



CABINET OFFICE

Central Statistical Office

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From the Director: J. Hibbert

CH/EXCHEQUER	
REC.	30 AUG 1988
ACTION	MR SCHOLAR ✓ 318
COPIES TO	PS/CST, AS/FST, PS/EST, SER P MIDDLETON SER T BURRIS, MR ANSON, MR PEZETZ, MR SEDGWICK, MR HIBBERT, MISS O'NEILL, MR POTTER MISS WHELOON (T.SOU) MISS PEARSON

26 August 1988

Dear Nick,

A signed copy of the letter to be given up with the prime minister's copy (X) (4).

RETAIL PRICES INDEX

The correspondence of your Secretary of State with the Chancellor of the Exchequer and with the Secretary of State for the Environment, about the treatment of the Community Charge in the Retail Prices Index, has been copied to me. I am writing to record my views on how the difficult issues involved might best be handled.

The arguments for and against the inclusion of the Community Charge in the RPI are set out in the paper by the Department of Employment dated 22 July 1988. In purely statistical terms the Community Charge is a direct tax. Unlike domestic rates (an indirect tax), its inclusion would change the RPI from a price index into a hybrid statistical indicator which would measure a mixture of changes in prices and changes in costs. In the past arguments for the inclusion in the Index of reductions in household costs which did not reflect actual changes in price (for example, those resulting from the switch of household purchases to cheaper brands of a given commodity, or to cheaper retail outlets) have been rejected. It would be ironic if the distinction between prices and costs were now to be abandoned at a time when this would be likely to lead to an upward bias in the RPI as a measure of price changes. Such a fundamental change would also no doubt lead to greater pressures in the future for other increases in household costs to be reflected in the Index. If the RPI is to remain a price index, the Community Charge should be excluded.

The arguments for the inclusion of the Community Charge rest on the expectation that householders will perceive it as replacing domestic rates and that its exclusion would be seen as manipulation of the Index. Public acceptability of the methods followed for compiling the Index is important and use of the RPI Advisory Committee has provided a mechanism for maintaining it.

Mr N Wilson
Private Secretary
Secretary of State for Employment

I believe that the best course now is to put all the arguments to the Advisory Committee and to be ready to accept the recommendations that emerge from its deliberations. The intention would be to let the onus for determining the outcome fall primarily on the non-government members of the Committee in the light of the technical arguments presented to them by officials. If the non-government members of the Committee were unable to agree on how to deal with the Community Charge then the Secretary of State would need to make the choice which, in the light of the Committee's discussion, seemed most likely to command public acceptability.

Why? In advocating this course of action I am aware that this could give rise to other problems to which solutions would need to be found. If, for example, the Committee recommended exclusion of the Community Charge from the Index the indexation of state retirement pensions by the RPI could then be seen as unjust, particularly by those pensioners not eligible for other assistance from the State. But in these circumstances there would seem to be no reason why the Government should not, if it wished, increase some pledged benefits by more than the increase in the RPI in recognition of the fact that some households were known to be faced with an increase in costs greater than the increase in the RPI. The differential effects on single and married couple households, for example, could be taken into account. *ly*

Despite the existence of such problems I believe that the normal process of consulting the Advisory Committee should take place in the way I have suggested. To act otherwise may destroy public confidence in the Index and lead to even greater difficulties for the Government in the future. The time available is extremely short and I hope that agreement can be now quickly reached to convene the Advisory Committee to consider these matters.

I am copying this to the Private Offices of the Chancellor of the Exchequer, the Secretary of State for the Environment, the Secretary of State for Social Security and the Secretary of State for Scotland, to Paul Gray at No 10 and to Sir Robin Butler.

Yours sincerely

Jack Hibbert

J HIBBERT

FROM: A C S ALLAN *pay*

DATE: 5 September 1988

MR SCHOLAR

cc PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Peretz
Mr Sedgwick
Mr Hibbert
Miss O'Mara
Mr Potter
Miss Wheldon - T.Sol.

COMMUNITY CHARGE AND RPI

The Chancellor has seen Mr Hibbert's letter of 26 August to the Secretary of State for Employment. He thought this was a singularly (if unintentionally) unhelpful letter. The Chancellor feels we need to consider a quick reply contesting the premise that if the community charge were included in the RPI that "would be likely to lead to upward bias in the RPI as a measure of price changes", and the conclusion that if the community charge were excluded from the RPI "the indexation of State retirement pensions by the RPI could then be seen as unjust".

A handwritten signature in black ink, appearing to read "ACSA".

A C S ALLAN