PRIME MINISTER 25 February 1988

NON-DOMESTIC RATE TRANSITION

E(LF) agreed in April that a limit should be placed on the annual percentage increase in non-domestic rate bills when the national non-domestic rate (NNDR) is introduced in 1990. Nicholas Ridley is seeking agreement to announce that the limit should be 15% plus inflation.

Factors Affecting Rate Bills

Individual non-domestic rate bills will be affected by two factors:

- the move to a uniform poundage;

- revaluation of non-domestic rateable values.

In some areas, for example Kensington and Chelsea, the combined effects of these changes will be very substantial. However, the DoE will not be in a position to give an accurate estimate of the effect until, at the earliest, the end of the year. So if we want to take a decision to ease the passage of the Local Government Bill we shall be no better placed later on than we are now.

Assessment of Proposal

The proposed figure of 15% is higher than the interest groups representing those affected would like but would ensure that rates bills moved to their eventual level except where they need to more than double over the five year transitional period. The cost would be met by charging a premium, estimated to be about 10%, on the NNDR. Because there would still be some areas where rates bills would not have risen to their eventual level in 1995 there would still be a premium on the NNDR. But this would be small and could be almost completely unwound in the following five years.

We therefore see no reason to object to Nicholas Ridley's figure. Certainly a 10% limit would be too low. Whilst a 20% one would be less of a hostage to fortune and ensure that more of the change worked through in the first five years, the advantages are not so great as to outweigh the political advantages of achieving smooth passage for the Bill.

We also agree that a 10 to 15 year transitional period, as proposed by the interest groups, is too long. Similarly, the Chancellor's flexibility to determine whether the annual increase in the NNDR should be at or below the rate of inflation should not be hampered by an RPI-X formula. The cost of this would have to be met either through higher Government grant or through a higher than expected Community Charge - unless local authorities changed their habits and increase expenditure by <u>less</u> than inflation.

<u>Conclusion</u>

Whether or not to announce now the limit to be placed on the annual increase in rate bills under the NNDR is largely a political one. It would certainly be unsatisfactory to announce an increase below the 15% proposed by Nicholas Ridley but the slight loss of flexibility compared to announcing an increase of, say, 20% or postponing or a decision has to be weighed against the help that an announcement now of 15% would give to the passage of the Bill.

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