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P 02783

PRIME MINISTER

COMMUNITY CHARGE: TRANSITIONAL ARRANGEMENTS

[(E(LF)(87)28, 29) & 32]

DECISIONS

The Sub-Committee needs to decide on transitional arrangements for introducing the community charge in England and Wales, and in particular -

a. whether to confirm its earlier decision that there should be a phased transition from domestic rates to the community charge, or (as Mr Ridley and Mr Walker would prefer) to agree that the community charge should be introduced in full in 1990/91;

b. how fast the transition should be, both as concerns any phased abolition of rates and the removal of safety net protection for different areas (Mr Ridley argues that if there is a transition, it should be 3 years at most; the Chief Secretary bids for 5 years);

c. whether special arrangements should be made to deal with the very high potential community charge levels in London, possibly through preferential access to the national non-domestic rate (NNDR).

BACKGROUND

2. During the preparation of the Green Paper "Paying for Local Government", E(LF) became concerned about two sorts of changes

which would follow from its proposals. First, the very substantial shift in the burden of domestic taxation from the South to the North of the country. To limit this shift, E(LF) agreed a system of safety nets, operated through the grant system or NNDR pool, to prevent any immediate changes in the burden of domestic taxation as between local authority areas. The grant adjustments would be fixed in cash, and would diminish only as they were eroded by inflation. Second, E(LF) became concerned about changes in the tax burden on individuals in any area. To limit these changes E(LF) agreed a phased transition from domestic rates to the community charge, with a period of up to 10 years during which both systems would run in parallel. Both these transitional arrangements were included in the Green Paper.

3. During the Parliamentary consideration of the Abolition of Domestic Rates etc. (Scotland) Bill there was pressure, backed by Scottish Councils, to move straight to the full community charge in 1989/90. E(LF) agreed on 24 February (E(LF)(87)2nd Meeting) to drop dual operation of the two domestic tax systems, and the Bill was amended accordingly. However, safety net arrangements are still proposed to limit shifts in the burden of taxation between areas in Scotland.

4. At E(LF) on 2 July (E(LF)(87)11th Meeting) Mr Ridley proposed to follow the Scottish example by introducing the community charge in full in 1990/91, and also to dispense with the general safety net on changes between areas. In their place he proposed a limited scheme of safety nets to mitigate only the highest community charges, principally in London. However, E(LF) did not accept these proposals, and considered that it was essential to retain transitional arrangements, including a phased transition from rates to the community charge and a general safety net to limit changes in average domestic tax bills. But they agreed that there should be further consideration of the precise period of the transition, and also asked Mr Ridley to look at the possibility of further special arrangements for London, including a purely local element of non-domestic rates or a larger allocation for London from the

NNDR pool.

MR RIDLEY'S PROPOSALS

Community Charge

5. Mr Ridley's paper returns to his earlier proposal to abandon a phased transition from rates to the community charge. He argues that running both systems together has formidable disadvantages: it keeps domestic rates in place for a considerable period; it is expensive; it is not cost effective; and it will mask accountability and confuse domestic taxpayers. He therefore recommends, despite the earlier decision of E(LF), that you should now agree to move straight to the full community charge as in Scotland. However, he recognises that E(LF) may not feel able to accept this recommendation: in that case he recommends a short transition of no more than 3 years, under which rates would disappear completely on 1 April 1993.

Safety Net

6. Mr Ridley also proposes a much shorter transition to the full effects of the new system as between areas and regions. IF colleagues agree to move straight to the community charge, he proposes then phasing out safety nets over 3 years. This is his preferred option. If, however, rates are phased out gradually (3 years at most in his view), he suggests that the safety net should be phased out pari passu with them. He points out that to allow the safety net to be eroded by inflation would only imply decline by a third in real terms after 10 years.

London

7. Mr Ridley argues against any special arrangement to keep down community charge bills in London by providing a larger contribution from non-domestic rates. He points out that the safety net will provide London with about £410 million of transitional assistance

in 1990/91. A further subsidy from non-domestic ratepayers would mean either non-domestic rates in London above the uniform national figure, or a reduced NNDR pool for distribution to all other areas.

MR WALKER'S PROPOSALS

8. Mr Walker also proposes to follow the Scottish example, by abolishing domestic rates completely in 1990/91, and to retain safety nets to prevent changes in the average domestic tax bill in different areas in Wales. But unlike Mr Ridley, he sticks with the Green Paper proposal of a safety net fixed in cash terms, and retained for at least 10 years.

THE CHIEF SECRETARY'S PAPER

9. The Chief Secretary argues strongly in favour of a transition from rates to the community charge. He advocates 5 years (as for the NNDR) with the safety net phased out over the same period. He argues that this is essential to prevent perverse effects on community charges during the period when the safety net applies, to smooth the transition to the new system. He also disputes Mr Ridley's figure of £200 million for the cost of running rates in parallel with the community charge, and contrasts this with the earlier estimate of only £50 million. The key issue here is how far the two systems - and particularly enforcement - can be run jointly.

THE RELEVANCE OF ILEA

10. You had asked the Education Secretary to provide a paper for this meeting, setting out a breakdown of ILEA expenditure, so that you could form a view of how savings on that front would affect the transition problem in London. Mr Baker has not been able to produce that paper in time for the meeting, and the ILEA factor is now less important for Mr Ridley since he is proposing a safety net for the first three years. You should probably assume that savings on ILEA would not begin to show for the first 3 years or so of the

opting out regime, and would therefore not have much influence on the community charge levels that would face London charge-payers when a 3 year safety net was phased out.

VIEWS OF OTHER MINISTERS

11. Other Ministers will have personal views about the advisability of moving straight to the full community charge in 1990/91 - most members of the Sub-Committee spoke against this proposal at the earlier meeting. The Social Services Secretary also has a major Departmental interest, because of the implications for housing benefit. The Green Paper estimated (in 1984/85 figures) that introducing the community charge in full would increase the benefit caseload by about 1,170,000 (18%) and benefit costs by £100 million (4%). But both the caseload and cost implications would be somewhat lower with a phased transition. With the £50 first year community charge proposed in the Green Paper, they would be 880,000 (14%) and £20 million (1%) respectively.

MAIN ISSUES

12. Mr Langdon's minute of 10 July discussed the main issues which arise from both papers. In particular it covers the following:-

i. whether to reverse your earlier decision and agree that rates should be abolished completely in 1990/91 (paragraphs 8 and 9);

ii. whether to have a safety net alone if you do decide to move straight to the community charge (paragraph 10);

iii. how long the transitional period should be (paragraph 11);

iv. whether to introduce special arrangements for London (paragraphs 12 and 13).

13. Taking Mr Ridley's fall back position, there are effectively three proposals on the table:

	Rates/Community Charge	Safety Net
Mr Ridley	3 year transition	3 year transition
Mr Walker	Instant change	At least 10 years
Chief Secretary	5 year transition	5 year transition.

Mr Ridley's proposal certainly has substantial advantages; it offers the prospect of abolishing rates completely by 1 April 1993, and also bringing the full distributional effect of the new system into place by that date. But this means some fairly sharp changes in individual tax bills between years (exemplified in table 4 to Mr Ridley's paper). Mr Walker's proposal would prevent such large changes as far as Wales is concerned, but at the cost of a very slow movement towards the full Green Paper system. It would of course be possible to have different arrangements for England and for Wales, as you have already agreed for the new grant system. Nevertheless, the Sub-Committee may want to express a definite preference on the speed of transition, which should then apply in both England and Wales. In reaching a decision you will obviously want to take account of political as well as practical considerations, including the timing of elections.

TIMING

14. A decision on whether or not to have a phased transition from rates to the community charge will have to be reflected in the legislation. The Bill has to be ready for introduction in the Autumn. If drafting is not seriously to be delayed, you therefore need to reach agreement <u>before the Recess</u>. You will also need to decide on the same timetable what general arrangement for safety nets you want, although the powers could be drawn fairly wide, leaving the exact form and speed of the transition to be decided later.

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HANDLING

15. You will want to ask the Environment Secretary, the Secretary of State for Wales and the Chief Secretary, Treasury to introduce their papers. The Social Services Secretary will want to comment on the implications for housing benefit of the transition from rates to the community charge. Other Ministers will also wish to comment.

J B UNWIN

13 July 1987
Cabinet Office