	-1379

Baseline (5 July Cabinet objective)** and implied changes 131671 +1766.4 136294 +2263.8 140400*** +3607.1

*Agreed programmes **excludes double counting ***Adjusted baseline

COVERING CONFIDENTIAL

6 NO



Treasury Chambers, Parliament Street, SW1P 3AG

27 September 1984

Andrew Turnbull Esq
PS/Prime Minister
10 Downing Street
LONDON
SW1

Dear Andrew

PUBLIC SERVICE PAY AND EXPENDITURE IN 1985-86

... I attach a draft paper which the Chief Secretary proposes to circulate to colleagues tomorrow or on Monday if the Prime Minister prefers.

Yours Sincerely
Paul Pegler
PAUL PEGLER
Assistant Private Secretary

COVERING CONFIDENTIAL

DRAFT

PUBLIC SERVICE PAY AND EXPENDITURE IN 1985-86Note by the Chief Secretary to the Treasury

We need to agree what to assume about public service pay increases in our public expenditure plans for 1985-86.

2 I am proposing that we should adopt an assumption of 3 per cent for all public service groups except the local authorities; and that public expenditure baselines should be reduced by the difference between this assumption and the 4 per cent factor originally used to construct baseline figures for 1985-86.

The choice of pay assumption

3 The pay assumption for 1984-85 was 3 per cent. With the prospects for private sector pay settlements for the next round no lower than 5½ per cent a lower figure for next year (say, 2½ per cent) would be seen as unrealistic and could be ineffective.

4 A higher figure (4 per cent) would give the wrong signal about the course we want future settlements to take. I have concluded that we should retain an assumption of 3 per cent. The CBI are arguing, on similar grounds, for a pay assumption of 3 per cent.

Application

5 The figure chosen underlies the provision made in the public expenditure plans for 1985-86 and later years for increases in pay rates and allowances deriving from settlements between now and 31 March 1986. It will be the basis of the provision for pay in 1985-86 Estimates. The assumption will not apply formally to local authorities (although it is not inconsistent with the targets that we have announced and in practice it should influence their behaviour). Similarly, as last year, the assumption does not apply to the nationalised industries (although tight EFLs and financial targets should help to ensure that discipline is maintained). A 3 per cent assumption will produce much needed baseline reductions of about £200 million in each year of the Survey.

Running Costs

6 Following our discussion in July (CC(84) 25th conclusions), I will be seeking to agree with colleagues a figure, for most departments in line with the provision sought in the Survey, for the increase in their running costs in 1985- 86. I will then expect Estimates provision for running costs to be within the agreed figure. My aim will be to agree running cost figures that in aggregate imply an increase of not more than 4 per cent above this year's provision. This approach should not be affected by our choice of a pay assumption.

Announcement

7 I think we should avoid any formal announcement of the pay assumption before other public expenditure decisions are announced in the Autumn. In the last 2 years we explicitly announced the pay assumption. In both cases, we got unhelpful headlines. If questioned before the Autumn Statement, we should say that there will again be a pay assumption, and that it will be much the same next year as this; pay assumptions are a routine part of public expenditure planning, under present arrangements; but they are not norms, do not determine particular settlements, and do not merit a special announcement.

Conclusion

8 I propose that:

- i. for the cash plans and Estimates we should use a single general assumption of 3 per cent for pay settlements affecting 1985-86 for all public service and affected groups, other than local authorities;

- ii. I should take account of the assumption by reducing the public expenditure baseline for all selected programmes to reflect the difference between 3 per cent and 4 per cent;

- iii. there should be no formal announcement^A in advance of the Autumn Statement.



FROM: CHIEF SECRETARY
DATE: 27 September 1984

PRIME MINISTER

PUBLIC EXPENDITURE IN 1984-85

At the end of last week's discussion in E(A) of my proposal for a moratorium on local authority capital spending you asked that the Chancellor and I bring forward proposals to deal with the expected overshoot on public expenditure this year. The current forecast of the overshoot is £1.25 billion, or £1.5 billion if the miners' strike goes on to the end of the year.

2 I have conducted a review of the possibilities. Although it is still open to us to take decision which would bring this year's spending closer to plan, I have concluded - in the light of the decision which we have taken on local authority capital and other issues - that the action necessary to get back to the planned figure would not be acceptable to our colleagues.

3 Numerous measures could be taken to defer expenditure, or to squeeze programmes generally this year. We could impose a moratorium on central government capital and on defence procurement, together with a cut-back on training in the armed forces, savings in the employment special measures programme, and so on. These measures could cause a great deal of disruption without large savings, and the least damaging way of squeezing programmes (as last year) would be by an across-the-Board reduction in cash limits of, say, 1 per cent (equivalent to about 3 per cent on the remaining spend this year). This would be worth about £430 million gross, or £300-350 million net after taking account of the fact that some of the reduction would have shown up anyway in underspending, and that some of the cuts might not stick.

4 Many of the individual deferments, cancellations and other savings implicit in a squeeze on this scale would, clearly, be resisted strongly by our colleagues. It seems unlikely that colleagues, who have ruled out at moratorium on local authority capital, would be ready to agree to one on their own Departmental programmes. At this late stage in the year there would be maximum opprobrium in seeking reductions in areas where it would be necessary publicly to withdraw funds already promised - for example from the Regional Health Authorities and the Research Councils (as you know, some of these are already arguing that their existing funding is inadequate).

5 These are some of the objections to an across-the-board cash limits cut. But we should, in addition, recognise the damage which would be done to the discipline of the cash limits system if - for the second year in succession - we changed cash limits in mid-year. In a year in which many cash limits are already under pressure from the extra costs of public sector pay settlements above the figure allowed for in the Estimates and from Budget VAT changes cash limit reductions would compel Departments to make cuts which make little economic or any other sense - in flat contradiction to all our efforts to improve financial management in Whitehall.

6 These considerations, in my view, rule out cash limit reductions as a practical possibility. Many of the non-cashlimit reductions which it is open to us to make - on social security, NHS charges, agricultural grants, for example - are, I believe, equally ruled out by existing pledges, or the force of political circumstances.

7 But there are some possibilities. We have already agreed in principle that the relevant costs of the miners' strike should be recovered through electricity prices once the strike is over. A decision now for a 10 per cent increase from 1 November would bring in some £250 million. I am separately considering savings on NCB investment, and from the electricity supply industry in the range of £100-150 million. If special asset sales go well (no hitches with the BT flotation, the civil aviation issue resolved satisfactorily and a number of other 'ifs' too) the proceeds may exceed our current forecast.

8 We should, in my view, pursue all these possibilities, with the objective of minimising the overspend. To that end we should severely limit any further claims on the Reserve, go hard for any savings, including increased charges, which we can identify, and accelerate asset sales and disposals of surplus public sector land whenever possible.

PK

PETER REES

How can we decide now whether strike is still continuing?



10 DOWNING STREET

From the Private Secretary

Prime Minister

The issues are difficult

(i) Moving to the Star Chamber phase without a Cabinet meeting as in para 3(b) would mean that the Chancellor was unable to deploy the economic prospects as a lever to secure greater cooperation from colleagues.

(ii) Postponing the Autumn Statement beyond the BT flotation means that the latter will take place against all the reports of Cabinet rows etc.

To discuss at next bilateral?

Yes

no

AT

24/9

Ref. A084/2371

PRIME MINISTER

Public Expenditure Survey 1984: Timetable

I should draw to your attention some potential difficulties over the timetable for the remaining stages of this year's Public Expenditure Survey.

BACKGROUND

2. Treasury officials have told us informally that they are working to a provisional timetable, the main features of which are set out below. The timetable assumes that, as you indicated was probable to the Cabinet on 5 July (CC(84) 25th Conclusions, Minute 5), there will be a small Ministerial "Star Chamber" Group, like MISC 99 last year, to consider and make recommendations to the Cabinet on expenditure programmes which cannot be agreed bilaterally between the relevant spending Ministers and the Chief Secretary, Treasury.

September/early October: bilaterals between Chief Secretary and spending Ministers.

Friday 12 October: paper by the Chief Secretary, following the bilaterals, circulated to the Cabinet and the small Ministerial Group.

Monday 15 October: Ministerial Group begins work.

Thursday 18 October: Cabinet discussion of public expenditure.

Friday 2 November: Ministerial Group finishes work.

Monday 5 November: Chief Secretary circulates further paper to the Cabinet.

Thursday 8 November: Cabinet concludes 1984 Public Expenditure Survey.

Tuesday 13 November: Autumn Statement published.

I understand that, for reasons connected with the BT flotation, the Chancellor of the Exchequer is anxious to publish the Autumn Statement not later than 13 November.

THE PROBLEM

3. I have serious doubts about the realism of the Treasury timetable, for the following reasons:

a. It is difficult to see how the Ministerial Group could begin work on Monday 15 October if the Chief Secretary's paper is not considered until Friday 12 October and, more importantly, if there is to be a Cabinet discussion of public expenditure on Thursday 18 October. Spending Ministers will reserve their positions until then, and the Ministerial Group will make no significant progress during its first week of operation. This would be particularly unfortunate since the week of 15 October is the last week before the House returns and Parliamentary commitments begin to restrict the time available for meetings of the Group.

b. Even if the Group is able to begin work on 15 October it is doubtful whether it will have enough time to resolve the issues on the outstanding programmes and complete its work by Friday 2 November. Experience last year and in earlier years has shown that several meetings are often necessary to settle a single programme. We understand that both the number of programmes on which there is no agreement and the issues at stake are likely to be greater than last year. Even if the Group is able to finish its meetings by Friday 2 November, there will be insufficient time for you to consider its report and have informal meetings on one or two politically difficult issues before the paper is circulated the following Monday 5 November (or possibly Tuesday 6 November) for discussion on Thursday of that week.

POSSIBLE ACTION

4. There are two ways in which the timetable might be changed while maintaining the objective of publishing the Autumn Statement on 13 November.



i. It would be possible to gain two days by having the public expenditure discussion at a special Cabinet on Tuesday 16 October. But that really requires the Chief Secretary's paper to be circulated before Friday 12 October - that is during the Party Conference - and it still leaves the timetable very tight indeed.

ii. It would be possible to dispense with any further discussion of the Survey until the final Cabinet on 8 November. After all, the Cabinet agreed the objectives of the Survey on 5 July, and it is not easy to see how their conclusions could be strengthened by another general discussion. On this approach, the Chief Secretary could give an oral report on progress in his bilateral discussions at the Cabinet meeting on 4 October (which is anyway due to take a paper on public expenditure and pay); and you could announce the establishment of the small Ministerial Group, remind your colleagues of the Cabinet's previous decision on the objectives of the Survey, and ask them to give the Group their fullest co-operation. It would not be possible for the Chancellor of the Exchequer to give on 4 October an account of the macro-economic situation with the benefit of preliminary indications of the likely results of the Autumn economic forecast, as he probably could on 18 October. But this is not, I think, a serious drawback: the Chancellor could circulate a paper on the macro-economic situation for discussion on 8 November.

5. There is also the more fundamental question whether it is wise to aim at publishing the Autumn Statement as early as 13 November. Even if one or other of the possibilities mentioned in the preceding paragraphs is acceptable, the timetable remains very tight indeed. In particular, it cannot be taken for granted that the Cabinet will reach final conclusions in one meeting on 8 November. If Ministers set a timetable which they fail to meet, that fact is, I fear, likely to become public knowledge; and it could well have adverse effects on confidence generally and perhaps on the success of the BT flotation itself.

6. The only way significantly to extend the time available to complete the discussion of public expenditure is to defer the publication of the statement until well after the flotation of BT: say, until the first or second week of December (there are precedents for publication in December). If it was decided to do that, it would be as well for the fact to be announced well in advance, so as to minimise the risk of creating in the financial markets an impression that the delay is unplanned, and reflects uncertainty or disarray in the Government as to how or even whether to keep public expenditure in the forecast period within the declared public expenditure totals.

7. No doubt you will wish to discuss these matters with the Chancellor of the Exchequer, when he returns from abroad, and the Chief Secretary, Treasury before reaching final decisions.

RA

ROBERT ARMSTRONG

24 September 1984



With the Compliments
of the
Chief Secretary to the Treasury's
Private Secretary

Treasury Chambers,
Parliament Street,
SW1P 3AG



cc: Chancellor

FST

EST

MST

Sir P Middleton

Mr Bailey

Mr Monck

Treasury Chambers, Parliament Street, SW1P 3AG

Mr Burgner

Mr Scholar

Mr Gray

Mr Webb

Mr Robson

Mr Bird

Ms Leahy

Rt Hon Peter Walker MBE MP
 Secretary of State for Energy
 Department of Energy
 Thames House South
 Millbank
 London
 SW1P 4QJ

18 September 1984

**NATIONALISED INDUSTRIES BILATERAL:
 24 SEPTEMBER 1984**

We are meeting on 24 September to discuss your nationalised industry programmes as part of the 1984 Investment and Financing Review. In preparation for this, I attach tables which set out the present financing bids received from each of your industries and I hope that we can use these as a common starting point for our discussions.

2 We agreed at E(A) on 3 July that we should reduce industries' aggregate bids to £250 million below the baseline in 1985-86, £500 million below in 1986-87, and £1,000 million below in 1987-88. These are demanding targets but it is essential that we meet them if our overall objectives are to be achieved. We have to recognise that some industries will be able to contribute more to this target than others. At E(A) the Prime Minister said that all sponsor Ministers will need to do their utmost to secure satisfactory reductions.

3 E(A) also agreed some general guidelines for our discussions and I shall want to consider for each of your industries the scope for:-

- (i) reducing current costs and improving profitability
- (ii) reducing working capital
- (iii) cutting investment
- (iv) selling fixed assets

4 Clearly the present coal strike creates uncertainty. I recognise that we may well have to look at the NCB (and possibly Electricity) figures again when it is over. At that time we shall obviously need revised projections from Ian MacGregor quickly. In the meantime, I suggest we assume for present purposes that the strike has no effect beyond 1984-85. This is admittedly artificial but I can see no other sensible basis for our discussion. My proposals for the NCB are in a separate Annex to this letter as this may be helpful for circulation. We will need to ensure that the figures (eg on coal deliveries) remain on a consistent basis between the industries.

5 Turning to the figures, I will be seeking reductions from the baseline for external finance for your industries of the order of £400 million in 1985-86, £600 million in 1986-87 and £1 billion in 1987-88. Against these we have to set the increases assumed for the Redundant Mineworkers Payment Scheme of £115 million in 1985-86, £15 million in 1986-87 and £22 million in 1987-88. Clearly I would be very ready to be guided by you about the way this is spread between your industries and about the form which the savings take. You might find it useful to know my thinking on these points and this is set out in the rest of this letter. You will note that the suggestions on individual industries total more than the aggregates I am seeking from you.

A Electricity Supply Industry (England and Wales)

6 The revised bids compared to baseline are (£m):-

1985-86	1986-87	1987-88
+ 24	+ 298	+ 570

We need to settle both the ESI's external financing requirements and its next financial target and performance aim from 1985 - 86.

7 Nigel Lawson wrote to you on 2 August and 13 September explaining our view that the next target should be based on a 5 per cent return on current cost assets. Our officials have also been exploring the scope for cost savings.

8 I suggest we consider a longer target period than the three years the industry have in mind, perhaps five years. That would give greater stability and, by running into the next Parliament, avoid any awkward hiatus just before the end of this one.

9 Five per cent targets are already in place on the Industry's appliance retailing and contracting activities. It appears to be common ground with the ESI already that, for transmission and distribution, charges should be based on a 5 per cent return. That leaves the generation assets (some 60 per cent of the total). Here I am prepared to see a gradual transition over the period to 1987-88. By then the new power stations currently under construction and the cross-channel link are due to be completed. Our assessment is that, with a determined drive to get full use from this investment and to reduce costs elsewhere, a 5 per cent return could be achievable without real price increases. This should be enshrined in a demanding performance aim.

10 Accordingly, I propose a target from 1985-86 to 1988-89 based on:-

- (a) A return on generating assets rising linearly to 5 per cent by 1987-88, remaining at that level thereafter.
- (b) An average return on non-generating assets of 5 per cent. This would give an overall figure of about 4.5 per cent for a five year period

Allowing for Corporation Tax and other adjustments, external financing requirements should be reduced by some:-

	1985-86	1986-87	£m 1987-88
Higher financial target	- 250	- 400	- 700

11 I am assuming that future arrangements for load management do not affect the financial target.

12 In order to achieve the E(A) target we need also to look for other savings. I suggest we look for reductions (net of Corporation Tax) of the following order:-

	1985-86	1986-87	£m 1987-88
Other savings	- 175	- 375	- 450

May we discuss the following areas:

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- (a) Capital investment where reductions could come principally from a prudent view of when Sizewell B might proceed; deferring refurbishment of the transmission and distribution system; leaving small generating projects (wind, hydro etc) to the private sector; reduced provision for development projects (eg oil to coal conversions); real reductions in the cost and volume of new connections by the later years
- (b) Working capital mainly from running down nuclear stock holdings more quickly; and a lower coal and oil price assumption.
- (c) Accelerating the sale of fixed assets
- (d) Recovering the cost of new connections up to the statutory limits (and again without changing the financial target).
- (e) Interest, resulting from other reductions.

13 We also have doubts about the economic viability of some non-operational investment by Area Boards, where there has been substantial growth in bids since last year; the Industry have not yet convinced us that these Boards' programmes will earn the Required Rate of Return. Normally I should have looked for further reductions of some £40 million a year here. But if the Boards can reassure us - by accepting the 5 per cent target - I will not need to pursue this.

14 Overall these savings would give external financing figures compared to baseline of:-

	1985-86	1986-87	1987-88
Reductions compared to baseline	- 401	- 477	-580

B British Gas Corporation

15 The original bids compared to baseline are (£m)

	1985-86	1986-87	1987-88
	+ 75	+ 237	+ 389

The Wytch Farm disposal gives rise to an additional £84 million in 1985-86 in respect of corporation tax.

16 BGC are forecasting substantial peak day physical surpluses of gas towards the end of the IFR period. This has substantial EFL implications and reducing the physical surpluses would produce corresponding savings - for example by postponing the second phase of the Morecombe project, by delaying filling the Rough reservoir and by contracting for less peak supply gas. These savings could build up to £115 million by 1987-88.

17 The Corporation's investment in research into substitute natural gas (SNG) is also proving expensive. Sir Denis Rooke himself has said that the country will not need to depend on SNG much before 2050. I suggest the research programme should be terminated. This would save £40 million a year by 1987-88.

18 I would like to discuss the prospect of increased sales of BGC's surplusland.

19 In addition to these savings, I should also like to discuss with you:-

- (a) capital investment - further reductions, particularly on exploration but also on onshore investment
- (b) working capital - reductions in stocks (other than gas) and some further pressure on debtors
- (c) trading costs - further reductions in trading costs, both as a result of not filling Rough and through continuing pressure on manpower.

Overall, I think we could achieve savings (after tax) in these areas of

1985-86	1986-87	1987-88	(£ million)
- 70	- 150	- 260	

20 On gas prices, you know my view, shared by the Chancellor, that gas is still substantially underpriced in both domestic and non-domestic markets. Our officials have together been looking at the figures over recent months and it would appear that BGC is currently undercharging by over 20 per cent in the domestic market and something of a similar order in other markets. BGC's tariff proposals over the IFR period do nothing to rectify this. Indeed, the gap widens by 1987-88. In my view, we must seek to close the gap. A 4 per cent real price rise each year for 3 years from 1 January 1985 would go a long way towards achieving this. After tax, and taking account of working capital effects, this would generate savings of around:-

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- 220 - 440 - 774

21 Overall these savings would amount to a reduction compared with BGC's initial bid of:-

- 290 - 590 - 1,034

After taking account of BGC's extra tax liability for the Wytch Farm sale, the reduction compared with baseline would be :-

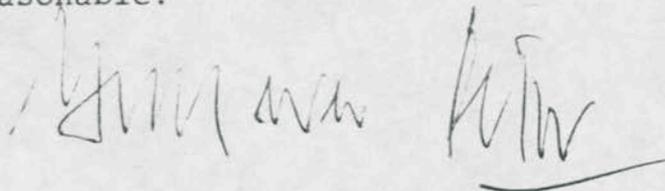
- 131 - 353 - 645

C. BNOC

22 The bids compared to baseline are (£m):

1985-86	1986-87	1987-88
+ 1.2	- 0.4	- 0.1

23 I appreciate that a measure of uncertainty surrounds BNO's finances over the IFR period. It would be very helpful if you could bring the Corporation back to baseline in 1985-86. I believe that the corporation's current losses should reduce the corporation tax payment they were anticipating in 1985-86. This means a return to baseline in that year is reasonable.



PETER REES

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NCB

1. The figures including RMPS are compared to baseline:

	£m		
	1985-86	1986-87	1987-88
Bid for external financing (i)	+172	+326	+80
Bid for additional RMPS	+115	+ 15	+22
	+287	+341	+102

(i) Adjusted for effect of full use of French interconnector
The strike clearly creates major uncertainties, particularly for internal resources and stock provision. Nonetheless certain areas for savings can be identified elsewhere, consistent with established policy:

(a) Investment in fixed assets

	1985-86	1986-87	1987-88
Baseline	784	748	767
Bid	+25	+39	+7
Saving	-75	-53	-40

This reduction simply reduces the provision for the four years (1984-85 to 1987-88, including £798m this year) down to a total of £3000m. Further reassessment will be needed later.

(b) Sales of assets

Saving	-20	-20	-40
--------	-----	-----	-----

Given NCB's dire financial circumstances, acceleration of the sale of non-mining subsidiaries and other assets is needed.

(c) Working capital General squeeze and elimination of contingencies.

	1985-86	1986-87	1987-88
Savings	-10	-30	-30

(d) Assume break-even by 1987-88 as in Mr McGregor's objectives

	0	0	-40
--	---	---	-----

These will give total reduction compared to base of:

	-105	-103	-150
--	------	------	------

and changes compared with baseline of:

NCB	+67	+223	- 70
RMB	+115	+ 15	+ 22

UNREVISED BID

Industry : NATIONAL COAL BOARD

BASELINE £ million	1984-85 forecast outturn	1985-86	1986-87	1987-88
Fixed asset investment	598	784	748	767
TOTAL CAPITAL REQUIREMENTS	322	640	600	615
TOTAL INTERNAL RESOURCES	-1,278	-83	218	223
TOTAL EXTERNAL FINANCE	1,600	723	382	392

PROPOSED CHANGES COMPARED TO BASELINE £ million	1985-86	1986-87	1987-88
Fixed assets in UK	+25	+39	+7
Working-capital	+39	+64	+40
Other	-	-1	-
TOTAL CAPITAL REQUIREMENT CHANGE	+64	+102	+47
EXPECTED CHANGE IN INTERNAL RESOURCES	-108	-224	-33
Grants	+93	+164	-18
PDC	-	-	-
Net temporary borrowing	-7	-7	-7
Net long and medium term borrowing	+81	+162	+96
Leasing	+5	+7	+9
TOTAL PROPOSED CHANGE IN EXTERNAL FINANCE	+172	+326	+80

ASSUMPTIONS % CHANGE	1984-85	1985-86	1986-87	1987-88
GDP	1.5	1.5	1.5	1.5
Retail Price Index	6.0	6.0	6.0	6.0
Average earnings (whole economy)	-	-	-	-
Average earnings (own industry)	4.0	4.5	5.0	5.0
Tariffs (overall)	2.0	5.0	5.5	6.0
Tariffs (domestic)	4.0	5.0	6.0	6.0
Tariffs (industrial)	2.5	5.0	5.0	5.5
Manpower (no)	220,800	199,700	185,700	176,100

REVISED BID

Industry : ELECTRICITY (ENGLAND AND WALES)

BASELINE £ million	1984-85 forecast outturn	1985-86	1986-87	1987-88
Fixed asset investment	1,321	1,195	1,095	1,123
TOTAL CAPITAL REQUIREMENTS	1,056	1,125	990	1,015
TOTAL INTERNAL RESOURCES	1,936	2,147	2,327	2,385
TOTAL EXTERNAL FINANCE	-880	-1,022	-1,337	-1,370

PROPOSED CHANGES COMPARED TO BASELINE £ million	1985-86	1986-87	1987-88
Fixed assets in UK	+23	+133	+75
Working-capital	+47	+55	+97
Other	-	+6	+24
TOTAL CAPITAL REQUIREMENT CHANGE	+70	+194	+196
EXPECTED CHANGE IN INTERNAL RESOURCES	+46	-104	-374
Grants	-	-	-
PDC	-	-	-
Net temporary borrowing	-168	-	-
Net long and medium term borrowing	+233	+343	+616
Leasing	-41	-45	-46
TOTAL PROPOSED CHANGE IN EXTERNAL FINANCE	+24	+298	+570

ASSUMPTIONS % CHANGE	1984-85	1985-86	1986-87	1987-88
GDP	2.7	1.8	1.4	1.4
Retail Price Index	5.0	5.0	5.0	5.0
Average earnings (whole economy)	7.0	6.0	6.0	6.0
Average earnings (own industry)	6.1	5.8	5.8	5.8
Tariffs (overall)	-	-	-	-
Tariffs (domestic)	1.8	3.3	3.5	3.5
Tariffs (industrial)	2.3	3.3	3.5	3.5
Manpower (no)	133,500	130,500	128,100	-

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UNREVISED BID ⁽¹⁾

Industry : BRITISH GAS CORPORATION

BASELINE £ million	1984-85 forecast outturn	1985-86	1986-87	1987-88
Fixed asset investment	841	731	811	831
TOTAL CAPITAL REQUIREMENTS	1,060	912	1,051	1,078
TOTAL INTERNAL RESOURCES	1,248	1,308	1,546	1,585
TOTAL EXTERNAL FINANCE	-188	-396	-495	-507

PROPOSED CHANGES COMPARED TO BASELINE £ million	1985-86	1986-87	1987-88
Fixed assets in UK	-93	-125	-93
Working-capital	+115	-4	+74
Other	-	-	-
TOTAL CAPITAL REQUIREMENT CHANGE	+22	-129	-19
EXPECTED CHANGE IN INTERNAL RESOURCES	-137	-366	-408
Grants	-	-	-
PDC	+84	-	-
Net temporary borrowing	+75	+237	+389
Net long and medium term borrowing	-	-	-
Leasing	-	-	-
TOTAL PROPOSED CHANGE IN EXTERNAL FINANCE	+159	+237	+389

(1) the original bid has been revised to take account of the corporation tax payment in 1985-86 resulting from the Wytch Farm disposal

ASSUMPTIONS % CHANGE	1984-85	1985-86	1986-87	1987-88
GDP	2.5	1.5	1.0	1.0
Retail Price Index	6.5	8.0	8.0	8.0
Average earnings (whole economy)	8.5	10.0	10.0	10.0
Average earnings (own industry)	6.5	8.0	8.0	8.0
Tariffs (overall)	4.7	6.9	7.8	7.8
Tariffs (domestic)	4.5	6.7	7.9	8.1
Tariffs (industrial)	5.7	7.6	7.8	7.5
Manpower (no)	97,000	95,000	93,000	91,000

UNREVISED BID

Industry : BRITISH NATIONAL OIL CORPORATION

BASELINE £ million	1984-85 forecast outturn	1985-86	1986-87	1987-88
Fixed asset investment	.4	.2	.3	.3
TOTAL CAPITAL REQUIREMENTS	.4	.2	.3	.3
TOTAL INTERNAL RESOURCES	4.4	3.0	2.3	2.4
TOTAL EXTERNAL FINANCE	-4.0	-2.8	-2.0	-2.1

PROPOSED CHANGES COMPARED TO BASELINE £ million	1985-86	1986-87	1987-88
Fixed assets in UK	-	-	-
Working-capital	-	-	-
Other	-	-	-
TOTAL CAPITAL REQUIREMENT CHANGE	-	-	-
EXPECTED CHANGE IN INTERNAL RESOURCES	-1.2	+4	+1
Grants	-	-	-
PDC	-	-	-
Net temporary borrowing	+1.2	-4	-1
Net long and medium term borrowing	-	-	-
Leasing	-	-	-
TOTAL PROPOSED CHANGE IN EXTERNAL FINANCE	+1.2	-4	-1

ASSUMPTIONS % CHANGE	1984-85	1985-86	1986-87	1987-88
GDP	-	-	-	-
Retail Price Inde	6.0	6.0	6.0	6.0
Average earnings (whole economy)	-	-	-	-
Average earnings (own industry)	6.0	6.0	6.0	6.0
Tariffs (overall)	-	-	-	-
Tariffs (domestic)	-	-	-	-
Tariffs (industrial)	-	-	-	-
Manpower (no)	140	140	140	140



10 DOWNING STREET

From the Private Secretary

12 September 1984

Dear Callum,

DTI EXPENDITURE

The Prime Minister was grateful to your Secretary of State for his minute of 5 September setting out past and prospective developments in DTI expenditure programmes. She hopes that the reductions in support for BSC and BL on which the downward profile for future years depends will in practice be realised.

Yours sincerely

Andrew Turnbull

Andrew Turnbull

Callum McCarthy, Esq.,
Department of Trade and Industry.

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FROM: CHIEF SECRETARY
DATE: 11 September 1984

PRIME MINISTER

PUBLIC EXPENDITURE IN 1984-85

I attach a minute to you, copied to colleagues concerned, about the substantial overspend we face on local authority capital expenditure in spite of the curbs announced last July. My minute proposes that local authorities should be asked not to enter into any further commitments for the rest of the financial year. This is against the background of the prospect that the Public Expenditure Reserve will be substantially overspent; I thought I should let you know the latest position in more detail.

2 When we were reviewing the position last July we were expecting an overspend of some £500 million. This figure has risen substantially. Three main factors are involved:

- i the prospective outturn on local authority capital; we suspected in July that the cash limit would be overspent and allowed £250 million in our assessment. But the new returns from local authorities mean we must add a further £250 million;
- ii the continuation of the miners' strike; as you know each week adds about £25 million to public expenditure;
- iii increases in interest rates which unavoidably affect some programmes, such as housing subsidies and export credit interest support.

3 The current position is being reviewed in detail by Treasury officials, but we must assume that we face a likely overspend of no less than £1 billion, even if the strike ends this month. Although less than 1% of total public expenditure, there is no doubt that a figure of this magnitude would be damaging to the credibility of the Government. So far we have resisted pressure to acknowledge such an overspend publicly, accepting only that the position is tight. But it will be difficult to avoid revealing the latest estimate at the time of the Autumn Statement in mid-November, a particularly sensitive time because of the importance of establishing market sentiment in the run up to the BT flotation. Of course the markets will be most concerned about the PSBR as a whole, and our assessment over the Summer was that the PSBR for the current year should not be much out of line with the Budget forecast. Nonetheless we must take action in those areas open to us to keep down the prospective overspend, and to indicate a continued determination not to see our plans exceeded. Hence my proposal in the attached minute.

4 As you will be aware, the other area where we might take action is an early increase in electricity prices, to shift some of the cost of the coal strike from taxpayer to electricity consumer. I am conscious of the disadvantages of this course, but the longer the strike proceeds the less will be the scope for offsetting the cost in this financial year, and the more exposed will we be to the charge of letting the expenditure situation drift

J. Gier
J. PETER REES

[Approved by the Chief Secy.]

Pulse Minister ②

AT 7/9

C

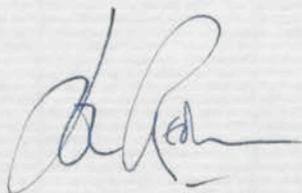
Any we discuss.
I think a well
done letter
would
be a point
is required
not

MR TURNBULL

The DTI figures show similar levels of expenditure over the seven year historic and forecast period for all items save support for nationalised industries and BL.

The decline in Nationalised Industry support excludes BT figures. No allowance is made for the £300 million plus which BL has received from the Jaguar sale. As they will now be spending this, and as no credit is given to the Government for this receipt, the figures understate BL cash support.

They also assume, as DTI say, continuing progress on BSC which we now know is very unlikely whilst an outturn in 1986/7 of no overall cash support is planned on current form it is highly unlikely.



JOHN REDWOOD



②
PRIME MINISTER
AT 6/9

DTI EXPENDITURE

When we spoke on Sunday I mentioned some charts which had been produced for me. I think they graphically illustrate the way in which both DTI expenditure is continuing to be held down and, within the reduced totals of expenditure, a shift is taking place in that expenditure away from nationalised industries and towards support for science and technology and product innovation. Two qualifications need to be made. Chart 2, representing the present PES bids, shows a decline in expenditure on nationalised industries rather less marked than in the present base line. I should make clear, however, that these bids cannot be certain while BSC's position remains unclear. Second, what the charts do not show, on either the base line or a bid basis, are the further measures we are committed to taking to reduce the level of regional support through our new regional policy. The substantial reduction in regional expenditure on which I shall be putting forward proposals to E(A) at the end of the month will give further scope to direct

JH2AZM



expenditure towards support for new technologies and
improving industrial efficiency, within a reduced total.

... 2 I attach a copy of the charts and I hope you will find
them of interest.

NT

N T

5 September 1984

Encl

Department of Trade and Industry

JH2AZM

CHART 1

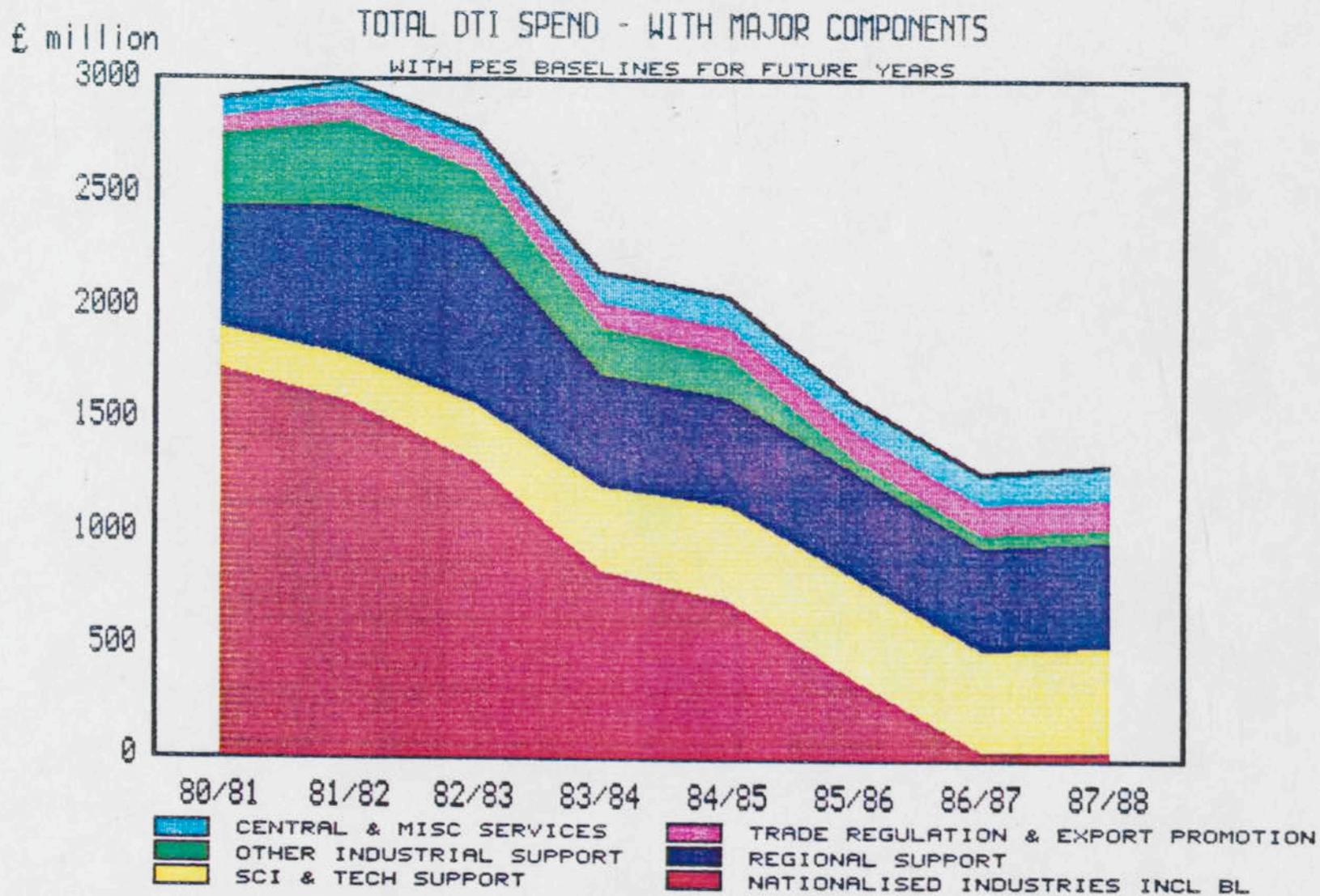


CHART 2

£ million

TOTAL DTI SPEND - WITH MAJOR COMPONENTS

WITH PES BIDS FOR FUTURE YEARS

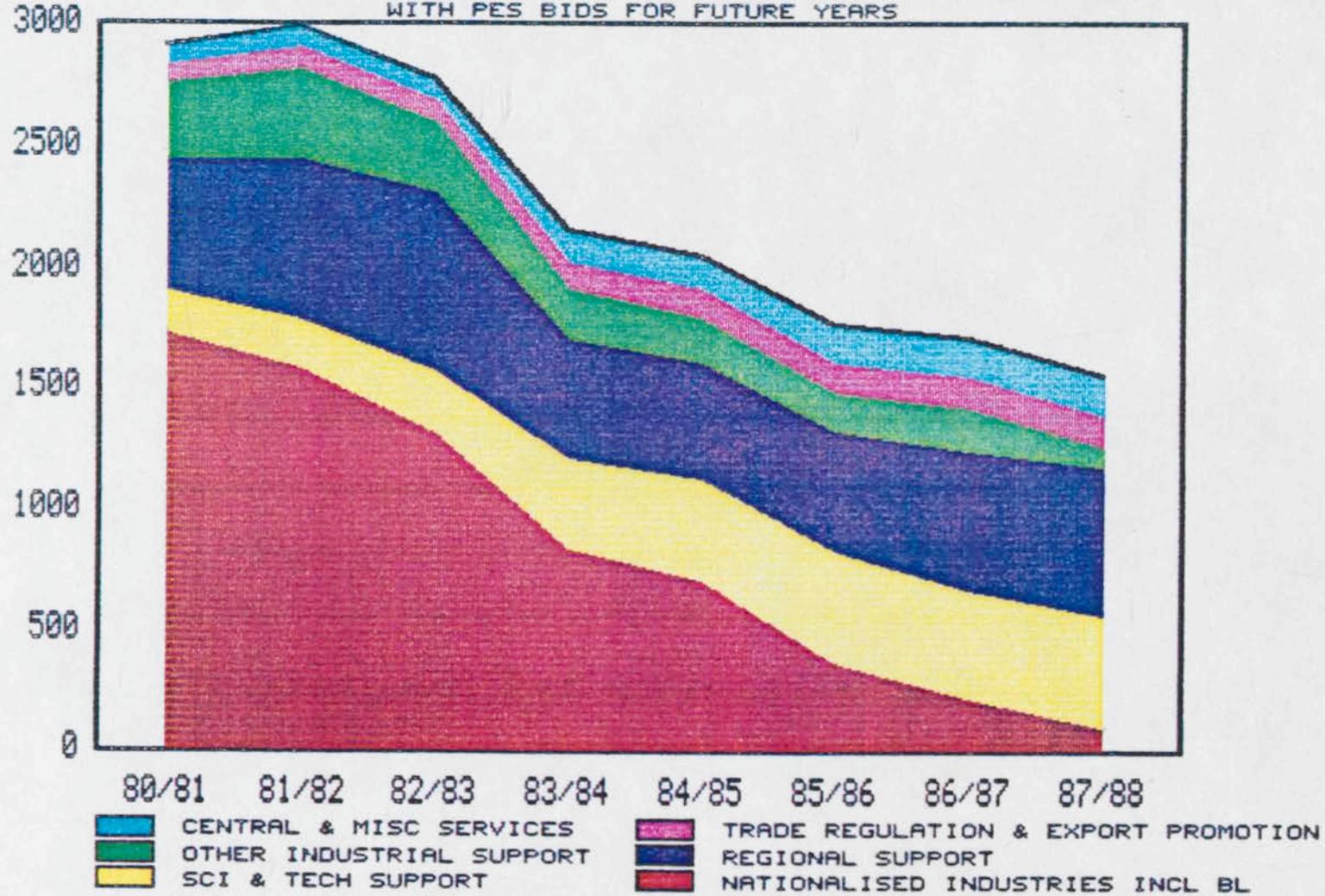
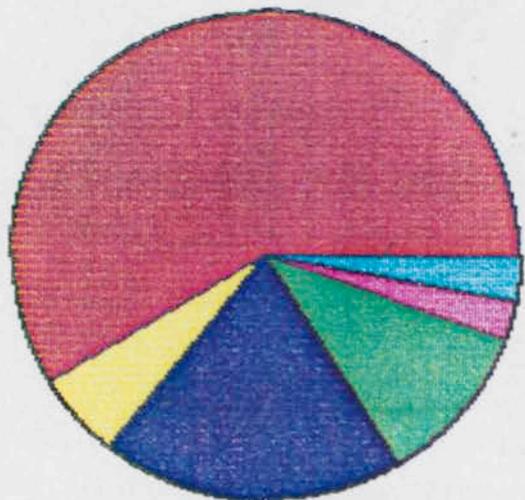


CHART 3

MAJOR COMPONENTS OF DTI SPEND

1980/81



1984/85

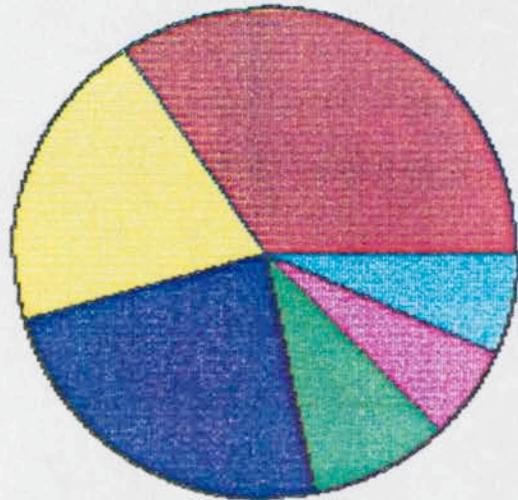


-  NATIONALISED INDUSTRIES INCLUDING BL
-  SCIENTIFIC & TECHNOLOGICAL SUPPORT
-  REGIONAL SUPPORT
-  OTHER INDUSTRIAL SUPPORT
-  TRADE REGULATION & EXPORT PROMOTION
-  CENTRAL & MISCELLANEOUS SERVICES

CHART 4

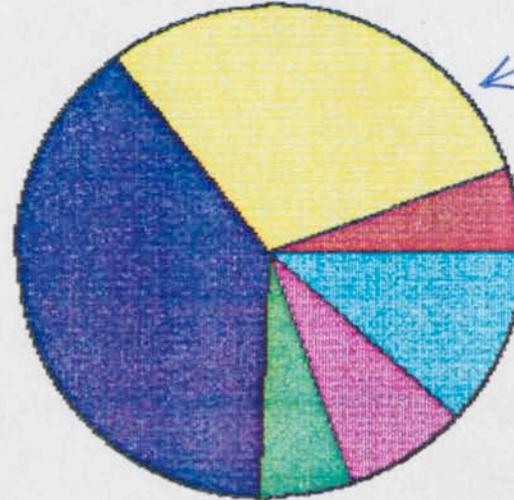
MAJOR COMPONENTS OF DTI SPEND

1984/85



1987/88

PES BID



- NATIONALISED INDUSTRIES INCLUDING BL
- SCIENTIFIC & TECHNOLOGICAL SUPPORT
- REGIONAL SUPPORT
- OTHER INDUSTRIAL SUPPORT
- TRADE REGULATION & EXPORT PROMOTION
- CENTRAL & MISCELLANEOUS SERVICES

That is I propose a 46% cut from 1980/81 to 1987/88.

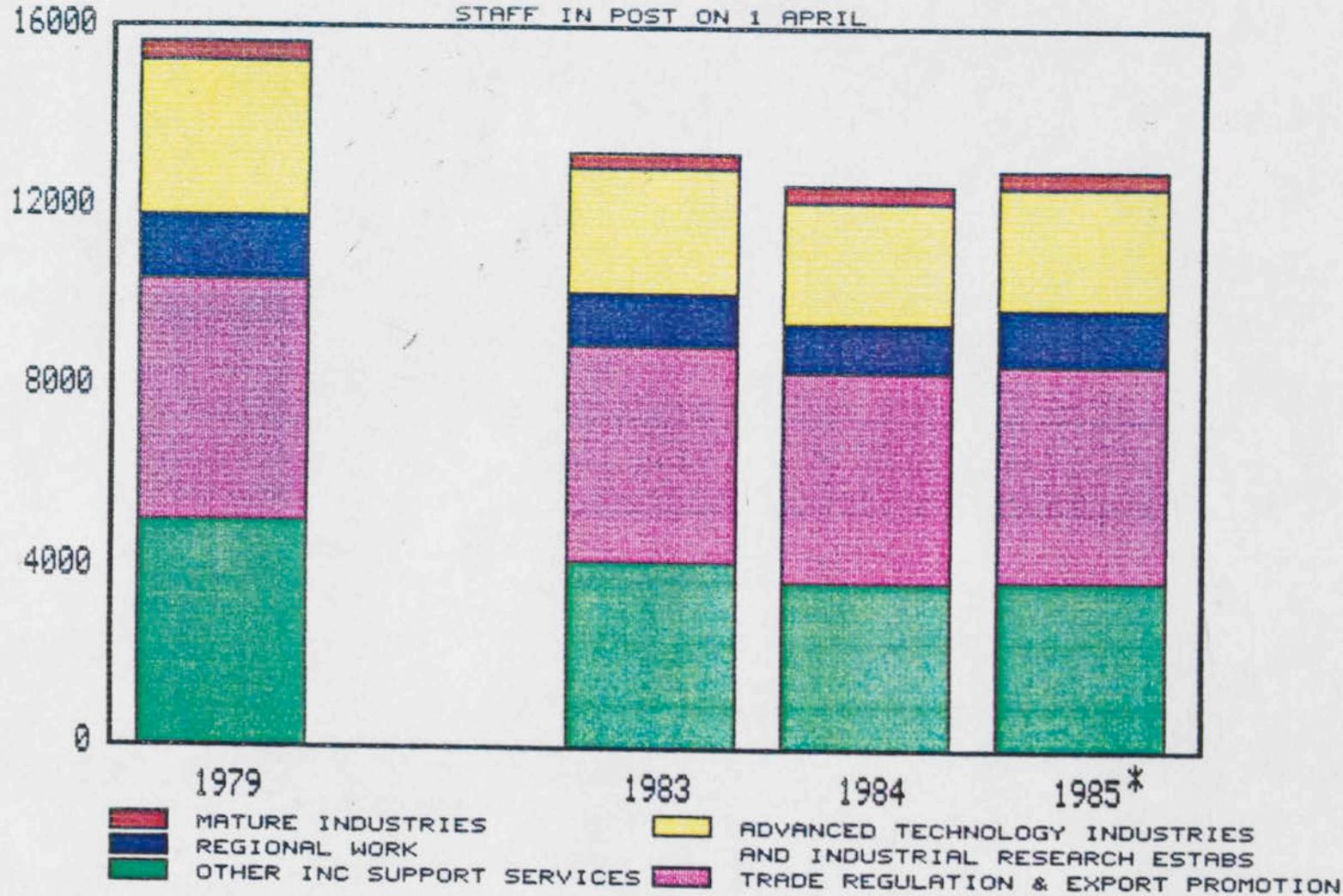
Cash figures

1980/81	£ 2,921 m.
84/85	£ 2,052 m.
87/88	£ 1,564 m.

CHART 5

DTI MANPOWER

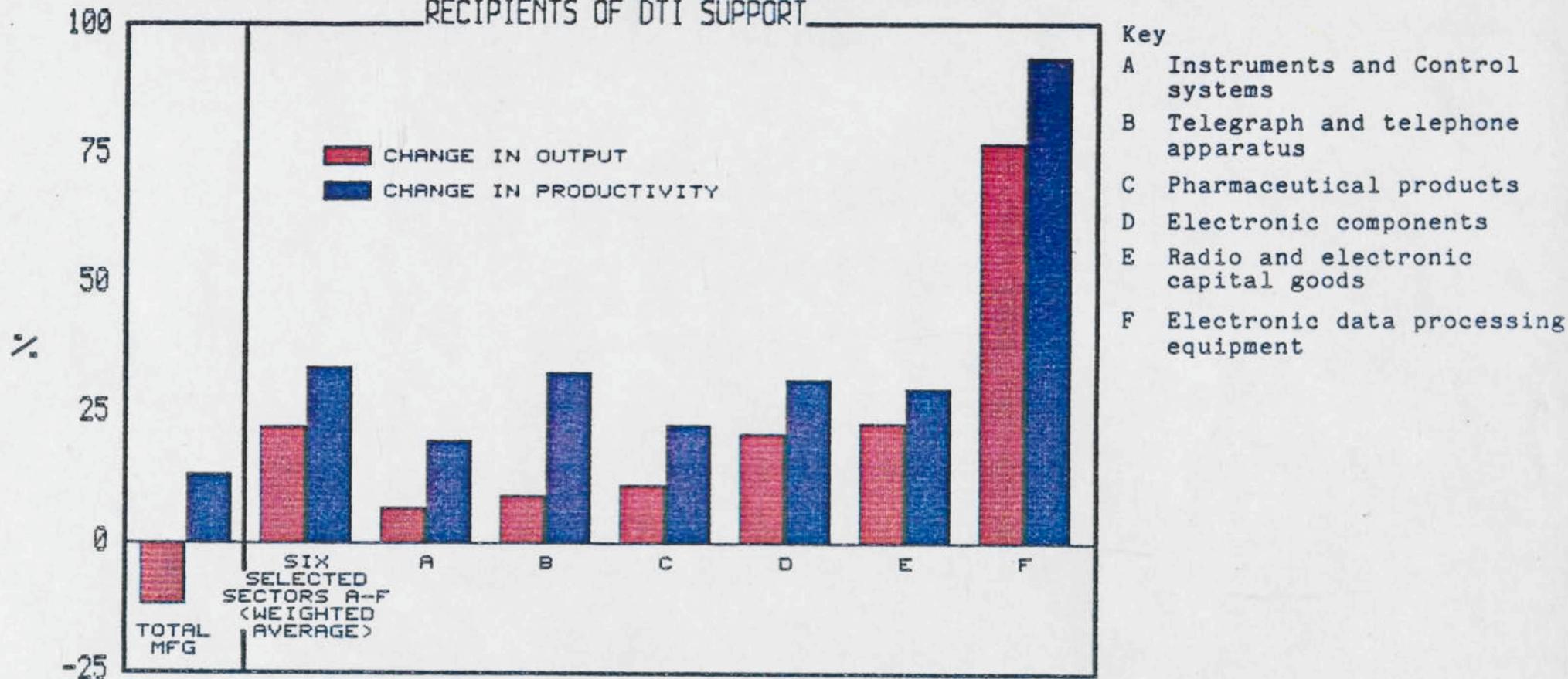
STAFF IN POST ON 1 APRIL



* The 1985 total represents the target of 12807 shown in the Supply Estimates, plus 120 additional posts sought for the new regional assistance schemes, minus 11 posts cut elsewhere.

CHART 6

CHANGES IN OUTPUT AND PRODUCTIVITY BETWEEN 1979/80 AND 1983/84 IN TOTAL MANUFACTURING AND IN SIX SELECTED SECTORS WHICH ARE MAJOR RECIPIENTS OF DTI SUPPORT



The selected sectors are major recipients of DTI financial support, and particularly of scientific and technological support. While together they accounted for about 10% of manufacturing net output, over the period from 1980 to 1982 they received 42% of total DTI science and technology support and 22% of total section 7 and 8 Industry Act support.

●. ART 27. ends:-

CST to PM 30.7.84.

PART 28 begins:-

SS/DTL to PM 5.9.84.

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