



POLICY - IN CONFIDENCE

PRIME MINISTER

THE NON-DOMESTIC RATE POUNDAGE FOR 1991-92

When I announce at the end of this month the details of the local government finance settlement for 1991-92 I shall need to say what the Distributable Amount of business rates to be paid out to local authorities next year will be and therefore also what the national non-domestic rate poundage, or multiplier, will be. The presumption of the Local Government Finance Act 1988 is that the multiplier will rise each financial year in line with the annual increase in the Retail Prices Index in the previous September. It cannot rise by more but the Act gives the Treasury power to under-index it.

The CBI and other leading business organisations, especially in the retail sector, have argued for some measure of under-indexation. Their case is that rates, having no direct relationship to profit, can be an especially difficult burden for business to bear in an economic downturn, and that under-indexation will help businesses cope with the present difficult trading conditions. They also contend that the September RPI will be artificially inflated by the present surge in oil prices and that this should not be carried through into the rates base.

Against these arguments we have to set the fact that business as a whole has done well from the move to the NNDR. In the previous 10 years average non-domestic rate poundages in England rose by 3.2% a year more than inflation, that is by 37.4% more than inflation over the whole period. And in 1990-91, authorities have budgeted to increase spending by 12.5%, whereas business rates have effectively gone up by 7.6%. If this large increase in local authority spending had fallen partially on business, as under the old system, rather than wholly on community charge payers, businesses would have been paying over £1 billion more in rates this year than they are in fact



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paying. Even if authorities spend in line with our Total Standard Spending Assessment in 1991-92 (ie an increase of 7.1% over this year's budgets), businesses would, with a rate increase in line with inflation, still be better off next year than if we had not made the change and their rates had continued to reflect the successive increases in local authority spending. In any event, our decision on the poundage will not affect the 1991/92 rate bills of the 50% of properties which will still benefit from the transitional arrangements.

On balance, I have concluded that it would not be appropriate to use the power to under-index this year and Norman Lamont and other colleagues agree. Our view is endorsed by David Hunt, who proposes to increase the Welsh Poundage in line with the September RPI.

With full indexation, the business rate distributable amount for 1991-92 in England is likely to be around £12.5 billion, almost 20% higher than last year - with the result that nearly two-thirds of the increase in Aggregate Exchequer Finance will be met from the NNDR. I think that we must expect criticism from business, which may see this as an attempt to moderate community charge levels at their expense. And local authorities will complain when they discover that the level of RSG will fall by around 5% in cash terms compared with this year. The real terms increase in the Distributable Amount is in fact largely attributable to an abnormal level of buoyancy in the rate base as a result of late additions to rating lists between December 1989 and March 1990 which were not reflected in the Distributable Amount for 1990-91. This excess has to be carried forward and added to the Distributable Amount for 1991-92. We shall need to take special care to get this message across both to business and local authorities.



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I am copying this letter to Geoffrey Howe, Norman Lamont, David Hunt, Malcolm Rifkind, Michael Howard, Peter Lilley, Tim Renton and to Sir Robin Butler.

A handwritten signature in dark ink, appearing to read 'P. Howard'.

CP

October 1990

Approved by the Secretary of State
and signed in his absence.