D

D

CCB/01.

PRIME MINISTER

P 03497

RSG SETTLEMENT 1990/91: SAFETY NET AND ILEA SPECIFIC GRANT

(E(LF)(89)4; minute of 3 July from the Secretary of State for Education; letters of 30 June from the Private Secretaries to Mr Ridley and Mr Major - not copied to other E(LF) members)

DECISIONS

1. There are two main issues: the safety net and the proposed specific grant for education in inner London.

2. The papers are now very confusing. You may find it helpful to go back to the basic questions:

i. how far losers should be protected. There are two options: full protection for losers in 1990/91 (the original proposal); or partial protection which would mean that, for instance, £26 per adult of the losses would feed through in year one. Both Mr Ridley and Mr Major now back partial protection. You will want to consider whether you agree.

ii. whether, if you back partial protection, there should be full protection for low rateable value (RV) authorities in the North. Mr Major proposes such a scheme, as part of the safety net. Mr Ridley has reservations about how such a scheme could be justified. But if it were adopted he would favour a specific grant rather than an adjustment to the safety net. You will want to decide whether there should be full protection for some authorities in the North, and if so how long it should last before it begins to be phased out.

iii. where the costs of the safety net should fall. The three main options are first, removing all gains up to a specified limit, eg £75 per adult (the original proposal); or second, removing a proportion of all gains, eg about 60% (the option favoured by the Chief Secretary); or third, a flat rate contribution from gainers and losers alike, eg £26 per adult (the option favoured by Mr Ridley). You will wish to decide which option is best.

iv. the mechanism for financing the safety net. Mr Major favours the original proposal for a self-financing safety net, operating entirely through adjustments to needs grant entitlements. Mr Ridley would prefer to use a specific grant, or what he calls "top-slicing" of needs grant, so that contributions to the safety net would not appear on community charge bills. This point is presentational. It would increase the community charge for standard spending, and would need legislation. These disadvantages may outweigh the benefits.

v. the details of the specific grant for education in inner London. These have been agreed between Mr Baker, Mr Ridley and Mr Major. But the combination of a needs grant and the safety-net may give rise to some perverse effects

MAIN DECISIONS

Protection for losers

3. The aim of the safety net is to protect domestic taxpayers in areas where the community charge will be higher than the average rate bill per adult. There are two main options for providing protection:

i. full protection. The main advantage of full protection is that it allows no losses to feed through in 1990/91. It holds down community charges in areas like central London and the North where there are concentrations of losing authorities, and it therefore makes a special scheme to protect community charge payers in these areas unnecessary. Its main disadvantages are that it is expensive, imposing greater burdens on areas which stand to gain; that it prevents any movement towards the eventual and correct level of community charges in losing areas in 1990/91; and that it therefore means sharper increases in charges in later years.

ii. partial protection, allowing eg £26 per adult of losses to feed through in 1990/91. The main advantages of this option are that it is less costly, so that gainers get more of their gains in 1990/91; and that all areas make some movement towards their eventual community charges in year one. The disadvantages are that community charges in sensitive areas like parts of inner London and the North are higher; and that special schemes to protect some of these areas may be needed.

4. The Government's original proposals provided full protection. This will be the basis of public expectations. But Mr Ridley and Mr Major both favour a move to partial protection, with losses of perhaps £25-26 per adult feeding through in 1990/91. You will wish to consider whether it would be right to adopt this option.

A special scheme for low RV authorities

5. If you decide in favour of partial protection for losers, the next question is whether there should be a special scheme to protect authorities with low rateable values in the North of England.

6. You will wish to decide whether there should be such a scheme. It would refund the losses of £25-26 per adult in qualifying authorities (perhaps those with average domestic rateable values below £135 per dwelling). The main advantage would be that it would reduce the community charge in a number of sensitive authorities, including some where £25 per adult would imply a large percentage increase in tax bills. The main disadvantages are the cost to the Exchequer of £70-100m; and the sharper losses which the authorities concerned would suffer in the remaining years of the transition. The presentation of the special scheme could also be difficult. Mr Ridley has sketched

out how the scheme might be justified. But he is likely to argue that the case is unconvincing, and that the scheme will be seen as a politically inspired fix. He may suggest that the money would be better spent elsewhere: for instance, to ease the burden of the general safety net.

Meeting the cost of the safety net

7. The cost of protecting losers from their full community charges has to be met by increased charges in other areas. There are three main options:

i. removing all gains up to a limit (eg £75 per adult with full protection for losers or £39 per adult with partial protection). This was the Government's original proposal, on which public expectations will be based. Its main advantages are that no gainers become losers, and that there is a limit on the contribution any area is asked to make to the safety net. Its main disadvantage is that the great majority of gains are reduced to zero in 1990/91, so that few areas see any benefit from the community charge.

ii. removing a proportion of all gains (eg 81% of gains to pay for full protection, or 57% to pay for partial protection). This is the option favoured by the Chief Secretary. The main advantage is that all gainers receive a proportion of their gains in 1990/91. The disadvantage is that some large gainers have to make very large contributions, which may exceed the maximum of £75 on which their current expectations are based (eg £108-165 per adult in Westminster).

iii. a flat rate contribution from all gainers and losers (eg £26 per adult with partial protection). This is Mr Ridley's preferred option. Its main advantage is that gainers get their full gains in 1990/91, less £26 per adult. There are no very high contributions like the £75 per adult which is already causing resentment in Westminster. The main <u>disadvantage</u> is that some modest gains are turned into losses, and modest losses are increased to £26 per adult. There are therefore more losers and fewer gainers from the new system in 1990/91.

8. <u>You will wish to consider which of these options provides the best way of meeting the cost of the safety net protection for the losers</u>.

Mechanism for financing the safety net

9. The legislation provides for the safety net to be implemented by self-financing adjustments to needs grant: losers would get more grant, offset by abating the grant of gainers. Mr Ridley now suggests that the safety net should instead be financed directly from money "top-sliced" from needs grant. This option is only available under Mr Ridley's preferred option of paying for the safety net by a fixed contribution (eg £26) from all gainers and losers. The sum involved - about £950m for partial protection - could be paid as a formal specific grant, or as a new element within Revenue Support Grant.

10. This proposal is essentially presentational. The main <u>advantage</u> is that the contribution to the safety net would not appear on charge bills. There might therefore be less resentment in the contributing areas (although they would be no better off in practice). A major <u>disadvantage</u> is that the community charge for standard spending (CCSS) would be higher: £301 per adult for partial protection. New legislation would also be needed in the current Local Government and Housing Bill. The necessary provisions would have to be introduced in the House of Lords, which might cause difficulties with Parliamentary procedure. The Chief Secretary opposes top-slicing for these reasons, and because he fears that with a higher CCSS authorities would be tempted to raise spending.

11. <u>You will want to consider Mr Ridley's proposal for top-slicing. You may conclude that the benefits are outweighed by</u>

the disadvantages.

Specific grant for education in inner London

12. Mr Baker's minute sets out more details of the specific grant proposed in Mr Ridley's earlier paper (E(LF)(89)3) to ease the abolition of the ILEA in 1990/91 and subsequent years. I understand that Mr Ridley and Mr Major are content with these proposals.

13. There is however an issue about the effect of the specific grant and the safety net taken together. The proposal is to pay the specific grant after the safety net protection has been calculated. This has the advantage of turning all the inner boroughs into gainers in 1990/91. But 7 of the 12 will be losers in the long run even if they get education spending down (Greenwich, Hammersmith, Lambeth, Lewisham, Southwark, Tower Hamlets and Wandsworth). Turning them into gainers in year one means that they will suffer even sharper losses in the remaining years of the transition. For example, the average tax bill in Greenwich would fall from £285 to £221-249 in 1990/91, but would rise to £579 over the next 4-5 years.

14. Results like this could be avoided by paying grant before the safety net is calculated. The boroughs which are gainers would still see a net benefit from the specific grant (Camden, Hackney, Islington, Kensington and Westminster). But the big losers would simply have their losses limited by the general safety net: they would not become gainers. You may want to suggest that the grant should be paid before the safety net is calculated.

The tables

15. There are now two tables to look at: table 4 attached to E(LF)(89)4, and the new table attached to Mr Ridley's Private Secretary's letter of 30 June. You may want to concentrate on the following columns:

i. table 4, column 3, which shows the Government's original proposals, on which public expectations are based. Total protection for losers is financed by removing all gains up to £74 per adult.

ii. table 4, column 8 (identical to the new table, column 3) which is Mr Ridley's preferred option. Losses of up to £26 feed through, financed by a fixed £26 contribution from gainers and losers alike.

iii. new table, column 4, which is the same option plus a special scheme for authorities with low rateable values in the North, at an additional cost of £100 million.

RJW.

R T J WILSON
Cabinet Office
4 July 1989

CONFIDENTIAL

	Letter to the Prime Minister of 30 June					E(LF)(89)(4)					
	Column 3	Column 4	Column 5	Column 6	Column 7	Column 3	Column 4	Column 5	Column 6	Column 7	Column 8
	AEF £23.0bn £950m specific grant	AEF £23.1bn £100m extra specific grant	AEF £23.1bn 0,6,12% or £28 cont	AEF £23.1bn £2.3bn topsliced	AEF £23.1bn old net £65 max cont	Old net £74 limit No losses	Old net £39 limit £25 losses	E(LF)(89)3 Proposed safety net	No losses 19% of gains allowed	£25 loss 43% of gains allowed	All adults pay £26 to net
<u>Losers</u>											
Full protection?	N(£26)	N(£26)	N(£28)*	Y	Y	Y	N(£25)*	N(£25)*	Y	N(£25)*	N(£26)
Pendle exempt?	N	Y	Y	-	-	-	N	N	-	N	N
<u>Gains</u>											
Only above limit.	-	-	-	-	Y(£63)	Y(£74)	Y(£39)	-	-	-	-
Percentage contribution.	-	-	-	-	-	-	-	Y(84%)**	Y(81%)	Y(57%)	-
Flat rate contribution.	Y(£26)	Y(£26)	Y(£28)*	Y(£61)	-	-	-	-	-	-	Y(£26)
<u>Topslicing/Specific Grant</u>											
Appears on Charge Demand?	N	N	Y	N	Y	Y	Y	Y	Y	Y	Y
Legislation required?	Y	Y	N	Y	N	N	N	N	N	N	N

* Loss of up to this amount.

** Gains above £25.