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Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Michael Heseltine MP  
 Secretary of State for Defence  
 Ministry of Defence  
 Main Building  
 Whitehall  
 London  
 SW1A 2HB

6<sup>th</sup> November 1985

Dear Michael,

MOD RUNNING COSTS

Thank you for your letter of 4 November.

I am glad that we are agreed that your department's running costs total for 1986-87 should be set at £5,215 million. This will enable me to report to Cabinet on Thursday that figures for all departments have been agreed.

You stressed the need to take account of the fact that the 58,000 Service personnel remaining within running costs perform functions in support of front-line units (who are now outside), and that-because of problems of disaggregation - you are involved in some very rough and ready figuring at present. I accept this, and confirm that the new regime for running costs control is aimed at achieving tighter discipline over such expenditure across all departments and is not intended as an attack on your block budget.

I also accept the need for flexibility in the last resort. But we have all agreed that sound planning for such expenditure is required and that every effort must be made to stay within the limits once they have been set. I am surprised that you thought MOD was in some way excluded from the Cabinet decision of 3 October; as you know, I certainly believed that we had already agreed your inclusion along with your reduced coverage at our bilateral on 26 September. Cabinet did not, of course, agree any exclusions.

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However, I acknowledge that the very significant changes we have made to your running costs coverage, when added to the untested nature of your monitoring mechanism for the Service personnel included, does leave you dependent upon uncertain forecasts for next year. Exceptionally, therefore, I am prepared to agree that you should apply the total as a target rather than a limit during 1986-87, on the understanding that you will observe this target just as keenly as you would a limit.

I am copying this letter to the Prime Minister and to Sir Robert Armstrong.

*Yours ever,*  
*John*

JOHN MacGREGOR

