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WF Spark

FROM: J P MCINTYRE
DATE: 8 April 1988

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There are clearly quite a lot of arguments against these proposals. But nothing else is on offer. Case for considering doing just taper.

CHANCELLOR

cc Chief Secretary
Mr Phillips
Mr Potter

COMMUNITY CHARGE REBATES

Mr Ridley's letter of 7 April proposes that he should announce at Report Stage of the Local Government Finance Bill (18 April):

- i. a reduction in the slope of the community charge rebate taper from 20 per cent to 15 per cent;
- ii. an increase in the earnings disregard, for the purpose of calculating entitlement to community charge rebate, from £5 to £15 for single people and from £10 to £20 for couples.

2. We and LG have considered these proposals in the light of Mr Allan's minute of yesterday, recording your view that we should look at some relief for those worst affected by the community charge but that the cost should not fall on the Exchequer. However, as explained below, our conclusion is that not only are there serious disadvantages in the proposals but that it is hard to see how their cost could be offset by reducing the AEG or its successor.

The existing rebate scheme

3. The background is that there are two income tapers under the new social security system. These tapers are applied when incomes rise above the level of Income Support to which an individual or family is entitled. One is applied to assistance with rents (65 per cent in 1988-89 and planned to rise to 70 per cent in 1988-90, though the latter has not been announced). The other applies to assistance with rates (20 per cent). Ministers have not yet

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decided what the taper for the community charge should be. But it was agreed last year that the rebate arrangements would be broadly similar to those for rates, and Mr Scott has announced this in the House. The expectation, therefore, is for a 20 per cent taper.

4. The earnings disregards are £5 for single people and £10 for couples for calculating both Income Support and Housing Benefit entitlements. This is one of the simplifying features of the new system. The only exception is lone parents who have a £15 disregard for the purposes of calculating Housing Benefit.

The effect of Mr Ridley's proposals

5. Total community charge rebates in 1990-91 will be very roughly £1.6 billion. This is already about £140 million more than the existing rate rebate scheme would cost, because more people will be entitled to rebates under the community charge. A reduction in the taper to 15 per cent would cost about £130 million, and the proposed increase in the earnings disregard would add around £100 million to the cost of the scheme. The combined effect would be around £200 million, as there would be some overlap. This would be all income forgone and add to the PSBR, but it would not be public expenditure. DHSS account for it as part of the Housing Benefit scheme.

6. Neither proposal would affect those entitled to the maximum 80 per cent rebate, who will also get some (though not necessarily full) compensation in their Income Support for their 20 per cent community charge payments.

7. The effect of the proposals would be on those on incomes just above Income Support levels. Those already entitled to less than the maximum rebate would get increased rebates, and additional people would be floated on to Housing Benefit because it would extend further up the income scale. To give one example, a couple with two children paying average rent and community charge would see their HB entitlement extinguished at gross earnings of £10,000 instead of £8,250 (£147 weekly net income instead of £125.)

8. Taken together, Mr Ridley estimates that his proposals would add about 1¼ million individuals and couples to the numbers already expected to be entitled to community charge rebates (7 million). 300,000 would be single pensioners or pensioner couples. 250,000 would be single people below retirement age. 700,000 would be couples below retirement age. Most of the 1¼ million would add to the total Housing Benefit population, as they would not be recipients of rent assistance.

9. The annex illustrates how the proposals would help some typical charge-payers on low incomes.

Assessment

10. The arguments against the proposals are:

i. They would add £200 million to the PSBR.

ii. Additional financial support for those paying community charge would have the effect of making it less painful and so reduce its effectiveness in improving accountability.

iii. The proposals would be seen not only in terms of the community charge but as a major retreat in the context of the social security reforms, only a week after their introduction. This might well encourage pressure for more concessions.

iv. They would add perhaps a million to the number of people on benefit, when the government's general strategy is to reduce dependence on benefits.

v. They would make it very difficult to proceed with the planned increase in the rents taper to 70 per cent in April 1989, as this would be seen as the government getting back the 5 per cent lost on the community charge taper. Mr Ridley would see this as an advantage; he has already argued for the reversal of the 70 per cent

seen as it is anyway

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decision. But it would add £50 million (public expenditure) to the DHSS programme.

vi. The community charge rebate scheme (even without Mr Ridley's concessions) will cost over £1½ billion, already £140 million more than the rate rebate scheme, because more people will be entitled to rebate. The new rents policies are also putting strong upward pressure on Housing Benefit. Against this background, we need to look for ways of containing expenditure rather than adding another £200 million.

vii. It is not easy to see why a 20 per cent taper should be right for rates but only 15 per cent for the community charge. A reduction to 15 per cent would give a windfall gain to a householder paying the same in community charge as in rates.

vii. The higher earnings disregard would remove one of the elements of simplicity in the new benefit system. It would make housing benefit more complex for Local Authorities to administer. And there might well be pressure to raise the disregards for Income Support and the rent rebate element of HB to the same level. On HB alone, this would add £110 million to public expenditure.

ix. They would conflict with the government's objective of concentrating help on the poorest. The beneficiaries of the concessions would all have incomes above Income Support levels, and the biggest gainers would be better off rebate recipients (see annex).

11. I am afraid we are unable to find anything to say in favour of the proposals except that they would slightly reduce the marginal tax rate of very roughly 50,000 people by 3-5 per cent. Even this advantage is more than offset by the disadvantage that they would increase the MTRs of up to 1 million people brought within the rebate system from 34 percent to 44 percent.

(so just do taper?)

All this is true, but there is nothing that can be done to help poorest unless some concession is made 20%

Alternative concessions

12. We and LG have considered whether there are less objectionable counter-proposals we could put to Mr Ridley that would be likely to satisfy him. But we have not come up with any. If Mr Ridley's aim is to make a gesture of substance towards those just above Income Support levels, the two concessions he has proposed are the obvious means of achieving this.

13. One way of responding would be to argue that only one of the concessions be made. This would roughly halve the cost. But the other objections listed above would remain.

Offsetting the Cost

14. You suggested that we might seek to offset the Exchequer cost of any additional relief by a reduction in grant (probably Revenue Support Grant rather than specific grants). In that way, the cost of extra help for the poorest chargepayers would be met by chargepayers as a whole. But, in practice, shifting the cost on to chargepayers would be difficult. There is no forward plan in the PEWP for the RSG at present - though there will be under the new planning total post-1990. Whatever commitment might be made now to reduce grant, it would be impossible to prevent DOE taking the cost of the relief into account in determining their bottom line in the negotiations on grant for 1990-91.

Mr Mates' new clause

15. It is obviously a matter of political judgment as to whether Mr Ridley's proposals are necessary to ensure the defeat of the new clause. (As you know, Mr Ridley is also pressing for concessions on other issues in the Bill eg dual running and transitional arrangements for small business.) We would only comment that concessions made at this stage might not be enough to avoid problems in the Lords. Indeed, concessions now might even encourage opposition in the Lords to go for more. Although Mr Ridley's proposals are expensive and would provide significant gains for the better off rebate recipients, they might not be enough to satisfy the government's critics - many would get only modest increases in rebate, and the effect on MTRs would be

slight. If this assessment were to prove correct, we might well be faced with demands for further concessions when the Bill is in the Lords.

Conclusions

16. On the substance, the arguments against Mr Ridley's proposals are very strong. And, on tactical grounds, it is not clear that, if concessions have to be made, now is the time to make them, in advance of the Bill going into the Lords. However, you may not wish to rebuff Mr Ridley completely, and the attached draft reply ends by offering urgent consultations between DOE officials and ourselves to see whether there might be alternative solutions which avoid the disadvantages in the proposals Mr Ridley has put to you.

17. This has been agreed with LG.

Jm

J P MCINTYRE

DRAFT LETTER TO MR RIDLEY

COMMUNITY CHARGE REBATES

*Considerable
expensive
what
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than you
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spoke,*

Thank you for your letter of 7 April.

As you know from our talk before Easter, I well understand the difficulty ^{yes} you are ⁱⁿ caused by ^{in as a result of} Michael Mates' new clause. And I can see why you are attracted by the idea of announcing concessions at Report Stage. ^{in order to reduce support for the clause.} [However, ^{But} the proposals in your letter ^{do raise} would not only be expensive but have a number of other disadvantages]. ^{considerable difficulties} In particular, ^{they are expensive, and} they would conflict with our policies of reducing dependence on benefits; ^{and} ^{they} would ^{also} weaken accountability, ^{which is at the heart of our policy in introducing the community charge.} I also have doubts whether, on tactical grounds, it would be right to offer any such concessions at this stage.]

^{They would,} As you say, [^] [your proposals would] cost around £200 million. This would be over and above the £400 million or so we will already be providing through Income Support in compensation for those on benefit who will have to pay 20 per cent of the community charge. It would also be additional to the £1½ billion or more we are likely to spend on the rebate scheme as it stands. [It really is very difficult to contemplate adding to these already large expenditures.]

[^] Your proposals would also, as you acknowledge, bring a further 1¼ million individuals and couples within the rebate

scheme. This would be on top of the 7 million or so who are currently expected to be entitled to rebates. The proposals would therefore be a major reverse for our policy of reducing dependence on benefits.

A further consideration we need to keep in mind is that your proposals would be seen not only in the context of the community charge but ^{also} of the social security reforms. [Within days of the reforms being introduced, we would be seen as beating a major retreat. This might ^{only} encourage critics of the reforms to demand further concessions, [and I would not like to add to ^{at} the pressures ^{thus adding to} [John Moore is] ^{we} already facing] on this front.]

[So I am afraid that, on their merits, I see very considerable disadvantages in the proposals. However, I know that they also need to be considered against the need to deal with Michael Mates' new clause. On this point, I do wonder whether your proposals, even if they were to achieve their objective in the Commons, might only encourage our critics in the Lords to seek further changes. If this proved to be the case, we might be faced with demands for more concessions. Defeat of Michael's new clause without offering concessions might strengthen our position in the Lords.]

[However, in view of your concern, I would be content for your officials and mine to consider as a matter of urgency whether

The clause is being disregarded

there are any alternative means of reducing support for Michael's clause which would avoid the expense to the Exchequer and the other disadvantages of the proposals you have put to me.]

NIGEL LAWSON

The increase in the earnings disregard raises particularly difficult problems. It would remove one of the ~~main~~ ^{important} simplifying features of the new social security system, since it would open up a gap again between the earnings disregard for different benefits. This would inevitably make it more complicated to administer, and would create pressure to raise the earnings disregard for Income Support to the next element of Housing Benefit.

The reduction in the ^{commensurate change} rebate taper also raises difficulties. But if, following our discussion with the Prime Minister & the Chief Whip on Monday, we are convinced that a concession is necessary, it is in this area I think a more here might be the least damaging. But I could only accept it on two conditions (i) that we stick firmly to our existing decision to raise the rent taper from 65 per cent to 70 per cent in 1989-90; and //over

(ii) ^{that} we ^{agree to} recover the cost of the
commission (about £130 million)
from a commensurate reduction in
aggregate grant to local authorities
in 1990-91. This is fully within
the spirit of the Mates clause, since
it will mean that a small amount
is added to all community charge bills
to finance additional rebates for the
less well off.

I am copying this letter and yours to the
Prime Minister & Chief Whip.

NIGEL LAWSON

(Nigel Wickes knows about the
Redley letter & is keen to have
it & your reply on the table for
Monday).

ANNEX - ILLUSTRATIVE EXAMPLES

(i) Couple, two children under 11, net income £120 per week, paying average community charge of £235 each, i.e. £9 per week total.

	Existing rebate scheme	Ridley scheme
Maximum rebate		
(80 per cent of community charge)	£7.20	£7.20
	-----	-----
Net income	£120.00	£120.00
Income support applicable amount	£79.10	£79.10
Earnings disregarded	£10.00	£20.00
	-----	-----
'Excess' income	£30.90	£20.90
applying the taper to this	£6.15	£3.15
and deducting it from the	-----	-----
maximum rebate above to give	£1.05	£4.05
the actual rebate		

Gain £3.00 per week

[The two changes - disregard and taper - are to some extent self-cancelling. Changing the disregard only would produce a gain of £2 - changing the taper only would produce a gain of £1.50]

Further examples

(ii) Pensioner couple, state and occupational pension totalling £90 net, paying average community charge of £235 each.

Existing scheme **£2.75 per week** Ridley scheme **£3.85 per week**

Gain £1.10 per week

[Pensioners will not gain from the increase in the earnings disregards since pensions are not earnings]

(iii) Single person, under 25, net income £80 per week, paying London community charge of £10 per week.

Existing scheme **nil** Ridley scheme **£2.15 per week**

Gain £2.15 per week

(iv) HEO(D), married, one child under 11, gross salary £13,500, net income £190 per week, living in Hackney (community charge £700 each).

Existing scheme **nil** Ridley scheme **£6.25 per week**

Gain £6.15 per week