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From the Private Secretary

9 April 1990

Dear John,

RPI AND THE COMMUNITY CHARGE

We spoke this morning about the Prime Minister's extreme concern about the projected RPI figure for April. I attach the minute dictated by the Prime Minister: she would be grateful if the Treasury could investigate urgently whether an instruction can be issued that from 1 April (pending changes to the RPI to bring it into line with other countries) the community charge reliefs - that is both community charge rebates and community charge transitional relief - should be taken into account in working out the community charge component of the RPI.

The Prime Minister would also be grateful if the Treasury could examine the idea of a community charge surcharge for those on high incomes.

We agreed that it would be appropriate to report back on changing the construction of the RPI figure for April at next Tuesday's discussion. The work on a community charge surcharge fits more naturally into the further consideration of the community charge. In the first instance, however, it would be appropriate to report the outcome of the Treasury's analysis to the Prime Minister.

I should be grateful if you would ensure that this minute, and the attached from the Prime Minister, are seen only by those with a strict need to know, and copied only with your permission.

*Yours**Barry*

BARRY H POTTER

John Gieve Esq
HM Treasury



10 DOWNING STREET

THE PRIME MINISTER

Personal Minute

No. M2/90

CHANCELLOR OF THE EXCHEQUER

Your minute dated 6 April, on RPI etc. contains such serious news that I don't think we can leave things as they are - the consequences are too devastating for all our policies.

To leave out of account the massive reliefs which reduce the community charge for several million chargepayers, flies in the face of commonsense. And that is how our backbenchers react when I discuss the matter with them. I think we should be justified in issuing an instruction that (pending changes in the RPI to bring it into line with other countries) the reliefs must be taken into account. The reasoning is clear - people are not paying the price (ie. charge) that is in the RPI; they are paying the charge less all reliefs.

This would also have repercussions on the treatment of rate rebate last year. I note from your minute that CSO is already considering revising downwards their estimate of the rates component last year. If that is so, they have had the RPI too high for a year and it should go down retrospectively. But assuming they are already recalculating the figure, they can quite easily include the rebates so that the new figure (rates less rebates) will compare with community charge less rebates including transitional and other reliefs.

This does make common sense. I would not advocate it otherwise. We may have to put down a resolution and debate it in the House, but we should have no difficulty in getting it through.

The alternative, (ie. to do nothing, because we have listened to technical arguments) would be much worse. An added attraction of this proposition is that an RPI adjustment would in any case have to be made to put our 'inflation' figures on the same basis as those elsewhere in the EEC. It would help from the point of view of joining the ERM.

May I raise one other point that came up obliquely at our community charge meeting when someone, I think it was Chris, raised the question of 'banding' the charge. It is clear that we have two problems on our hands:

- the charge is too high - we are already proposing measures to deal with that;
- it is thought to be unfair because the widely differing income groups all above relief levels pay the same charge. Our efforts to explain that the taxpayer pays 100 per cent of all the reliefs and the lion's share towards local expenditure, have not removed this feeling of unfairness. I feel we must do something about this.

Bearing in mind that the business rate is now collected centrally and distributed on a population basis, I suggest we consider something similar for top rate taxpayers. A possibility would be a personal surcharge applicable to all taxpayers whose preceding year's income was above say £50,000, of an amount equal to the average community charge over the whole country, or a fraction of a multiple thereof according to the net income level we select.

This sum would be collected centrally, that is in the ordinary way, by the Inland Revenue and distributed like the business rate. We accept an ability to pay test at the bottom, this would be a limited such test at the top. Problems - the step change at the relevant income level, although the average community charge would not be an enormous sum at those levels of income.

Moreover, there is a risk that the modest amount we propose could

be increased during its passage through the House. Advantage - the higher income would pay more towards community charge and it would be equitably distributed.

Details would need to be worked out, eg. relief when income falls as in retirement year or other circumstances.

This proposal could either be a transitional scheme (the mirror image of the transitional relief) or a permanent feature. Also we have a transitional approach to business charge - why not a similar one for the domestic charge?

On this scheme it doesn't matter where you live because the whole thing is distributed centrally and therefore the local authority need know nothing of one's personal financial circumstances.

The whole proposal would only work provided the 'surcharge' is a tax and does not come on the RPI. Otherwise it would only add to our RPI problems.

I know there are lots of snags but we must try to remove the unfairness feeling. Could I have your reaction? I am about until Thursday morning for any discussions required. Or we could talk on the phone.

Nargans halber

9 April 1990