

CONFIDENTIAL

FROM: P N SEDGWICK
DATE: 28 FEBRUARY 1989**CHANCELLOR**cc Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Edwards
Miss Peirson
Mr Peretz
Mr Gieve
Mr Hibberd
Mr Mowl
Mr O'Brien

Ms Wheldon Tsy. Sol.

RPIAC REPORT ON THE IMPLICATIONS FOR THE RPI OF THE ABOLITION OF DOMESTIC RATES

Mr Fowler has sent you a letter together with a copy of the RPIAC report.

2. He has asked for comments on the report and his proposals for handling it by this Thursday, March 2. All being well he would like to announce his decision on Friday, March 3 by means of an arranged PQ and to publish the RPIAC report at the same time. In practice this would mean that commentators would get copies of the RPIAC report plus a DE note for editors by c. 2.30 pm on Friday. The draft press notice has not yet been received.

3. As you are aware the RPIAC recommends that the average Community Charge per head should replace average rate poundages in the RPI. The change would take place in April this year for Scotland, and in April 1990 for England and Wales. The report also recommends that the Community Charge element of the RPI should be included in the housing component of the RPI (paragraph 67 of the report): this does not have any implications for the calculation of the total RPI.

4. All RPIAC members agreed the report and its recommendations. The text makes clear, however, that there were major divergences of view.

5. The Bank of England cannot make a formal determination under the relevant clause of the IG prospectus until the government's

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OK?
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OK in
Sunderland

decision has been made. The Bank have however seen the RPIAC Report, and have assured us that if its recommendations are accepted they will not reach a view that triggers the early redemption clause.

6. Mr Fowler is not strictly speaking correct to claim that the RPIAC's proposals have never been rejected in the past. (The Committee recommended the calculation of regional price indices. DE never calculated them.) It is true, however, that successive Ministers have always accepted recommendations relating to the coverage and calculation of the main RPI. The Committee's recommendations is in line with the view that you and other Ministers reached before the convening of the Committee, following extensive discussion of the possible implications for IGs if the Community Charge was not included in the RPI. There is therefore no problem agreeing with Mr Fowler's proposal that he should accept the RPIAC's recommendations. It is likely that most shades of political opinion and all interested pressure groups will welcome such a decision. The only criticism is likely to come from economists who believe that there are strong technical arguments for excluding a direct tax such as the Community Charge from the RPI. Some members of the RPIAC - Harold Rose, Bill Robinson, and John Pickering - argued strongly for this. They may even set out their views publicly. It is quite likely that some other economists will advance such arguments.

7. There is one aspect of the RPIAC report that could conceivably lead to more significant problems in the future, namely its assessment of "volume adjustment" of the Community Charge indicator used to calculate the RPI. (Paragraphs 44-53 of the report discuss this: Annex C - written by DOE statisticians - discusses the practical problems in some detail.) In spite of some assertions to the contrary (eg the first sentence of paragraph 55), some parts of the report give the impression (a) that adjustment of the Community Charge indicator in the RPI for the volume of services provided is in principle correct, and (b) that adjustment would be necessary if there were large changes in the volume of LA services. The Chairman agreed to these passages to meet the strong advocacy by David Lee of volume adjustment - if necessary of a rough and ready nature.

8. There are two potential disadvantages of such an impression being given:

first it may undermine the credibility of the RPI if local authorities do curb the services they provide and the Community Charge indicator in the RPI is thought to be growing unjustifiably slowly;

and second any possible change in methodology to cope with this problem would almost certainly involve a change of "coverage", and "basic calculation" for the purpose of the IGs prospectus.

9. There is not much that we can do about this aspect of the RPIAC report. If the issue of volume adjustment does indeed arise in future we will of course have to look at it carefully and consider any RPIAC report - but volume adjustment could be difficult to justify as well as to implement.

10. I attach a short letter for you to send to Mr Fowler.

P.N.J

P N SEDGWICK

Juliet insisted on this bit being included!

DRAFT LETTER FROM CHANCELLOR
TO SECRETARY OF STATE FOR EMPLOYMENT*Please type
for signature*

Thank you for your letter of March 26 together with the final report of the Retail Price Index Advisory Committee.

formally
Though unanimous, the report reflects what was obviously a wide range of views among Committee members. Nevertheless I agree that you should accept the recommendation that the Community Charge should replace domestic rates in the RPI, and am content with your proposals for the handling of the announcement of your decision.

Copies of this letter go to recipients of yours.

[N.L.]



PRESS NOTICE

48\89

February 24, 1989

RETAIL PRICES INDEX ADVISORY COMMITTEE'S REPORT

Employment Secretary Norman Fowler today said that he had received a report from the Retail Prices Index Advisory Committee recommending that the Community Charge should be included in the retail prices index.

In answer to a Parliamentary question from Emma Nicholson, MP (Devon West and Torridge), Mr Fowler said:-

"I have today received a report from the Committee recommending that the Community Charge should be included in the retail prices index when domestic rates are abolished. I will shortly be publishing the report and announcing the Government's decision on the recommendation."

Note to Editors:

Membership of the RPI Advisory Committee comprises academics, nominees of the National Consumer Council, the British Retailers Association, the National Federation of Consumer Groups and representatives of the TUC, CBI, Co-Operative Union, Age Concern, the National Chamber of Trade, the Bank of England and Government Departments closely concerned with the RPI.

The Committee's terms of reference are:

"To advise the Secretary of State for Employment on the effect of the abolition of domestic rates on the construction of the Retail Prices Index and on the way in which expenditure on holidays should be taken into account in the index; and to review progress on implementing longer-term recommendations made in the Advisory Committee's last report (Cmnd 9848, July 1986)".

60712



Department of Employment
Caxton House, Tothill Street, London SW1H 9NF
Telephone 01-273 5803
Telex 915564 Fax 01-273 5821

Secretary of State

CH/EXCHEQUER	
REC.	27 FEB 1989
REPLY	MR SEDGWICK
SERIES' TO	SIR P MIDDLETON
	SIR T BURRIS
	MR ADSON
	MR SCHOLAR
	MR PERLETZ
	MR EDWARDS
	MR WHELDON - T/SOL

The Rt Hon Nigel Lawson
Chancellor of the Exchequer
Treasury Chambers
Parliament Street
LONDON SW1

Nigel Lawson *February 26*

RETAIL PRICES INDEX ADVISORY COMMITTEE REPORT

I have now received the Advisory Committee's report on the Community Charge issue, and have announced that I intend to publish it shortly, together with my decision on the recommendations. Printing arrangements have been put in hand which would allow publication as a Command Paper on Friday 3 March, on which day I hope to make a substantive announcement by means of an Arranged PQ, with an accompanying Press Notice from my Department.

I enclose a copy of the report, whose main recommendation is that the Community Charge should be included in the RPI in future in a similar way to that in which rates are included at present. I understand that this conclusion was reached by consensus amongst the non-Government members of the Committee, who represent consumers and employees, retailers, business interest and the academic community. As we had agreed, officials representing Government Departments avoided expressing strong preferences on the issues before the Committee. However, the conclusion reached by the Advisory Committee seems likely to be acceptable in all the circumstances, and likely to command greater public acceptance than the alternative of excluding the Charge from the Index.

Though the Committee is only advisory, its recommendations have never been rejected in the past and my view is that we should accept them on this occasion. The arguments for including the Community Charge in the RPI, and, indeed, the

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Employment Department · Training Agency
Health and Safety Executive · ACAS

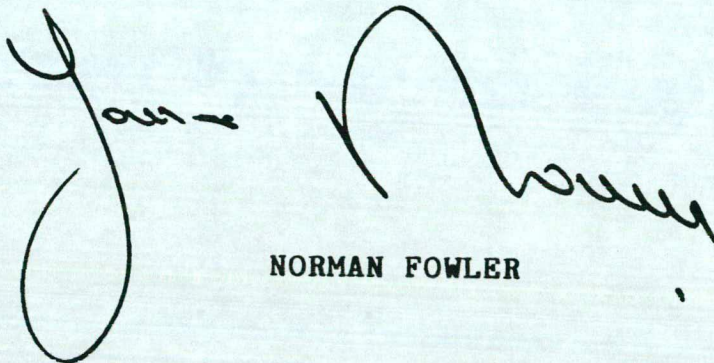


Secretary of State
for Employment

contrary case, are set out at some length in the report. It is precisely because the matter is a difficult one, which cannot be easily resolved on technical grounds, that we need the seal of approval which a recommendation from an independent body gives. In the past this has provided a good defence against criticism of the methodology followed in compiling the Index. It is helpful that the arguments both for and against inclusion have been set out so fully in the attached report. Nevertheless, there is a clearly stated consensus in favour of inclusion.

You know of the need for early publication, and since your officials have been involved in the discussions throughout, I now seek your early comments (and those of Nicholas Ridley, John Moore and Malcolm Rifkind, to whom I am copying this), by noon on Thursday, 2 March if at all possible, please.

I am also copying this letter and the report to the Prime Minister and the Head of the Governmental Statistical Service.



NORMAN FOWLER



DEPARTMENT OF HEALTH AND SOCIAL SECURITY

Richmond House, 79 Whitehall, London SW1A 2NS

Telephone 01-210 3000

From the Secretary of State for Social Services Security

py

CONFIDENTIAL

The Rt Hon Norman Fowler MP
Secretary of State for Employment
Department of Employment
Caxton House
Tothill Street
LONDON
SW1H 9NF

CH/EXCHEQU.	
REC.	- 1 MAR 1989
ACTION	MR SEDGWICK
COPIES TO	SIR PHOENIX
	SIR T BURNS
	MR ADSON
	MR SCHWARZ
	MR PEREZ
	MR EDWARDS
	MR WHELAN-TISA

✓ 113

March 1989

Norman Fowler

RETAIL PRICES ADVISORY COMMITTEE REPORT

Thank you for sending me a copy of your letter of 26 February to Nigel Lawson.

I agree with you that the recommendations reached by the Advisory Committee for including the Community Charge in the RPI are acceptable and are likely to be seen as such by the public. I therefore agree that we should accept them and announce the decision in the way you propose.

I am copying this to the Prime Minister, Nigel Lawson and the Head of the Government Statistical Service.

John Moore

JOHN MOORE

CONFIDENTIAL

2 MARSHAM STREET
LONDON SW1P 3EB
01-276 3000



CH/EXCHEQUER	
REC.	-2 MAR 1989
ACTION	MR SEDGWICK
COPIES TO	SIR P MEDDLETON
	SIR T BURNS
	MR ANSON
	MR SCHOLAR
	MR PERETZ
	MR EDWARDS
	MS WHELAN-T/SA

My ref: ✓ 2/3
Your ref:

purp

The Rt Hon Norman Fowler MP
Secretary of State
Department of Employment
Caxton House
Tothill Street
LONDON
SW1H 9NF

2 March 1989

Dear Norman

RETAIL PRICES INDEX ADVISORY COMMITTEE REPORT

Thank you for copying your letter to Nigel Lawson of 16 February to me. The Advisory Committee's report recommending that the community charge should be included in the RPI in future in a similar way to that in which domestic rates are included at present is very much in line with my own views and I wholeheartedly welcome your proposal to accept it. The report will serve to bolster public confidence in the RPI in a way that avoids giving the opposition ammunition to use against the community charge.

The arrangements you have in hand for publishing the report should serve to demonstrate the importance that the Government attaches to this matter, and I agree that it is helpful that the arguments are so fully set out.

I am copying this letter to the Prime Minister, Nigel Lawson, John Moore and Malcolm Rifkind and also to the Head of the Government Statistical Service.

Nicholas Ridley
Amos

NICHOLAS RIDLEY

CONFIDENTIAL



py

Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

2 March 1989

Rt Hon Norman Fowler MP
Secretary of State for Employment
Department of Employment
Caxton House
Tothill Street
LONDON
SW1H 9NA

cc: PS/Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Edwards
Miss Peirson
Mr Peretz
Mr Gieve
Mr Sedgwick
Mr Hibberd
Mr Mowl
Mr O'Brien

Ms Wheldon TSol

Norman Fowler

Thank you for your letter of March 26 together with the final report of the Retail Price Index Advisory Committee.

Though formally unanimous, the report reflects what was obviously a wide range of views among Committee members. Nevertheless I agree that you should accept the recommendation that the Community Charge should replace domestic rates in the RPI, and am content with your proposals for the handling of the announcement of your decision.

Copies of this letter go to recipients of yours.

Yes eva
Nigel Lawson

NIGEL LAWSON



DEPARTMENT OF EMPLOYMENT
Caxton House Tothill Street London SW1H 9NF

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P N Sedgwick Esq
HM Treasury
Parliament Street
London SW1

Your reference

Our reference

Date

2 March 1989

Dear Peter

RPI ADVISORY COMMITTEE REPORT

I attach a draft press notice. Could you let us have any comments by noon tomorrow?

Yours sincerely

Copies to

PPS

Sir P. Middleton

Sir T. Burs

Mr. Shaw

Mr. Pevsley

Mr. Hibbard

Mr. Gieve

Mr. O'Brien

MARTIN HARGREAVES
Assistant secretary
to the Committee

Handwritten notes in red ink:
 V/S Pevsley
 Pevsley
 Shaw
 50/23
 CH
 I'd want to write off
 Para 7 A to Notes & Editors
 (which are much too long anyway).
 It contains some tendentious stuff

DRAFT PRESS NOTICE

3 March 1989

RETAIL PRICES INDEX ADVISORY COMMITTEE'S REPORT

The Government has decided to accept the recommendation of the Retail Prices Index Advisory Committee that the Community Charge should be included in the index when rates are abolished, from April 1989 in Scotland and a year later in England and Wales.

In answer to a Parliamentary Question from [] the Secretary of State for Employment, Norman Fowler, said:

"The report is being published today. I have decided to accept all its recommendations. They will start to take effect in April when the Community Charge comes into operation in Scotland."

The report, entitled *Treatment of the Community Charge in the Retail Prices Index*, is available from Her Majesty's Stationery Office as Cm [], price [].

NOTES TO EDITORS

1. The Retail Prices Index Advisory Committee is convened from time to time by the Secretary of State for Employment to advise on the method of construction and compilation of the retail prices index (RPI). The Committee first met in 1947, when the present index was initiated, and had had ten series of meetings before the latest one. Virtually every aspect of index methodology has been examined at one time or another, and each major development which has taken place in the RPI over the last forty years has followed from the Committee's recommendations. [For example in 1974 it recommended that mortgage interest payments should be included in the RPI for the first time, and in 1986 it defined how housing benefit should be treated in the index.] The Committee's reports are generally published as command papers.

2. The Committee consists of representatives of consumers and employees, retailers and business interests, the academic community and government departments, meeting under the chairmanship of a senior official of the Department of Employment. The procedure has always been for conclusions to be reached by consensus. There has never been occasion for a minority report but the agreed reports which are submitted make clear where differences of view emerged within the Committee and what the competing arguments were.

3. On 17 October 1988 the Secretary of State announced that he was reconvening the Committee to advise him on the effect of the abolition of domestic rates on the construction of the RPI and the way that expenditure on holidays should be taken into account in the index, and to review progress on implementing longer-term recommendations made in the Committee's 1986 report. So far the Committee has had time to consider only the first of these issues: the others will be addressed in a second report to be submitted within the next twelve months.

4. The present report, which was submitted to the Secretary of State a week ago, reviews in some detail the basis on which rates are currently included in the index, the arguments for and against including the Community Charge once rates are abolished, and the different ways in which this might be achieved. The Committee's recommendation is that the Community Charge should be included in the index, in a similar way to that in which rates are treated now. A prime consideration in reaching this conclusion was the desire to sustain public confidence in the RPI, and a belief that this confidence might be set at risk if the Community Charge were excluded.

5. The incorporation of the Community Charge in the RPI, replacing rates, will not have ^{a major} much effect on the level of the index. It is estimated that, taking the changes in England, Scotland and Wales together, the "all items" index will rise by between 0.1 and 0.2 per cent more than it would have done if the same local authority expenditure had continued to be financed by the rating system. This effect arises because the households covered by the index will have to meet a larger share of total Community Charge payments than they did of rates. (See paragraphs 64 and 65 of the report.) Once the changeover has taken place the effect on the RPI of including the Community Charge will depend upon whether the Charge increases more or less quickly than the other items in the index and, in the Committee's view this cannot be predicted.

6. The report points out that, though the precise nature of the RPI's coverage will have changed once the Community Charge has been introduced, its essential character should remain the same. It will continue to measure changes in prices across the whole range of goods and services purchased for consumption by households.

7. Other key points in the report are:

- a) The Community Charge can be seen either as a payment for services rendered by local authorities or as a tax. The Committee thought there was considerable justification for the former view, since the proceeds of the Charge will be used exclusively for the provision of local services, but it also recognised that the Charge - widely referred to as a "poll tax" - does have much in common with direct taxation of individuals. The report identifies a "middle way", saying that the Charge is something of a hybrid - a locally-oriented residence charge combining certain features both of a payment for services and of a direct tax. (See paragraph 17.)
- b) The inclusion of the Community Charge in the RPI can be justified in several ways. In the first place it is, like rates, directly associated with the occupation of property: those occupying two houses will pay two Charges while homeless people will pay none. Secondly, the aggregate payments made will be closely related to the amount of services provided by local authorities: consumers in areas where a high level of services is provided will pay more than those in areas with less provision. Indeed the link between payments made and services provided will be closer under the Community Charge regime than under the rating system. (See paragraphs 29 to 32.)

- c) The Community Charge has features in common with various items which are already included in the RPI, including television and motor vehicle licences, subscriptions and membership fees, standing charges for gas and electricity supply and telephone service, water and sewerage charges. The Committee commented that "It would be difficult to justify excluding such payments as these from the RPI, and the Charge evidently has much in common with them". (See paragraphs 34 to 37.)
- d) The Committee recognised the possibility that local authorities might reduce their Community Charges very significantly by simply cutting services or reducing their standards. Some members thought that, if this were to happen, it would be quite inappropriate for the RPI to fall as a result and that, ideally, the index should be adjusted for changes in the volume of services provided. Other members thought such changes were likely to be small while some, viewing the Community Charge as a tax, felt it would be inappropriate to allow for them in any event. However, the whole Committee agreed that there is no method currently available which would enable changes in the volume of local authority services to be properly estimated, and recommended against making adjustments for them. (See paragraph 45 et seq.)
- e) The Committee identified a particular problem which might arise if there were significant moves towards privatisation of what are currently local authority services, so that their cost was met directly by consumers rather than indirectly via the Community Charge. In this case the Committee said it would want steps to be taken to prevent a spurious fall in the level of the RPI. It therefore thought that the question of volume adjustment should be kept under review and that the Committee should be invited to look at the matter again in a few years' time. (See paragraph 54.)
- f) In line with the treatment of other subsidies and discounts the Committee thought that, in compiling the RPI, no account should be taken of the Community Charge rebates which will be received by many people with relatively low incomes, or of the concession whereby students pay only 20 per cent of the full Charge. (See paragraphs 58 and 59.)
- g) The Community Charge will form part of the "Housing" group within the RPI, as rates have always done. (See paragraphs 66 and 67.)



FROM: A C S ALLAN
DATE: 3 March 1989

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MR SEDGWICK

cc Sir P Middleton
Sir T Burns
Mr Scholar
Mr Peretz
Mr Hibberd
Mr Gieve
Mr O'Brien

RPI ADVISORY COMMITTEE REPORT

The Chancellor has seen Mr Hargreaves' letter to you of 2 March. He feels that the whole of paragraph 7 of the Notes to Editors should be omitted: it contains several contentious points, and the Notes are much too long anyway.

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

A C S ALLAN