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CAF

RESTRICTED

The Rt Hon Lord Whitelaw CH MC
Lord President of the Council
Privy Council Office
Whitehall
LONDON
SW1A 2AT

B/LF 13/5.
Any comments for
D. Willetts?

8 May 1986

PV advise that this
is entirely consistent with
the Green Paper proposals.
NSPR D/W 13/5.

Dear Willie,

For the meeting of E(LF) that was proposed for 13 May I had it in mind to circulate a paper relating to the financial framework of my legislative proposals, with particular reference to grants and non-domestic rates. I understand that since Norman Fowler's paper which was also to be on the agenda is not ready you are unwilling to convene a meeting on 13 May. I quite understand your thinking.

It is however of importance that if the timetable for the preparation of instructions to the draftsman is not to be put at risk I can be quite clear without much more ado that colleagues are content with what I have in mind in these respects. I therefore attach a draft of my E(LF) paper and should be grateful if colleagues would let me have by 15 May any comments which they wish to make.

Copies of this letter go to members of E(LF) to Kenny Cameron and to Sir Robert Armstrong.

Yours ever,
Malcolm Rifkind

MALCOLM RIFKIND

CABINET

MINISTERIAL STEERING COMMITTEE ON ECONOMIC STRATEGY SUB-COMMITTEE ON LOCAL GOVERNMENT FINANCE

LOCAL GOVERNMENT FINANCE STUDIES: SCOTLAND: PROPOSED GRANT ARRANGEMENTS

Memorandum by the Secretary of State for Scotland

1. This paper deals with the changes to the grant distribution arrangements needed with the introduction of a community charge in Scotland. The arrangements described are interim in the sense that they deal with the period during which non-domestic rates have been frozen and their further increase linked to the rate of inflation. They do not deal with the full implementation of the Green Paper proposals which involve a centrally set non-domestic rate poundage, accruing centrally. The proposals described in this paper elaborate the arrangements outlined in the Scottish chapter of the Green Paper. (A subsequent paper will deal with issues affecting the community charge itself.)

Specific Grants

2. At present Scottish local authorities receive central government support in the form of specific grants and rate support grant. Specific grants represent 12% of total grant (about half the English proportion). Four specific grants have just been abolished following a review. Specific grants will continue within the criteria set out in the Green Paper and subject to further review.

Revenue Support Grant

3. Rate support grant is at present distributed in three elements: needs element, resources element and domestic element. It is proposed that rate support grant should be replaced by a single revenue support grant which would contain, in line with the Green Paper, a needs equalisation element and a standard per capita element. The needs of local authorities would be equalised on the basis of the assessments of expenditure need which at present form the basis of the distribution of the needs element of rate support grant. An attempt would be made to simplify the assessments in advance of the change in order to make them more comprehensible. In each tier the equalisation of need would be carried out

by compensating every authority with an amount equal to the difference between its expenditure need per adult and that of the authority with the lowest expenditure need per adult. This amount would constitute the needs element of the new revenue support grant. The remainder of the grant would be distributed on a per capita basis. This would be the standard element of the grant. It is proposed that, as under existing Scottish legislation relating to rate support grants, the amount of the revenue support grants payable to local authorities should be prescribed in an order which would be laid before the House of Commons for affirmative resolution, together with a report setting out the considerations upon which the amount of the grant, including its two elements, is based, although those considerations would not be specified in the primary legislation.

Non-domestic rate income

4. As described in para 8.31 of the Green Paper, during the interim period non-domestic rates would be frozen and index linked to inflation. Not until there was a common basis of valuation and a common non-domestic rate poundage throughout Great Britain, would the non-domestic rates be pooled centrally. Until that time non-domestic rates would continue to be collected by the local authorities as being obviously the most economic solution given the existing rate collecting machinery. The authorities would also remain responsible for setting the rate within the maximum figure set by the Government each year. There would thus continue to be variations in the rating resources available to authorities and resource equalisation would in this interim period continue to be necessary. This would be achieved by taking non-domestic rate income into account in calculating entitlement of each authority to revenue support grant. This would be done by subtracting from the needs assessment an estimate of non-domestic rate income, before equalising needs in the way described in para 3 above. In making this calculation on an estimate of non-domestic rates based on full collection, authorities will have an incentive to collect non-domestic rates efficiently. Annex A shows how the grant calculations described would be carried out. Special arrangements would, as indicated in the Green Paper, be needed for Orkney and Shetland, but there are precedents for these.

Safety Netting

5. Changes of the scale involved are bound to mean significant movements of grant and it will be necessary to have safety netting arrangements (para 8.38 of the Green Paper). There are already arrangements within the present grant

distribution arrangements for rate support grant designed to prevent excessive swings in grant from one year to another. In recent years these arrangements have been necessary to manage the phasing in of the client group method of rate support grant distribution. The present arrangements derive from the Secretary of State's general power to prescribe rate support grant and are described fully in the Report on the Rate Support Grant Order. The arrangements are not based on a specific statutory power to safety net. This present arrangement allows the maximum flexibility and is satisfactory to the local authorities. It is proposed that safety netting should continue on this basis for revenue support grant. In the base year, the effect would be to ensure that in relation to the change in the method of financing local government the total claim on domestic taxpayers was unchanged from the preceding year, if spending remained constant. Thereafter the aim would be to contain yearly movements in grant within acceptable limits while remaining able to react flexibly to the significant changes which may come about and which may at this stage be difficult to predict.

Selective Action

6. The Secretary of State has at present a power to take action to reduce the rate of any local authority planning "excessive and unreasonable" expenditure. The Green Paper (para 8.41) envisages this continuing with the reduction being made in the community charge instead of the rate. It is proposed that a similar procedure should be followed, including approval of the House of Commons before a reduction is made in the community charge.

Conclusion

7. The Committee are invited to agree to the detailed proposals described. They are consistent with the Green Paper and in line with existing Scottish legislation on this subject, which is much less detailed than the English. In particular the Committee are invited to agree to:

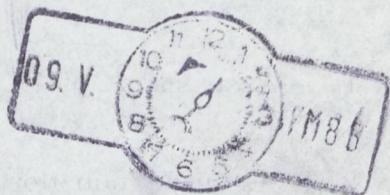
- i. a single revenue support grant with a needs element and a per capita element
- ii. the retention of non-domestic rates by local authorities in the interim period prior to a uniform Great Britain non-domestic rate poundage

- iii. an adjustment to the revenue support grant to take account of the variation in resources during this interim period
- iv. safety netting to take account of changes in grant during the transition to the new arrangements
- v. the continuation of selective action in cases of excessive and unreasonable expenditure leading to a reduction in the community charge.

EXAMPLE OF GRANT CALCULATION PROPOSED FOR INTERIM PERIOD FOR AN
IMAGINARY SCOTTISH REGION WITH ADULT POPULATION 200,000

1.	Assessment of Expenditure Need	£150 million
2.	Assumed non-domestic rate income	£50 million
3.	Resource equalisation by subtraction of non-domestic rate income from assessment of expenditure need to produce needs net of non-domestic rates (1 - 2)	£100 million
4.	Needs per adult ($3 \div 0.2$)	£500
5.	Needs per adult of lowest region	£400
6.	Needs equalisation by multiplying difference between imaginary region and lowest region by adult population. Needs grant of imaginary region = $(4 - 5) \times$ population or $(£500 - £400) \times 200,000$	£20 million
7.	Standard grant of all regions £300 per adult multiplied by adult population of region	£60 million
8.	Total revenue support grant entitlement Needs element plus standard element $(6 + 7)$ or £20 million plus £60 million	£80 million

The safety net is not included in this calculation since it will depend on a number of factors in particular the grant received by the authority in the preceeding year.



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Secretary of State for Trade and Industry

RESTRICTED

30 May 1986

The Rt Hon Malcolm Rifkind MP
Secretary of State for Scotland
Scottish Office
Whitehall
London SW1A 2AU

NBPM.

Dear Malcolm

"PAYING FOR LOCAL GOVERNMENT": 1986/87 SCOTTISH LEGISLATION

FILE WITH DN

Thank you for copying to me your letter of 8 May to Willie Whitelaw, inviting comments on your proposals for grant arrangements and non-domestic rates.

I have seen a copy of Kenneth Baker's response of 21 May and I very much agree with the points he made.

I am copying this letter to the recipients of yours.

[Handwritten signature]

PAUL CHANNON

Paul

LOCAL GOVT Rating PTH.



papers please

Prime Minister

22 May 1986

Agree to write as proposed?

MR NORGROVE

*DRN
2/6*

*Too soon - prefer
discussion first
not*

PAYING FOR LOCAL GOVERNMENT: 1986-87 SCOTTISH LEGISLATION

Malcolm Rifkind and the DoE are corresponding about the arrangements for grants and non-domestic rates in the Scottish legislation.

The DoE letter makes three points.

Capping non-domestic poundages for an indefinite period

We are planning to move to a non-domestic rate uniform across the whole of Great Britain. Scottish non-domestic rates tend to be higher than in England. The Scots therefore need to work out a way of financing a reduction in their non-domestic rates without getting subsidies from English taxpayers or ratepayers. This is a tricky task, and the DoE are afraid that the Scots will shirk it and never get beyond the interim solution of capping the non-domestic rates.

Capping non-domestic rates is fine as a temporary measure: it does ensure that variations in spending will fall on the community charge. But the Prime Minister might want to back the DoE in pressing the Scots to think carefully about what comes after it.

Local authority responsibility for collecting non-domestic rates

It would be very odd if local authorities ceased to be responsible for collecting non-domestic rates. We don't want central government to get into this game. The DoE are right to be worried. I recommend the Prime Minister back them.

Can authorities levy less than the poundage set?

This is an interesting possibility. Imagine that a prudent council is elected in place of a spendthrift one. They cut their expenditure so much that they can lower the non-domestic poundage to below what is required for the central pool and meet the balance from their low-rated householders. They can thus encourage business into their area. This is attractive, and the DoE are wrong to want to rule it out.

Their worry is that a new spendthrift council can increase their spending without increasing the community charge if they have headroom on the non-domestic rate. This problem can be met by a requirement that non-domestic poundages should not be increased suddenly by more than the rate of inflation. I recommend that the Prime Minister propose this compromise so that local authorities remain free to levy less than the set non-domestic poundage.

David Willetts

DAVID WILLETTS

LOCAL GOVT

RATES

PTY

cc BF



2 MARSHAM STREET
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01-212 3434

My ref:
Your ref:

CF
Pse ask
Poundage unit
of any
comments.

21 May 1986

Jim Malahan

PAYING FOR LOCAL GOVERNMENT: 1986/87 SCOTTISH LEGISLATION

Thank you for copying to me your letter of 8 May to Willie Whitelaw, with which you enclosed a paper setting out your proposals for grant and non-domestic rates. I have no comments on your grant proposals, but three on your proposals for non-domestic rates.

While I understand your wish to move to a GB poundage and harmonize the valuation system, I must continue to reserve my position at this stage about the implications for England. When this subject was discussed by E(LF) on 19 December, the conclusion was that "there was a strong view that the existing financial balance between Scotland, England and Wales should not be disturbed".

Rather than introduce a uniform poundage, the CBI in England are arguing for permanent capping on non-domestic poundages. Unless it is presented very carefully, an announcement that you intend to do just that for an unspecified, but perhaps lengthy, period will cause people to doubt our commitment to uniform poundages. If the harmonization of valuation systems north and south of the Border is to be the public reason for the interim position in Scotland, we should be making efforts to identify what changes are needed to existing practices, and how those changes could be achieved. Ideally, we should consider whether anything could be done in the run-up to the 1990 re-valuation.

The arrangements you describe in paragraph 4 of your note for sharing out non-domestic rating capital will have broadly the same practical effect as those set out in the initial Green Paper, although the presentation of what is happening will be more difficult. I have two worries, however. First, you imply that once non-domestic rate income is centrally pooled, local authorities must cease to be responsible for collecting it. That would mean central government setting up separate collection arrangements, with all that entails. I would certainly not want to go down that path for England.

Secondly, you seem to envisage authorities being able to levy less than the poundage set. Variations in the extent to which authorities make use of this facility from year to year would undermine the link between changes in spending and changes in the

level of charge. I also wonder whether in setting the poundage to be levied by authorities, it might be better to start to narrow the gap between the high rated and low rated areas by expressing the annual increase in rate as a flat rate poundage amount, rather than a percentage of the previous year's rate.

Our officials are already working closely together. I suggest that they should also take on board the points in this letter.

I am copying this to Willie Whitelaw, to members of E(LF), to Kenny Cameron and to Sir Robert Armstrong.

Kenneth Baker

KENNETH BAKER

LOCAL GOVT: Rating reevaluation: Pt 4



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Oddi wrth Ysgrifennydd Gwladol Cymru

The Rt Hon Nicholas Edwards MP

From The Secretary of State for Wales

14 May 1986

NBP

John Nelson

RATES REFORM

In your letter of 8 May to Willie Whitelaw you invite colleagues to comment on your draft E(LF) paper summarising the proposed arrangements for grant and non-domestic rate income in Scotland.

In general I believe that what you propose is fine. However, there are two aspects which I think it would be useful for officials to discuss prior to issuing detailed instructions to draughtsmen.

First, there is the implication in paragraph 4 of your paper that when a uniform non-domestic poundage is introduced the actual collection of non-domestic rates will be taken out of local authorities' hands. This is not my understanding of what is proposed in the Green Paper - see, for example, paragraph 2.35 of the Green Paper - and any such arrangement would present considerable administrative and presentational difficulties for us.

Secondly, the idea of allowing for a measure of resource equalisation during the interim period, combined with the use of existing powers to safety net grant, appears to be slightly at odds with Green Paper thinking. I would have thought that exactly the same result could be achieved by deploying just one safety net - as suggested in the Green Paper - covering not only the changes flowing from the capping of business rates, but also shifts in grant. The advantage of an all-embracing safety net of this sort is that it is easier to understand and more perceptible.

Finally, while we all agree that at some stage a Great Britain-wide non-domestic rate poundage would be desirable, the Green Paper deliberately does not quote a target date for this. It is, therefore, quite possible

/that in the ...

The Rt Hon Malcolm Rifkind QC MP
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that in the early years of the new system there will be a separate uniform non-domestic rate poundage in each country. However, the absence of a target date for harmonisation of the business rate throughout Great Britain should not, of course, affect the drafting of your Bill.

/ Copies of this letter go to Members of E(LF), Kenny Cameron and to Sir Robert Armstrong.

Jan Cameron
Robert Armstrong

ORN

Please see SS.Scotland to LPC
of 8.5.86 - at the top of
the file.

David Willetts verbal comment
is as follows

"It is entirely consistent
with the Green Paper proposals
and therefore should cause
no problems for the Prime
Minister"

Amanda
12.5.86