CC BH/CP

PRIME MINISTER 29 April 1987

MEETING OF E(LF)

You are meeting after Cabinet tomorrow to discuss the minimum contribution that householders will be expected to make to domestic rates under the new housing benefit arrangements that come into force on 1 April 1988, and the initial level of and transitional arrangements for the national non-domestic rate.

Minimum contribution to domestic rates

Norman Fowler proposes confirming the decision that from 1 April 1988 householders will be expected to meet at least 20% of their domestic rates. We agree with this.

He also proposes that in setting the level of income support benefits from 1 April 1988 additional resources should be provided to enable benefit recipients to meet the 20% of their rate bill they will face for the first time. Without an increase in benefit the standard of living of benefit recipients will be reduced. On the other hand, replacing a proportion of housing benefit, which is available to householders both in and out of work, with an increase in benefit rates generally will reduce incentives to work (although this effect could be reduced by increasing family credit as well). We therefore favour increasing benefit rates only for those groups who are not in the labour market, ie pensioners and the long term sick and disabled. This approach can be defended as ensuring that those groups most in need are broadly protected from the change in housing benefit regulations.

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Married / Single

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The National Non-Domestic Rate

Mr Ridley proposes taking power to:

1. set the poundage for the National Non-Domestic Rate (NNDR) below the level needed to maintain revenue from non-domestic rates;

2. put a cap on the increases in rateable values that result from revaluation;

3. phase in the NNDR over five years.

A lower starting poundage for the NNDR will increase the number of gainers and reduce the number of losers from the change. It will also moderate the impact in areas that will otherwise face large increases in non-domestic rates. However, it is not clear how Mr Ridley proposes to compensate for any resulting reduction in revenue. Although he is only seeking a power to make such reduction its inclusion on the face of the legislation will lead to pressure on the Government to use it. In practice the cost will be met either by reductions in public expenditure, an increase in Corporation Tax or pre-empting some of the Chancellor's fiscal adjustment. We think it is unwise to take a decision in principle on this issue until further thought has been given to the question of how the short fall in finance would be made up.

We see no such difficulty with the proposal to limit the increase in rateable values on revaluation. This affects the distribution of the burden of the NNDR but not the total amount levied.

The NNDR will be introduced for the first time in 1990. Mr Ridley proposes phasing in the charge over the five year period up to 1995 by placing a limit on the increase in rate bill faced by individuals in any one year. This ensures that phasing applies only to those businesses facing the greatest impact. There are some attractions in introducing the NNDR without a transitional period because it would concentrate the problems in a single year rather than the Government facing criticism and requests for further concessions each year over a five year period. Although some businesses will face very large percentage rate increases it is not clear how large these increases will be as a proportion of their total costs. If the proportion is relatively small for the vast majority of businesses the balance of advantage is against a transitional period. If, on the contrary, a significant proportion of businesses will face substantial increases in their total costs the balance of advantage is in favour of a transition in order to give them time to adapt. Further work needs to be done on this.

Finally, Mr Ridley now proposes going on back on E(LF)'s decision to give the Chancellor discretion to increase the NNDR by less than the rate of inflation. He argues that this is a less effective way of reducing the impact of the NNDR on business costs than his current proposal to reduce the initial poundage and that taking such a power reinforces the criticism that the NNDR is a new national tax and if used, would allow local authorities to blame the Government for increases in the Community Charge. We do not find these arguments particularly strong. We earlier argued that the increase in the NNDR should be something less than the rate of inflation, in order to exert pressure on local authorities to improve efficiency. But failing that, we see advantage in the Chancellor retaining a power to reduce the rate of increase in the NNDR.

Conclusions

We support the proposal to fix the maximum level of assistance with rates at 80%. We do not favour increasing all benefit rates to compensate but see a case for increasing them for pensioners and the long term sick and disabled.

No decision should be taken on reducing the initial poundage for the NNDR until thought has been given to how the Government will compensate for the reduced revenue. Further work also needs to be done on the impact of increased rate bills on companies' costs before a decision can be taken on a transitional period since there are some presentational attractions in getting the transition over as quickly as possible. But we support the proposal to place a cap on the increase in rateable values arising from the proposed revaluation. However, we favour placing a limit below the rate of inflation on the annual increase in the NNDR or at least maintaining the earlier decision to give the Chancellor discretion to vary the NNDR by less than the rate of inflation.

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