24/1/DJS/1801/28

CONFIDENTIAL

Thanks. I w'd delete X, not that because rather policy objections to a surrogate local income tax are more important; administrative difficulties are also important & should be for general. N.

FROM: R FELLGETT

DATE: 12 January 1988

1. MR POTTER BHP 12/1

2. CHANCELLOR

Ch
Administrative diffs are also important (consider husband & wife problems for example)
AA

cc PS/Chief Secretary
Sir P Middleton
Mr Anson
Mr Kemp
Mr Scholar
Mr Hawtin
Mr Turnbull
Mr Culpin
PS/Inland Revenue
Mr A J Walker (IR)

**COMMUNITY CHARGE: BRIEFING LINE**

We and the Inland Revenue are being asked by DOE to comment on papers about proposals to make the Community Charge better related to individuals ability to pay. DOE have, for example, sought some comments on a paper they are preparing for Mr Ridley about Mr Michael Mates' ideas for a banded Community Charge; Mr Ridley is likely to draw on this in seeking to persuade Mr Mates to continue to vote for the Government on the Local Government Finance Bill (the Poll Tax Bill).

2. We are not happy with the way DOE tend to concentrate on the <u>administrative</u> difficulties of proposals of this type; in our view, <u>policy</u> objections to extra taxes on income are much more important. We do not propose to trouble you with all the detailed papers shown to us by DOE. But you will wish to consider the general line that we propose to take in response to DOE requests of this type.

**<u>The Community Charge and Ability to Pay</u>**

3. Mr Mates proposal is that basic-rate income tax payers should pay a basic Community Charge, with a lower charge for non-tax payers and a higher one for higher-rate income tax payers. Other suggestions for banded Community Charges have been put forward by Sir George Young and CIPFA and other ways of making the Community Charge more related to ability to pay could of course be devised.

4. If the Government ever went beyond commenting on proposals of this type, and seriously considered making some concession, the DOE fallback is likely to be a request for more grant, paid for by higher income tax. They would argue that this would increase the amount of local authority spending financed by progressive taxation, and reduce the Community Charge. New legislation, or amendments to the Local Government Finance Bill (or Act) would not be needed. In reply, we would of course argue that extra grant would simply fuel extra local authority spending. In addition, the proposed briefing line attempts to inhibit serious consideration of this option by emphasising the strong policy objections to adding to the burden of taxation on incomes, whether local or central.

**Proposed Line**

5. Our proposed line in comments to DOE about their analysis of proposals for banded Community Charges, therefore concentrates on three points:

(i) The Government's firm intention is to reduce, not increase, taxes on incomes, to improve incentives to work etc.

(ii) Any banded Community Charge would, if the amount an individual paid depended on their income band, be a crude local income tax. A crude approach is no better than a full local income tax; on the contrary, there would be very high marginal rates of tax (with consequent earnings traps and effects on incentives) at the point an individual's income moved from one band to a higher one.

(iii) The DOE presentation of the case for a Community Charge has, in effect, emphasised the policy advantages of a universal tax that is very visible to those who pay it. There are wider public finance arguments against giving local authorities a new, powerful revenue raising power. The fact that the Community Charge will not always be easy to pay is accordingly central to the accountability arguments to which the Government is publicly committed.

6. We may add points of the following type, although we suggest these should be very much secondary arguments:

(i) Such a proposal might have a sharp effect on one group of individuals. For example, Mr Mates' proposal would involve higher Community Charges for single, basic-rate taxpayers on modest incomes, including many nurses. (On the other hand, it would help groups like grannies looked after by their families, to whom we earlier drew attention.)

(ii) If the proposal requires Inland Revenue information, there may be significant administrative difficulties and problems over the confidentiality of Revenue data. (On the other hand, these could no doubt be overcome, probably at the expense of your other priorities for the Revenue, if the Government attached sufficient policy importance to them.)

7. In our view, DOE are prone to make too much of the administrative arguments. We will accordingly press them to concentrate on the main policy points mentioned above, and will decline to put substantial time and effort into investigating the administrative implications of policies that the Government does not intend to consider seriously. Nor do we intend putting substantial time and effort into checking the DOE figures exemplifying the effects of Mr Mates or others proposals; the Treasury and Revenue's priority should be given to modelling central taxation options for the Budget and later.

8. We do not, of course, intend to object to appropriate general DOE arguments that have been cleared with us in the past. Examples are that rates are poorly correlated with income so it is not unfair to replace them with a flat charge; rebates will be available for the poorest people; the very poorest households

(mainly single parent families) on average face decreases in rebated local tax bills; and grant paid for by central taxation, which is in aggregate more progressive than either rebated rates or rebated Community Charges, will continue to fund a higher proportion of local authority spending (in GGE terms, grant currently finances about 50%, and domestic rates only about 15%).

9. Subject to any comments you may have, we should be grateful for your authority to follow the proposed briefing line in our comments to DOE.

10. This advice has been discussed with FP and the Revenue.

Robin Fellgett

R FELLGETT

EXTRACTS FROM GREEN PAPER

3.38 "Alternatives to Domestic Rates" concluded that a flat-rate charge payable by all adults would meet all the technical criteria described in paragraph 3.7. It would be capable of producing a yield equivalent to that of rates, would be suitable for all tiers of local government, and would be conducive to proper financial control. But, in the White Paper, the option of introducing such a tax was rejected. The major objections put forward were operational:

> "... the tax would be hard to enforce. If the electoral register were used as the basis for liability it could be seen as a tax on the right to vote. A new register would therefore be needed but this would make the tax expensive to run and complicated, particularly if it incorporated a rebate scheme."

These problems are not insuperable. In view of the overriding importance of increasing local accountability through the introduction of a community charge they must now be tackled. Operational issues are considered briefly below and in more detail in Annex G.

## Transition

3.39 The move from rates to a community charge will inevitably affect the personal finances of households since single-adult households gain at the expense of multi-adult households. The Government considers that the change should be made gradually by introducing the community charge initially at a low level. In the first year of the new scheme rates would be reduced – by, say, an amount equivalent to the yield of a £50 per adult community charge. That would mean that the overall position of the average two-adult household would be broadly unaffected: their rates would go down by about £100, but they would have to pay an additional £100 – £50 per adult – in community charges. In some authorities where rate bills are low, a £100 reduction in rates would be a large proportionate reduction. In other authorities, mainly in London and South East England where some authorities have domestic rate bills in excess of £500 per adult – over £1000 a year for a two-adult household – it would be a much smaller proportionate cut and rates would continue to meet a large part of the local tax bill. All those paying local taxes for the first time would however face a similar bill, and there would be a similar *cash* reduction in rate bills across the country. And in all areas single householders would pay less, and households with more than two adults would pay more, towards the cost of local services.

3.40 In subsequent years any additional local revenue would be raised through the community charge. That would ensure that the cost of extra spending would be met in full by all local residents. There would remain, however, in all authorities some residual rate burden. It would be possible to freeze this sum, and leave it frozen until it constituted a sufficiently small proportion of the total local tax bill to be wound up. But that would mean that rates would continue well into the 21st century. The Government's objective is to replace domestic rates entirely within a reasonable timescale.

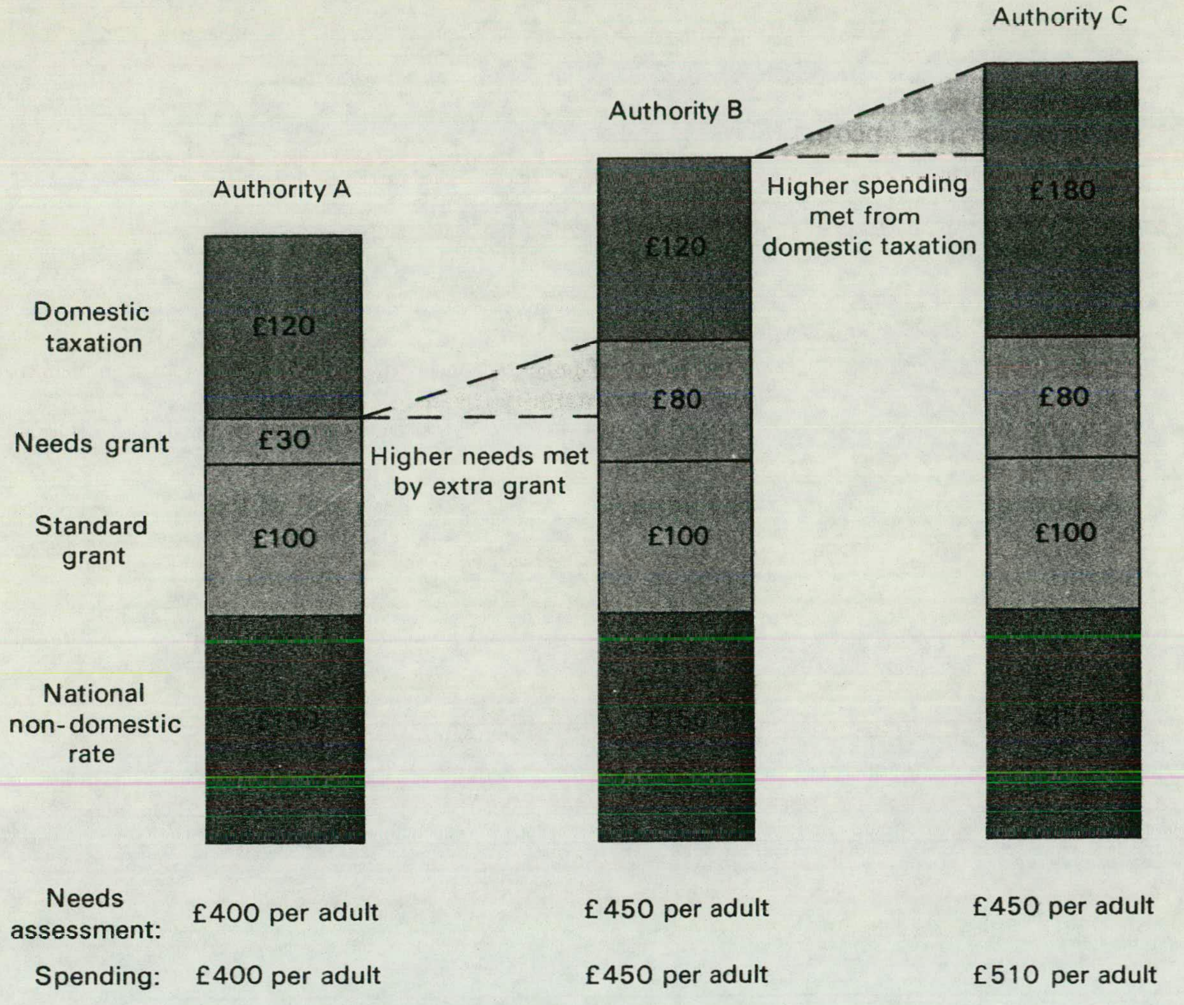
3.41 But people will need time to adjust. It is reasonable to expect domestic rates to have been phased out completely within 10 years of the introduction of the new system. In order to achieve this, it will be necessary to require periodic transfers from rates to the community charge. In Scotland and Wales, and in parts of England where rate bills are not high it will be possible to move relatively quickly. But in parts of England where there are higher rate bills a longer period of adjustment will be necessary. This will mean that rates will disappear in some areas before others. The arrangements for the transition in Scotland and Wales are discussed in Chapters 8 and 9 respectively.

3.42 Annex E considers the impact of these proposals on the housing market and concludes that any effects on the price and supply of housing arising from the abolition of domestic rates are likely to be small and spread over a long period.

## Operational issues

3.43 As paragraph 3.38 made clear, the previous examination of alternative local taxes concluded that the major objections to a new flat-rate charge were operational. The Government recognises that there would be problems in any move away from a tax on property to a personal tax. This would, of course, apply just as much to local income tax, for example, as to the community charge. Residence would have to be defined and people would have to be registered for the tax. Since the tax is not a tax on the right to vote – and would be paid by people such as foreigners who do not have the right to vote in UK elections but who benefit from local services – the Government proposes that there should be a separate register for this purpose. A separate register would also be necessary because, unlike the electoral register, the new community charge

Figure 14: THE GRANT SYSTEM AND DOMESTIC TAXATION




All figures are per adult

## The effect on local tax bills

4.40 The Government's proposals:

— that there should be a new grant system under which all marginal changes in spending are met by local domestic taxpayers;

— that the proceeds of non-domestic rates should be pooled and allocated as a constant amount per adult to all authorities;

— that there should be no other form of resources equalisation

would mean that some authorities would have to finance more of their spending from their domestic taxpayers than at present. In other areas the burden of domestic taxation would be less than it is now. Low spending authorities with high domestic rateable values would gain most. High spending authorities would lose, and so would authorities with low domestic rateable values.

4.41 In the bulk of authorities, the size of the changes would be small. But, in a small minority of cases, changes could be significant. And these effects would be superimposed on changes in the pattern of household bills *within* areas resulting from the gradual introduction of a community charge.

4.42 Allowing the effects of the grant and non-domestic rate proposals to feed through immediately, or within a very few years, would end the confusing situation that exists at present where domestic tax bills are lower in some high-spending areas than they are in authorities that spend much less. But the Government is mindful of the fact that householders have taken on commitments on the basis of the present patterns of local taxation. It would be unreasonable to disrupt that pattern too severely or too quickly.

4.43 The Government therefore envisages that special arrangements would be introduced to avoid any significant shifts in the burden of local taxation *between* local authorities on moving to a new system. These arrangements would take the form of a "safety net", which would prevent changes in authorities' income in the first year of the new system arising from the structural changes to the grant and non-domestic rate arrangements proposed in this Green Paper. The method of setting the safety net would ensure that authorities could not benefit from any increase in expenditure between now and the introduction of the new arrangements. And the amount of an authority's safety net entitlement would be fixed in cash terms so that its real value would progressively decline. Changes in the balance of local taxation *within* a local authority, arising from the widening of the local tax base by the introduction of the community charge, would begin to feed through immediately. So would the effects of any *increases* in spending. But under these arrangements for the same level of spending under the new system the average level of an authority's local tax bills would be virtually unchanged. Once the new system is in operation and sufficient time has elapsed to permit a proper assessment of its impact and effects, the basis of the special arrangements could be reviewed.

4.44 A more detailed account of the impact of the new system and of the design of the special arrangements is given in the next chapter. Chapters 8 and 9 discuss the position in Scotland and Wales.

## Specific grants

4.45 So far this chapter has discussed the main system of unhypothecated grants towards local authority expenditure. But a significant proportion of Exchequer support is paid in the form of specific grants. These make up about 20% of the grant total, amounting to some £2.8 bn in 1984/85. Police grant alone, which meets 50% of spending on the police service, cost about £1.4 bn in England in 1984/85. Contributions towards local authority spending on home improvement grants in England amounted to about £370m. At the other end of the scale, civil defence grant was worth only £8m, and that for sheltered employment only £9m.

4.46 Specific grants take a number of forms. Some are paid towards capital expenditure, some towards current expenditure and some, like slum clearance subsidy, towards a combination of the two. Grant rates vary from 100% in the case of some civil defence grants to 40% for spending on clean air. Some, like police grant, are paid towards actual expenditure on a complete service. Others, like the new education support grants, offer help towards service expenditure of particular types up to a total approved in advance. Specific grants can be either for programmes of expenditure or, as with transport infrastructure grant, for particular projects.

4.47 There will remain a role for certain existing specific grants, such as that for police expenditure. There may also be a case for some new grants, for example in the education field in support of the Government's objective of raising standards at all levels of ability. But, equally, extensive use of such grants could run counter to the approach set out in this Green Paper of local accountability and choice. And it is several years since there was a thorough appraisal of the role of specific grants. It is not clear that the existing pattern of grants can easily be justified in terms of current policy objectives.

4.48 The Government is therefore undertaking a separate review of the role of specific grants in the new system. In its view, specific grants may be justified where they are intended:

- to assist the delivery by local authorities of central Government policies of continuing national importance;
- to give special encouragement for a limited period to expenditure on activities or services which fulfil a specific central Government objective;
- to recompense local authorities for expenditure on activities carried out by them or other authorities at the request of central Government where there is limited or no local discretion over the expenditure incurred;
- to assist in the financing of activities that are not adequately covered by the proposed needs assessments.

4.49 In the Government's view, any existing or new specific grant must satisfy at least one of these criteria. But that would not, in itself, be sufficient to justify the continuation or introduction of a particular grant. It must be demonstrated, in addition, that the grant will

# Chapter 5: The combined effects of changes to local taxation and grant

5.1 Chapter 1 explained how the present Government's efforts to constrain local government expenditure had revealed some serious underlying flaws in the present system of local government finance. These flaws weaken the accountability of authorities to local people, with the result that many electors are indifferent to how much their local council spends or are encouraged to vote for ever higher expenditure on services.

5.2 The Government intends to tackle the problem not by increased central control of local authority expenditure but by taking action to remedy the weaknesses in the present system which undermine local accountability. Accordingly, Chapter 2 set out proposals for limiting local authorities' access to non-domestic rates, by setting a uniform national non-domestic rate poundage, and redistributing the yield among all authorities as a common amount per adult. Chapter 3 described proposals for transferring the burden of local domestic taxation from rates to a flat-rate community charge levied on all adults resident in an authority's area. Chapter 4 set out proposals for a new simplified grant system, consisting of a "lump sum" needs grant to compensate for differences in authorities' assessed expenditure needs and a standard grant, which would be distributed as a common amount per adult to all authorities. In addition, there would be special arrangements to ensure that in the first year of the new system authorities' income from grant and non-domestic rates would broadly be the same as under the old system.

5.3 These proposals are interrelated and together provide a comprehensive reform of the local government finance system, the main features of which would be as follows:

- non-domestic rates would still make the same overall contribution to aggregate local authority expenditure, but individual authorities would no longer be able to increase the rates paid by non-domestic ratepayers in their area so as to finance marginal increases in expenditure;
- the local domestic tax arrangements would be fairer; all electors would make some contribution to the expenditure of their local authority and this contribution would be more closely related to their use of local services;
- the grant system would be more stable and more comprehensible; the grant an authority received would no longer depend upon how much it spent and there would be no grant support for marginal spending; and the grant system — in combination with the new tax arrangements — would be based on equal tax bills for comparable levels of service rather than the equalisation of rate poundages, which at present causes significant disparities between the tax bills of different areas;
- the combined effect of the tax and grant reforms would be to ensure that the full costs or benefits of increases or savings in expenditure accrued to local domestic taxpayers; with the widening of the tax base and the much more understandable relationship between spending and tax demands, this would greatly improve the accountabilty of local authorities to their electors.

5.4 These reforms would have important distributional consequences, affecting the finances both of local authorities and of households and individuals. This chapter explains in general terms what those would be likely to be and describes how the reforms might be phased in over a transitional period so as to keep their distributional effects within reasonable and tolerable limits. It is chiefly concerned with England; Scotland and Wales are discussed in Chapter 8 and Chapter 9. Annex J describes the distributional effects in greater detail.

5.5 The modelling assumptions on which this Chapter and Annex J are based include actual local authority spending in 1984/85; Family Expenditure Survey data for 1980 to 1983 combined and repriced to a common 1984/85 level; full implementation of the proposals contained in the White Paper "Reform of Social Security" (Cmnd 9691) before the new arrangements come into operation; and an unchanged overall contribution from national taxpayers, non-domestic ratepayers, and local domestic taxpayers towards local authority spending. The assumptions are purely illustrative and simply show the effects of the measures proposed in the Green Paper, had they been in place in 1984/85.

## The effects on local authorities

5.6 Local authority income would be affected by two aspects of the proposals: the national pooling and redistribution on a per adult basis of the income from non-domestic rates; and the ending of resources equalisation. The effects of these proposals on individual local authorities would be determined by the level of their expenditure in relation to their grant-related expenditure (GRE) and the size of their rateable values per head of population.

5.7 Two types of local authority would gain extra income from the non-domestic rate and grant proposals.

i. *Low-spending authorities.* Authorities spending at a low level in relation to their GREs will be levying non-domestic rates below the national average and will thus get a below-average yield from their non-domestic ratepayers. National redistribution of the total yield of non-domestic rates as a common amount per adult (as proposed in Chapter 2) would increase the amount of non-domestic rate income going to these authorities.

ii. *Authorities with high domestic rateable values.* At present, the block grant system equalises differences in the rateable resources of authorities; grant is in effect transferred from authorities with high rateable values to those with low rateable values. The discontinuation of this process means that authorities with high rateable resources — which generally have high rate bills at present — would retain a larger proportion of their grant than hitherto. Since non-domestic rates would now be dealt with separately, this effect would depend on the level of an authority's domestic rateable values.

In practice most gaining authorities would tend to fall into both categories. They would be those which have fared worst under the present system, facing disproportionately high rate bills for a relatively low level of spending.

5.8 Conversely, two types of local authority would experience a reduction in their non-domestic rate and grant income as a result of the proposed reforms.

i. *High-spending authorities.* The limitation of non-domestic rate poundages and the pooling and redistribution of non-domestic rate income would mean a reduction in revenue to authorities spending above the level of their GRE and currently levying an above-average non-domestic rate poundage.

ii. *Authorities with low domestic rateable values.* Just as authorities with high domestic rateable values would gain from the discontinuation of resources equalisation, so authorities with low domestic rateable values would lose.

As with the gaining authorities, most of those losing would tend to lose on both counts. They would be those which have fared best under the present system, with disproportionately low rate bills for relatively high levels of spending.

5.9 On the basis of 1984/85 data, over two thirds of authorities in England would be likely to gain extra income as a result of the grant and non-domestic rate proposals. Most of these authorities would be in southern, eastern and central England, where spending in relation to GRE is generally low and rateable values relatively high. The minority of authorities which stand to lose grant and non-domestic rate income would mostly be in northern England where spending in relation to GRE tends to be high and rateable values are relatively low.

5.10 The effects of the proposals in London would be different. Total rateable values per head of population in many London authorities are substantially above rateable values elsewhere. This advantage would normally be offset by a reduction in grant under the resources equalisation arrangements of the block grant system. Successive grant regimes have however protected London from the consequences of full resources equalisation by allowing its authorities to retain a significant proportion of its resource advantage over other authorities, primarily to moderate the very high rate bills which would otherwise occur. Because resources equalisation has always been limited for London, its high resource authorities stand to gain relatively little in grant terms from the complete abolition of domestic resource equalisation. But many London authorities, particularly in inner London, are spending very significantly above the level of their GREs. They therefore stand to lose substantial amounts of revenue from the proposal to pool and redistribute non-domestic rate income. The combined effect would be significant reductions in non-domestic rate income for many London authorities which would be only partially offset by gains in grant.

5.11 The proposal to move the burden of local domestic taxation from rates to a community charge means that domestic tax bills in London would no longer be inflated by high rateable values. There would therefore in principle no longer be any case for affording London any special resource advantage over other areas. In the case of non-domestic rates, the proposed revaluation will ensure fair treatment for all non-domestic ratepayers across the country, although the need for some transitional arrangements in introducing both the new values and the new non-domestic rating system is recognised.

## Moderating the effects on local authority areas

5.12 Changes in the non-local income — ie non-domestic rate income and grant — of local authorities would inevitably affect the burden falling on their local domestic taxpayers. If an authority's total income from grants and non-domestic rates were to go down, average domestic tax bills would have to be higher to finance any given level of expenditure, and vice versa. In a number of authorities these changes would be likely to be significant.

5.13 As indicated in paragraph 4.43, the Government believes that such changes would be too disruptive in their likely effects on the personal finances of local taxpayers. It therefore proposes that there should be a "safety net" system of adjustments to the grant and non-domestic rate income of authorities, so as to eliminate changes in their income from these sources as a result of the proposed restructuring of the grant system and the proposal to pool and redistribute the yield of non-domestic rates. The safety net would take the form of offsetting adjustments to the grant and non-domestic rate allocations of authorities; it would effectively operate as a self-financing pooling arrangement. After allowing for the normal year-on-year changes in grant entitlements (for example, to update the data used in the needs assessments) the effect of the safety net would be to preserve authorities' grant and non-domestic rate income in the first year of the new system at broadly the same level as under the present grant and taxation arrangements.

5.14 The arrangement would generally provide local domestic taxpayers with full protection from the distributional effects of the grant and non-domestic rate proposals in the first year of the new system. After the first year of the new system the adjustments would be frozen in cash terms.

5.15 In preserving the initial entitlement to grant and non-domestic rate income, the Government would have no intention of validating excessive rate increases or any increases in expenditure which are not compatible with its public expenditure plans which occur between the publication of this Green Paper and the introduction of the new system. In determining the level at which grant and non-domestic rate income is to be preserved by the pooling adjustments, the Government would take account of authorities' expenditure and rating behaviour in the remaining years of the existing system.

## The effects on households and tax units

5.16 If the level of local authorities' grant and non-domestic rate income were held constant in the changeover from the present local government finance system to a new system, the position of households and individuals would initially depend solely on the change in the domestic taxation arrangements described in Chapter 3. Since an authority's grant and non-domestic rate income would be preserved, the total amount of revenue to be raised from its domestic taxpayers would remain unchanged for any given level of expenditure. But the *distribution* of that burden between the authority's taxpayers would change as a result of the new domestic taxation arrangements.

5.17 Since the key objectives of the new arrangements include broadening the local tax base to include all adults and moving towards a situation where all local taxpayers pay a flat-rate charge for local services, this redistribution of the local domestic tax burden would affect both households and tax units (that is single people or couples) within households.

5.18 Within a local authority area the proposals would affect households in two different ways.

— *According to the size and composition of the household.* In general, single person households would benefit from the replacement of a tax on property by a tax on people, and households with three or more adults would lose.

— *According to the rateable value of the household property relative to that of other domestic properties in the authority's area.* For any given household type relatively high rateable value households would benefit more from the gradual move away from using property values as the basis of local taxation, while those in low rateable value properties would take a bigger share of the financing of local services. This effect would occur both across precepting authority areas and within rating authorities.

5.19 Among tax units, the principal redistributive effect would be between householder tax units and non-householder tax units, ie between those who are currently liable to pay rates and those who are not. The main beneficiaries would tend to be single-person householders and the main losers would be young single adults who at present are not householders and are not liable to pay rates.

5.20 Chapter 3, however, made it clear that the Government recognises that people would need time to adjust their personal finances to cope with the new community charge. It therefore proposed (paragraphs 3.39 to 3.41) that there should be a transitional period of up to ten years during which rates would be phased out and progressively replaced by the community charge. The distributional effects of this process on households and tax units can therefore be considered at two stages:

i. the effects in the first year of transition, with the community charge introduced at £50 per adult and the rest of local domestic tax revenue raised from rates;

ii. the effects when rates have been completely replaced by the community charge.

These effects are shown in detail in Annex J; the main points are summarised below.

### (i) Effects in the first year of transition

5.21 A modest move towards the community charge of £50 per adult in the first year would produce a very small redistribution of the total local tax burden. The typical two-adult household would on average tend to face no significant change in their total local tax bill. Over 80% of households would gain or lose less than £1 a week — about the price of a pint of beer — and for 94% the changes would represent less than 1% of net household income.

5.22 The picture would be much the same for tax units. Almost 90% of them would gain or lose less than £1 a week and for 98% the changes would represent less than 2% of net income. The main losers would be non-householder tax units who would become liable to pay local taxes for the first time, the majority of whom are single adults in the 18-24 age group. This is the expected and proper consequence of widening the tax base to include all adults.

### (ii) Effects of the complete replacement of rates by a community charge

5.23 The distributional effects of completely replacing rates by a community charge accentuate the scale of changes which would occur in the first year of transition. Nevertheless, the changes would still be relatively small for most people.

5.24 Just over half of all households would be better off with a community charge instead of rates, and half of those losing would lose less than £1 a week. Among tax units, the main effect would be a shift in the burden from householder tax units to non-householder tax units. The main gainers would be single adult households, primarily one-parent families and pensioners, while the main losers would again be young single adults because they would become liable to pay local tax for the first time. Overall, 52% of tax units would lose and 48% would gain; but over 70% of gains and losses would be less than £2 a week.

## Interaction with the social security system

5.25 The proposal for replacing rates with a community charge would have implications for the social security system. If help for those with low incomes continues to be provided through the housing benefit scheme, the widening of the local tax base to include non-householders would increase the numbers eligible for benefit, although the scale of support needed for existing ratepayers would be reduced. On the basis of the assumptions set out in paragraph 5.5, the full replacement of domestic rates by the community charge would lead to an estimated increase in housing benefit caseload in Great Britain of about 18% but an increase in cost of only 4%. However, with the proposed transition over a number of years, these increases would build up gradually.

5.26 The impact of the community charge on the net tax payments of both householders and non-householders will be affected by the proposal in "Reform of Social Security" (Cmnd 9691) that all benefit recipients should pay at least 20% of their tax bill. Otherwise, the interaction between the proposals in Cmnd 9691 and those in this Green Paper are very limited. The proposals in Cmnd 9691 redistribute income support among low income households, generally in favour of families with children. The local taxation proposals described in this Green Paper involve a switch in local tax burden from householders to non-householders and affect all income groups. The effects are discussed in more detail in Annex J.

## Limitation of local domestic tax bills

5.27 The new grant and taxation proposals should considerably improve the accountability of local authorities to their electors for their expenditure and taxation decisions. The reasons for increases in local taxes will be clearer. At the same time, if all local electors have to bear the full cost of marginal increases in their local authority's expenditure, they will have a strong incentive to take a much keener interest in the levels of such expenditure and may be less inclined to tolerate large increases.

5.28 This increased accountability will only be fully achieved, however, once rates have been completely replaced by the community charge. In the early years of the transitional period the impact of the community charge on electors who are brought into the local tax net for the first time would be modest. In order to ensure that local authorities do not take advantage of this situation by increasing their expenditure excessively the Government proposes to retain a power, similar to the selective rate-capping power, to prevent irresponsible authorities from imposing excessive burdens on their taxpayers.

## Summary

5.29 The proposals for reforming the non-domestic and domestic local taxation arrangements and the system of Government grants to local authorities are radical and far-reaching. Yet with the system of adjustments to grant and non-domestic rate income described in this chapter there would be no dramatic shifts of resources between local authority areas on introduction of the new arrangements; and the proposed transitional mechanism for transferring the burden of domestic taxation from rates to a community charge would ensure that there were no drastic effects on the income of households or individuals. The introduction of the new arrangements would therefore be neither sudden nor disruptive. Despite that they will ensure that the local tax burden will be more equitably shared between domestic taxpayers than at present and that local electors will have to bear the full cost of any increases in expenditure for which they vote. They will narrow the gap between those who pay, use and vote for local services.

EXTRACT FROM MR RIDLEY'S PAPER
E(LF)(87)28 of 9 July 1987.



**Non-domestic rates**

15. I was also asked to consider the possibility of providing a larger contribution from non-domestic ratepayers in London, to keep down community charge bills.

16. The idea of a surcharge on non-domestic ratepayers is unattractive. Non-domestic ratepayers in parts of inner London will, in any case, lose considerably from the move to the national poundage (on 1987/88 figures, the poundage in Wandsworth will, at the end of the 5 year transition, have increased by 61%; and in Kensington and Chelsea by 91%). And most London rateable values are also likely to increase - often substantially - in real terms as a result of the 1990 revaluation. We would give ourselves an even bigger presentational problem if we said that on top of this non-domestic ratepayers in London had to pay 105% of the national poundage.

17. We could get round this problem by keeping the same poundage in London, but requiring only 95% of it to be paid into the national pool. The remaining 5% would then be shared equally across inner London. This would reduce community charge bills in inner London by around £50; but increase them by around £3 everywhere else. However,

- we will in any case be providing inner London with generous transitional help from the safety net (amounting to some £410m in the first year);

- it would be extremely undesirable to pay for further reductions in London by - in effect - a surcharge on community charge payers elsewhere: our supporters are urging strongly that, whatever else we do, we do not make the north contribute financially to alleviating the problems of London.

CONFIDENTIAL

My own view is therefore that we should not pursue the idea of additional help from non-domestic rates.

CL

In case point is raised again

AT

mjd 63m

CONFIDENTIAL

pmp

FROM: MOIRA WALLACE

DATE: 13 January 1988

MR FELLGETT

cc PS/Chief Secretary
Sir P Middleton
Mr Anson
Mr Kemp
Mr Scholar
Mr Hawtin
Mr Turnbull
Mr Culpin
Mr Potter
PS/Inland Revenue
Mr A J Walker IR

**COMMUNITY CHARGE: BRIEFING LINE**

The Chancellor has seen and was grateful for your minute of 12 January. He is content with your proposed briefing line ,with one amendment; he would delete the passage in brackets at paragraph 6(ii), because, although the policy objections to a surrogate local income tax were the most important, administrative difficulties also matter, and need not be played down.

MPW

MOIRA WALLACE