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c.B. / 4.4.90

PRIME MINISTER

COMMUNITY CHARGE: TRANSITION

[E(LF)(87)42]

DECISIONS

1. E(LF) agreed in July that in England (but not in Wales or Scotland) there should be a phased transition from rates to the community charge over four years after 1 April 1990 ("dual running"). The Environment Secretary now seeks agreement to a change of policy which would allow individual local authorities in England to choose a shorter transitional period, or to opt out of dual running altogether. He does not however propose to announce this change immediately. His preference is to announce it as a concession during Second Reading of the Rates Reform Bill, and to introduce the necessary provisions by way of amendments, probably at Committee Stage. If the meeting agrees with Mr Ridley's general approach, you will wish to satisfy yourself that this timing of the announcement is politically viable.

2. Alternatively, the meeting may wish to see more information before taking a decision. Such information could be exemplifications of the rates and community charges if various local authorities exercised the option that Mr Ridley proposes, compared with those under present policy. The meeting might also wish to see more information about possible criteria for circumscribing the right to opt. But you will wish to bear in mind that any scheme more refined than Mr Ridley proposes is likely to be difficult and time-consuming to draft.

3. Finally, you should be aware that all these proposals can only bear on the lower-tier, tax-gathering, authorities, and not on the upper-tier authorities that precept on them. This point may not be of prime political importance, but it is not mentioned anywhere in the paper.

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BACKGROUND

4. E(LF) considered the transitional arrangements for the introduction of the community charge at a number of meetings during July (E(LF))(87)11th, 14th, 17th and 19th Meetings). The Green Paper "Paying for Local Government" had proposed long transitional arrangements (lasting for up to 10 years) involving both a phased transition from rates to the community charge ("dual running"), and safety net arrangements operated through Exchequer grant to moderate the large shifts in tax burdens between areas resulting from the new system. At the July meetings, Mr Ridley proposed abandoning these arrangements, and introducing the community charge in full in 1990/91. There would have been no dual running, and no transitional safety nets. However, these proposals were strongly contested by the Chancellor of the Exchequer, who was concerned both about the sharp changes in tax bills which they would imply for individuals, and about the implications of relying on an untested tax to meet a substantial proportion of local authority expenditure in its first year.

5. E(LF) finally agreed to retain full transitional arrangements in England, but ^{said} that these should be phased out over a much shorter period than had been envisaged in the Green Paper. The agreed arrangements were -

i. The community charge would be introduced at the rate of £100 per adult throughout England in 1990/91, and rates would be reduced by a corresponding amount.

ii. There would be a full safety net in 1990/91, to prevent any shift in the balance of local domestic taxation between areas in that year.

iii. Both the remaining amount of rates and the transitional safety net would be phased out entirely over the following four years, so that the new system would apply in full in 1994/95.

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The Rates Reform Bill is being drafted to provide for this transitional scheme in England. However, different arrangements have been agreed for both Scotland and Wales. In Scotland the community charge will be introduced in full in 1989/90, and the same will apply in Wales from 1990/91. But in both countries there will be a transitional safety net.

MR RIDLEY'S NEW PROPOSAL

6. Mr Ridley now proposes to allow individual local authorities to opt out of one part - dual running of rates and the community charge - of the transitional arrangements agreed earlier. They would have three options:

i. To adopt dual running for the full four year period. This would be an expensive option, because they would need to collect both rates and the community charge throughout the transitional period. (E(LF) earlier recognised that this might cost three times as much as collecting rates alone, and 50 per cent more than collecting the community charge alone). However, individual tax payers in their area would be protected from the very sharp changes in individual tax bills which would otherwise occur (eg for people paying the community charge for the first time, and for those with very low rate bills).

ii. To adopt a shorter period of dual running, eg two years. Higher costs of collection would be incurred for a shorter period, but individual tax payers would have a correspondingly shorter period to adjust to changes in their tax bills.

iii. To introduce the community charge in full in 1990/91. This would minimise collection costs. But individual tax payers in each area would receive no protection from sharp changes in tax bills.

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7. Mr Ridley does not propose to give authorities any option about the application of the safety net. An authority which opted to move straight to the full community charge in 1990/91 would get the same safety net treatment as if it had retained dual running. This means that an authority with high rateable values will pay into the safety net arrangements from 1990/91 to 1993/94, as if it were still raising a proportion of its revenue from rates. If it opts to dispense with dual running, it will need to levy a high community charge in 1990/91. This will be the position of many authorities in the South-East, eg in Surrey. Conversely, an authority with low rateable resources will get a large benefit from the safety net arrangements, and if it opts to avoid dual running will be able to charge a very low community charge in 1990/91. This will be the position of many authorities in the north, eg Barnsley and Burnley. It was effects of this sort which persuaded E(LF) in July that the transitional arrangements should incorporate both a safety net and dual running and not a safety net alone as Mr Ridley at one point proposed. (Similar effects will occur in Scotland and Wales as a result of adopting a safety net but no dual running. However the range of variation in rate bills is much lower in these two countries than in England, and the problems are therefore much smaller).

MAIN ISSUES

8. Mr Ridley believes that his new proposal will be seen as a concession and will ease the passage of the Rates Reform Bill through Parliament and the general introduction of the community charge. He is responding to representations which have made to him by local authorities and MPs, and particularly to the concerns expressed at the Party Conference. You will have formed your own view about the force of what was said at the Conference. But before you agree to Mr Ridley's proposal, you will want to consider the advantages and disadvantages for all those affected, including domestic tax payers as well as local authorities.

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9. Local authorities are likely to welcome Mr Ridley's proposal. It gives them an option which they did not have under the earlier proposals. They can decide whether or not they want dual running, and for what period, up to a maximum of four years. Many are likely to see substantial advantages in avoiding dual running: that will minimise their costs, and simplify the major administrative task of switching over to a new tax system, which is bound to tax their staff resources. The local authorities have a very effective lobby in Parliament, and if they support Mr Ridley's new proposal it may well ease the passage of the Bill.

10. For local tax payers the advantages of the new proposal are far less clear cut. Local authorities may choose to exercise the new option for their own financial and administrative advantage rather than in the interests of tax payers. Some domestic tax payers will of course benefit from the exercise of the new option, particularly those with high rate bills who stand to pay a much lower community charge. But many others will face sharp increases in their tax bills, particularly non-ratepayers and those with very low rate bills at present. The operation of the safety net will result in some perversely high charges in what would otherwise be areas with low community charges eg £393 per adult in Chiltern in Buckinghamshire. It was such implications for domestic tax bills which earlier convinced E(LF) that it was right to have dual running as well as a transitional safety net. These considerations may carry less weight in Parliament than the well-articulated concerns of local authorities. But they may come to the fore in 1990/91, with the result that the introduction of the community charge is that much more difficult and controversial.

11. Mr Ridley will argue that if the option to avoid dual running does lead to substantial losses for some tax payers in 1990/91, the local authorities concerned will take the responsibility. However, this message may be a difficult one to get across. The Government will inevitably be seen to carry the major responsibility for the introduction of the community charge as a whole. You will want the meeting to balance the immediate political advantages of giving

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local authorities more flexibility against the danger of greater opposition to the introduction of the community charge in 1990/91. The meeting may wish to see some exemplifications of possible scenarios in 1990/91 before this question is decided.

12. If you agree to Mr Ridley's basic proposal, you could still seek ways to limit the danger of very sharp changes in tax bills in 1990/91. One way to do this would be to restrict the new option to local authorities which met certain criteria - eg that the community charge resulting from the option was below a certain threshold level. However, Mr Ridley rejects this possibility. He believes that it would be too difficult to develop such criteria, particularly given that authorities would have to make their decisions on dual running well before 1 April 1990. He also argues that to set criteria would exclude some Conservative authorities who might resent the fact that they could not exercise the option. But there are also arguments in favour of restricting the right to opt. In particular, an unrestricted option could lead to some very high community charges in areas with high rate bills. Camden Borough Council, for example, might well see political advantages in opting to go straight to the full community charge in 1990/91, in the belief that the Government would take the odium for the very high charges which resulted. You may therefore wish to ask Mr Ridley to investigate the possibility of restricting the option to authorities which meet certain criteria, with a view to preventing the imposition of very high community charges in 1990/91. There is, however, a real risk that anything much more complex than the simple scheme now proposed would put too heavy a load on the draftsmen.

Implications for the Uprating of Income-Related Benefits

13. You will also want to consider the implications of Mr Ridley's new proposal for income-related benefits. E(LF) agreed in July that income-related benefits should be uprated to take account of the average liability of claimants to meet the 20% minimum contribution to rate bills from 1 April 1988, and to the community

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charge when that is introduced. An increase of £1.30 in income support rates for 1988/89 has now been agreed. The Social Services Secretary will shortly be bringing a paper to E(LF) about the basis on which benefits should be uprated when the community charge is introduced. When the charge is fully in place, the appropriate allowances in benefits would be 85p for single people and £1.70 for couples on today's figures. But the position is complicated by the fact that the community charge will be introduced in Scotland a year earlier than in England and Wales, and by the different transitional arrangements agreed for the 3 countries. Mr Moore's paper will need to address this issue. But you should note that the problems will be made yet worse if individual local authorities in England can decide whether or not to operate dual running.

Form and Timing of an Announcement

14. Mr Ridley asks E(LF) to make a decision now on his new proposal. But, if it is agreed, he proposes to hold this concession in reserve until Second Reading on his Bill, and then to introduce the necessary provisions by way of Government amendments. You will wish to explore this carefully. To introduce a major piece of Government legislation and announce a key change of policy on Second Reading might attract comment. Indeed, if Mr Ridley's proposal is agreed now, there must be a danger that it will become public at some stage before Second Reading, and it might therefore be better for the Government to make an announcement as soon as possible. Drafting of the Bill is proving difficult, and Parliamentary Counsel would not welcome a decision to incorporate Mr Ridley's scheme in the Bill as introduced. But the scheme is simple and it might not be too difficult to draft. If it is adopted there would be everything to be said for having it in the Bill as introduced if that is attainable.

VIEWS OF OTHER MINISTERS

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15. The Chancellor of the Exchequer will almost certainly oppose Mr Ridley's new proposal. He will see it as an attempt to re-open the decision which was reached after very lengthy consideration in July. He will argue that it will result in very sharp changes in tax bills which will provoke considerable opposition to the community charge as a whole. The Social Services Secretary will be concerned about the implications for income-related benefits. A number of other Ministers without a direct Departmental interest are also likely to be concerned about the implications for tax bills (eg the Secretary of State for Trade and Industry and the Home Secretary). The Business Managers will have views about anything likely to delay the Bill, but also about the wisdom of taking a decision now but delaying its public unveiling until Second Reading (which will be just before or after Christmas).

HANDLING

16. You will want to ask the Environment Secretary to introduce his paper. The Chancellor of the Exchequer and the Social Services Secretary will wish to comment from a Departmental point of view. Other Ministers will also wish to contribute to the discussion.

R.T.W.

R T J WILSON

23 October 1987

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