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PPS pot . 22/76

FROM: R M PERFECT

DATE: 20 April 1988

Not rec'd until 21/4

1. MR POTTER <sup>BHP</sup> 20/4
2. CHIEF SECRETARY

cc PPS ←  
 Sir Peter Middleton  
 Mr Anson  
 Mrs Case  
 Mr Hawtin  
 Mr Turnbull  
 Mr Call

## LA CAPITAL CONTROLS

Mr Ridley spoke to you about barter deals - Jill Rutter's minute of 18 April refers. We have discussed the problem with DOE officials and Mr Ridley will be writing to you.

2. Mr Ridley's announcement of 9 March brought into the LA capital control system: sale and leaseback deals; barter deals; purchases of shares and payments in respect of guarantees. The problems that mainly concern Mr Ridley are arising on barter deals, under which a local authority swaps land or buildings for other land and buildings or services (typically construction work). It is now clear that far more local authorities have been setting up barter deals than DOE realised. So local authorities' ability to obtain new assets (in return for existing assets) has been higher than we realised. Local authorities, and their MPs, do not see why these deals should be stopped.

3. Barter deals are caught by the amendments to the Local Government Finance Bill which are due to be discussed between 7.30 pm and 9.00 pm on Monday 25 April. Regulations, to control short term leases, under the 1980 control system, will be debated between 10.00 and 10.30 pm that evening. Government supporters are likely to be particularly concerned with the first Vote, on the amendments. And in view of the wider problems on local government finance Mr Ridley is anxious to go some way towards meeting their concerns.

## Why control barter deals?

4. DOE want to stop barter deals so that they, and the district auditors, can be sure that local authorities are not selling assets too cheaply. We do not regard this as a very strong case. Treasury



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has not been concerned about deals under which one piece of land is swapped for another. But deals which swap land for services do concern us, because they increase the level of economic activity in the economy in the same way as public spending does. We believe this argument is convincing.

Possible solutions

5. Mr Potter and I have discussed with DOE officials three possible solutions to Mr Ridley's problems. We have expressed a strong preference for option (iii).

i. Drop the proposals. Mr Ridley could drop his proposals to control barter deals. But this would be a defeat for him. And there is a danger that many barter deals will then be arranged before the new capital control system is in place.

ii. Increase spending power from receipts. DOE officials have suggested that the existing restrictions on the use of accumulated and in-year non-housing receipts (known as the prescribed proportion) could be increased from 30 per cent to 40 or even 50 per cent. This is an indirect solution to the problem. DOE hope it would ensure that most local authorities have sufficient spending power to complete the deals that the 9 March statement brought into the control system. We have argued against this approach for two reasons. Firstly, loosening the present control system now will make the Government's proposals for a new control system less attractive. Secondly, if this approach is adopted we could end up with more spending (including barter deals) than would have taken place had Mr Ridley never tried to control barter deals.

iii. Generous transitional arrangements. Local authorities could be given extra spending power to cover barter deals in the pipeline. Deals which the local authority were committed to would be allowed through. And deals which local authorities had approved in principle might also be accommodated. As a result local authorities existing plans for barter deals would be allowed through. Recorded gross spending and in-year receipts would be increased, but there would be no net effect on the planning total or the PSBR. In future, deals would have to be arranged within the constraints of the capital



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control system. This approach ensures that any concessions have a smaller effect on gross spending than the original decision to control barter deals.

**Future years**

6. Mr Ridley is likely to want to say that, in future, spending power will be set higher to reflect the fact that barter deals (and leasing deals) have been brought within the control system. We will need to check the form of words he wishes to use. But now that the scope for arranging capital spending outside the control system has been substantially reduced, there is a case for allowing higher gross spending within the control system, provided it is offset by higher receipts. We would then have stopped a growing amount of uncontrolled and unrecorded expenditure and increased the Government's plans for future gross spending without increasing the planning total.

**Action**

7. Mr Ridley will consider these options and write to you, probably seeking a decision by close on Friday 22 April. He may also raise the issue at Cabinet tomorrow.

R. M. Perfect.

R M PERFECT





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My ref:

Your ref:

The Rt Hon John Major MP  
Chief Secretary  
HM Treasury  
Parliament Street  
LONDON  
SW1P 3AG

CHIEF SECRETARY	
REC.	21 APR 1988
ACTION	Mr Potter
COPIES TO	Cy, Sir P. M. Deeken Mr Anderson, Mr Phillips Mrs Case, Mr Hanston Mr Perfect, Mr Call

21 April 1988

*Dear Chief Secretary*

We had a word the other day about the consequences of my statement in the House on 9 March. The amendments to the capital control legislation which I announced in that statement are due to be taken on Monday immediately before Third Reading of the Local Government Finance Bill and the Opposition's motion against the regulations made on 9 March will be debated later that evening.

The reaction to the statement has amply confirmed that we had correctly identified the loopholes which local authorities were using to avoid the effect of capital expenditure and borrowing controls. If anything, it shows that we had underestimated the extent to which leasing and barter, and in particular the latter, were being used.

The statement was of necessity made without prior consultation or notice. For that reason, I said I would consider extra capital allocations for schemes caught by the changes. Such schemes fall into two categories: those which were already in the pipeline at the time of the statement, for which we have to be reasonably generous, and those for which no commitments had been entered into, but which would be treated unreasonably under the new rules we have introduced.

On the first category, inevitably there were many schemes which were caught by the changes in the primary and secondary legislation but to which the authorities concerned (and in some cases other parties) were committed in the sense of having incurred expenditure (for instance on acquisition of sites or on design work) or having entered into other obligations (for instance rehousing tenants). I have received many representations about such schemes and I am satisfied that it is right that we should be generous in issuing capital allocations to cover such cases. Most of the schemes concerned were originally framed as barter deals and the effect of making available an additional

*ok*  
*This was what Mr Ridley raised yesterday*  
*AA*





allocation would be that they would now be carried out on a cash basis. The expenditure would be matched by an equal and opposite receipt, so there would be no net public expenditure consequences and conditions would be attached to any allocations that would preclude additional borrowing or the use of spending power in future years. In the case of short-leases, I understand that the Treasury's view is that the taking of such leases should not be recorded as public expenditure, so there would likewise be no adverse public expenditure consequences.

The criteria that I would propose to use in considering "pipeline" cases would be that:-

- (i) expenditure has been incurred, or substantive negotiations or moral commitments entered into by the local authority or a third party; and
- (ii) the scheme is not designed primarily to increase the stock of physical assets over which the local authority has effective control or to raise money on the strength of operational assets.

Turning to schemes which were not in the pipeline on 9 March, the principal reason why local authorities seek to use barter deals is to avoid the present restrictions on the rate at which they may use their capital receipts to justify new expenditure. We have recently discussed at E(LF) the general question of the use of capital receipts and I need not rehearse the arguments now. It has, however, to be conceded that the existing rules work harshly in cases where a receipt can only be realised as a result of expenditure having been incurred. Typically, this will happen where an operational building needs to be replaced before the site on which it stands can be released for sale. Many of the cases which have been drawn to my attention following the 9 March statement are of this type. The Audit Commission in their report on "Local Authority Property" have also drawn attention to the inhibiting effect of the capital control system on sensible property rationalisations.

We already have a very limited scheme under which additional allocations are given to facilitate "back-to-back" transactions under which authorities acquire land and then dispose of it again (typically as part of wider redevelopment by the private sector). What I propose is an enhancement of this scheme which would apply in cases where a local authority need to acquire land (or incur other capital expenditure) in order to release other land for development. I would propose to offer extra allocations for:-

- (i) the exchange of land for land;
- (ii) the replacement of existing assets held by the local authority by assets to be used for a similar purpose; or
- (iii) schemes in which the main intention is to facilitate the investment by the private sector in assets which when the scheme is complete will be owned, operated, and controlled by the private sector.



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Here again conditions would be attached to allocations to ensure that there was no net additional expenditure or borrowing.

I hope you will be content for me to announce these measures when moving the new clauses to the Local Government Finance Bill on Monday. I also hope that they will be sufficient to allay the concern which some of our supporters have expressed about the short-term consequences of the 9 March statement.

In the longer term, the 9 March measures do, however, have implications which ought now to be the subject of examination by officials. It is argued, with some justice, by the local authorities that the bringing of leasing and barter within controls represents a general reduction in the level of expenditure which they can incur. Some leasing (eg of offices for terms of less than 20 years) has hitherto been regarded as unexceptionable and likewise barter has been used by authorities for many years, though not indeed on the scale which has recently become apparent. Insofar as assets (eg houses) have been provided by such means, we have taken credit for them in estimating the outputs of our programmes. We have changed the control framework and the question arises of whether we should make some corresponding adjustment to the permitted level of spending power to reflect what one might call "legitimate" barter and leasing. I see two options, namely

- (i) an increase in what one might call the "baseline" level of allocations, which could be justified on the grounds that the existing allocations methodology is based on pre 9 March assumptions; or
- (ii) an increase in the prescribed proportion for non-housing receipts, which would be of particular assistance to shire counties and to those districts which have been most inclined hitherto to use barter.

These need further investigation and I do not propose to say anything about them on Monday. But I have asked my officials to examine the implications and to report in time for the launch of the new capital control regime.

I am sending copies of this to the Prime Minister, Peter Walker, Kenneth Baker, Paul Channon, John Moore, John Wakeham, David Waddington, and Sir Robin Butler.

Yours sincerely  
Roger Butler

N.R.  
NICHOLAS RIDLEY  
(Approved by the Secretary of State and signed in his absence)



# A digest

for Councillors and Officers

No. 108

21 APRIL 1988

## 150 DISTRICT COUNCIL PROJECTS IN JEOPARDY 000

ALMOST 150 local authority projects - worth more than £350 million - may be abandoned because of the Government's clampdown on leaseback and barter deals.

These schemes range in value from under £1 million to a mammoth £45 million housing development in Oxford and a £40 million redevelopment of Bournemouth's Pavilion entertainment centre.

Information from ADC members shows at least 65 districts have schemes which will be severely affected by the new rules announced by Environment Secretary Nicholas Ridley last month. They include a £10 million shopping and car park development and a £1.5 million housing scheme in Mr. Ridley's own Cirencester constituency.

These schemes will now count as prescribed expenditure and thus push councils over their capital spending limits. Yet they would allow community assets to be provided without spending ratepayers' money and would put vacant land to good use.

The Government has praised such joint ventures between local authorities and the private sector but now it is killing them off because a few councils exploited the system to evade spending limits.

Our members have acted responsibly. None have entered into "Brent type" arrangements, according to our information, and none of their barter or leaseback deals have been challenged on legal grounds.

The Association has urged the Government to think again. But if

it does stand firm the best to hope for is DOE approval for schemes which meet certain objectives, such as housing the homeless.

### MEMBERS ALLOWANCES

IN response to a letter from John Denison, Chairman of General Services, calling for discussions on members allowances, Michael Howard, Minister of State for Local Government has written that he believes that "the level of allowances is not unreasonable."

The whole of his reply was read to the General Services Committee, which was incensed to hear his assertion that "many of the representations I receive are to the effect that councillors are overpaid, rather than underpaid". He had not been persuaded that the value of the allowances had fallen substantially since 1974, and he had figures to show that 38% of authorities paid the maximum allowance irrespective of the length of duty. In his opinion, this was the sort of practice which brought the system into disrepute, and had to be taken into account in setting the maximum level.

However, he did say that the DOE were examining the whole basis of



remuneration in their response to the Widdicombe Report, to be published shortly, and he would then meet with the ADC on the issue.

### CITIZENS ADVICE BUREAUX

THE time is fast approaching when the demands on Citizens' Advice Bureaux will outstrip the ability of local authorities to fund them. This was the feeling of the General Services Committee when it considered the growing volume of enquiries dealt with by CABX about social security and debt.

The problem was highlighted this month when many CAB offices were forced to close on the first day of the new social security regulations by the crowds of people seeking help. It is also likely to be intensified by Legal Aid Bill which would allow bureaux to offer legal advice in areas previously the work of solicitors.

Other sources of funding need to be identified, such as from those agencies which have contributed towards the problems which bureaux are now being asked to resolve. A meeting has been arranged with the National Association of CABX.

### DON'T IGNORE US, LORD YOUNG

LOCAL authorities have a crucial role to play in the regeneration of urban areas, the ADC has told Lord Young. While welcoming the Department for Enterprise's objective to encourage business the ADC is unhappy local authorities' role in this field was ignored in the White Paper.

The majority of district councils are heavily involved in economic development and the public see councils as the place to go for advice. The Association would like to discuss with Government departments and other agencies how they can all co-ordinate their activities at a local level.

The lack of extra aid has also been a disappointment. Lord Young was told that the move away from automatic grants in development areas will make it more difficult to attract inward industry.

The ADC is doing a review of regional aid and will present its ideas to the Government next year.

### BREATHING SPACE ON COMPULSORY COMPETITION

A welcome was given to the Government's decision to move the starting date for compulsory competitive tendering of services back from 1 April next year to 1 August.

"Those extra months will be very useful for local authorities, especially those which will have to start contracting out the more difficult functions of refuse collection and vehicle maintenance," said ADC Chairman, Roy Thomason.

### ORAL TOBACCO PRODUCTS

THE Association was delighted to learn that Health Ministers propose to make safety regulations to prohibit the supply of tobacco products which take the form of small sachets and are sucked.

The ADC has previously expressed concern at the introduction of these Skoal Bandits to the UK, because of the evidence about cancer of the mouth, and the aggressive marketing campaign for the products aimed at the young.

### CEMR ASSEMBLY

Don't miss out on the Assembly of European Municipalities and Regions, which is to take place from 1-4 June in Glasgow. This important event for Britain coincides with Local Government Week and the National Garden Festival. Over 1,000 people from throughout Europe are already lined-up to attend.

*Any enquiries relating to the contents of this newsletter should be addressed to the Publishers:*

## **ASSOCIATION OF DISTRICT COUNCILS**

Secretary: Gordon McCartney

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FROM: R M PERFECT

DATE: 21 April 1988

1. MR ROTTER <sup>BHP</sup> 21/4
2. CHIEF SECRETARY

cc

PPS

Sir Peter Middleton  
 Mr Anson  
 Mr H Phillips  
 Mrs Case  
 Mr Hawtin  
 Mr Turnbull  
 Mr Call

### LA CAPITAL CONTROLS

The Secretary of State for the Environment's letter of 21 April proposes concessions on barter, and sale and leaseback, deals. My minute of 20 April outlined the problem and the options.

2. Mr Ridley's proposals would allow local authorities to complete some of the deals that were caught by his announcement of 9 March. And he wishes to offer extra allocations to allow assets to be swapped for other assets. We recommend you agree subject to two provisos, which do not give DOE any difficulty. A draft letter is attached.

### "Pipeline" cases

3. Mr Ridley's immediate problem is caused by the large number of deals that local authorities are committed to but which, now that they have been brought within the scope of the LA capital control system, cannot be completed unless more spending power is issued. Mr Ridley wishes to issue extra allocations to cover these cases provided they are not intended to increase the local authority's stock of physical assets or to raise money. We recommend you agree. All of the deals will increase gross spending and capital receipts by offsetting amounts, so there will be no net effect on public spending.

### Future cases

4. Mr Ridley also wishes to extend the existing arrangements under which gross expenditure on assets can be offset against receipts



from sales of assets - with no net effect on public expenditure. He proposes to offer allocations to allow:

i. the exchange of land for land. There are no Treasury reasons for stopping this.

ii. the replacement of existing assets held by local authorities by assets to be used for a similar purpose. This also presents no problems except to the extent that extra economic activity is generated. However, on Monday E(LF) favoured allowing such deals under the new capital control system. And there are no effects on net public spending, so you need not object.

iii. Schemes intended to promote private sector investment in assets which will end up in the private sector. This is intended to allow DOE to approve town centre developments in which local authority assets may be involved. DOE say they intend to ensure the local authority does not retain an influence over those assets by selling the freehold and keeping a long lease. We have recorded the point in the draft letter.

#### Longer term

5. Mr Ridley also suggests officials should consider whether allocations should be set higher in future, now that barter deals and sale and leaseback deals have been brought within the control system. LG can discuss this with DOE and other departments over the next few weeks. But we see no reason why including these deals in the LA capital control system should increase public spending - any extra gross spending should be fully offset by higher public expenditure receipts.

R.M. Perfect.

R M PERFECT



**CONFIDENTIAL****DRAFT LETTER TO:**

The Rt Hon Nicholas Ridley AMICE MP  
Secretary of State for the Environment  
Department of the Environment  
2 Marsham Street  
LONDON SW1

April 1988

**LA CAPITAL CONTROLS**

Thank you for your letter of 21 April.

I am content with the line you propose to take on Monday on the understanding that, as stated in your letter, none of the barter and sale and leaseback deals allowed through as a result will increase net public spending. Where allocations are given to facilitate private sector investment, the local authority should not be allowed to keep any undue interest in that investment eg in the form of a long lease on property.

I also agree that officials need to consider the future effects of bringing barter, and sale and leaseback, deals within the capital control system. You identify two possible approaches in your letter. But both would increase net public expenditure. I see no reason why any higher gross spending should not be fully offset by extra capital receipts. But I am content for our officials to pursue this.

I am copying this letter to the Prime Minister, Peter Walker, Kenneth Baker, Paul Channon, John Moore, John Wakehan, David Waddington and Sir Robin Butler.

**JOHN MAJOR**