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From R J T Wilson

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MR GRAY

**UNIFORM BUSINESS RATE AND REVALUATION: TRANSITIONAL ARRANGEMENTS
HARMONISATION OF RATING: THE CONTRACTORS BASIS**

You asked for advice on Mr Ridley's minute of 29 November to the Prime Minister about the Uniform Business Rate (previously known as the National Non-Domestic Rate or NNDR). You may also find it helpful to have comments on the related correspondence about the harmonisation of rating.

BACKGROUND

2. It has always been recognised that the simultaneous introduction of the first business rating revaluation since 1973 and the new Uniform Business Rate (UBR) on 1 April 1990 would mean very large changes in the rate bills of many businesses. E(LF) have twice discussed transitional protection for businesses with the largest increases, on 30 April 1987 (E(LF)(87)7th Meeting) and 14 April 1988 (E(LF)(88)3rd Meeting), and there was correspondence in February 1988. The outcome of these discussions was a transitional scheme with three main elements:

i. a percentage ceiling on the annual increase in any individual business rate bill. In April Mr Ridley envisaged a ceiling of 15% in real terms. A business with a very large increase would see its bill rise by 15% per annum in real terms for a run of years;

ii. a lower ceiling for small businesses. In practice, this meant any business occupying premises with rateable value below a threshold. In April Mr Ridley envisaged a ceiling of 10%, 5% below that which would apply generally;

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iii. a limit on the largest reductions in rate bills sufficient to finance the cost of the protection for businesses with increases. The level of the UBR poundage would therefore be unaffected by the transitional arrangement: gainers would pay for protection to the losers.

3. This scheme was drawn up without the benefit of reliable figures for actual changes in rate bills. The Inland Revenue Valuation Office have now completed a survey of the likely effects of the revaluation which for the first time provides this information. The results are shown in the tables attached to Mr Ridley's minute. The range of changes in rate bills is even larger than had been expected: 4% of businesses face increases in excess of 200%, and a further 8% face increases between 100 and 200%. The pattern of gains and losses is also skewed, with a much larger range of losses than gains.

MR RIDLEY'S REVISED PROPOSALS

4. Mr Ridley has reconsidered the transitional arrangements in the light of these figures. He now proposes:

- i. a ceiling of 20% per annum on the real increase in any individual rate bill;
- ii. a lower ceiling of 15% per annum in real terms on increases for properties with a new (post revaluation) rateable value below £7,500 in London or £5,000 elsewhere;
- iii. a matching limit on rate bill reductions for larger properties, sufficient to meet the costs of protecting losers. The current estimate is that this would need to be set at 10%;
- iv. a complete exemption from the limits on gains for small premises, defined in the same way as under (ii) above.

Finally, Mr Ridley proposes to leave properties with rateable values below about £100 (eg. AA telephone boxes) out of the transitional arrangements altogether.

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MAIN ISSUES

5. The new forecasts of likely changes in rate bills make the transition to the UBR even more difficult than before. Nevertheless Mr Ridley's proposals stick closely to what was agreed by E(LF) in their previous discussions. The proposed ceilings on increases in bills are now higher than those mentioned in April, but within the range discussed a year earlier. I understand that the Chancellor of the Exchequer is likely to support the general structure of Mr Ridley's proposals.

6. There are however two points which the Prime Minister may wish to consider:

i. the disparity between the ceilings on losses (20%) and on gains (10%). This is a consequence of the skewing of gains and losses. Nevertheless it may provoke criticism from the gainers, who will say that the revaluation shows that they have been overcharged in the past, and that their well deserved gains are being constrained unreasonably. But if the ceiling on gains were to be relaxed, to say 20%, this would leave a large part of the protection for losers to be financed from another source. There are three main possibilities:

a. all other business ratepayers, through an increase in the UBR poundage. Ministers did not favour this approach in April, and Mr Ridley has said publicly that he is unlikely to adopt it;

b. community charge payers. But this would increase the charge in the early years;

c. the Exchequer. But this would be opposed strongly by Treasury Ministers.

None of these looks at all attractive, and Mr Ridley's approach may be the best which can be devised;

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ii. the exemption of small businesses from any limit on their gains. The Chancellor is likely to say that this would be unduly provocative to other gainers, who will face a 10% per annum ceiling. He may suggest that small businesses should be subject to a ceiling, albeit a higher one: perhaps 15% equal to the ceiling on small business losses. This may be a more balanced proposition, but it would put a cap on the gains of some hundreds of thousands of small businesses.

TIMING AND ANNOUNCEMENT

7. Regulations for the transitional arrangements do not need to be made until next summer. But Mr Ridley wants to make an announcement now about the arrangements, to fulfil undertakings he gave during the passage of the Bill. He proposes to give firm figures for the ceilings on losses, and an indicative figure for the limit on gains. I understand that the Chancellor may resist the publication of an edited version of the Valuation Office survey, despite commitments made by Mr Ridley in the past. The Prime Minister will probably want to leave the two Ministers to resolve this issue between them.

HARMONISATION OF RATING: THE CONTRACTORS BASIS

8. Mr Ridley minuted the Prime Minister on 5 October about a related issue: the rating of specialist properties (eg. steel, oil and ship building works, much of local government and many Crown premises) where the "contractors basis" of valuation is used. Most Ministers with an interest have since endorsed his proposal to prescribe a "decapitalisation rate" of 6% to be used in these valuations, with a lower 4% rate for educational institutions.

9. However, the Chief Secretary's letter of 21 November to Mr Ridley puts forward a number of alternative suggestions. One in particular, that the UBR poundage should be set in 1990/91 at the level which would maintain the overall bill of private business ratepayers in real terms (rather than the overall bill of all non-domestic ratepayers), appears to go against the Government's commitments. Mr Ridley wrote to Mr Major on 29 November contesting this and other proposals in his letter.

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10. This issue does not need to be settled before an announcement on the transitional arrangements can be made. The Prime Minister may therefore want to ask Mr Ridley and Mr Major to meet to resolve it, as suggested in Mr Ridley's latest letter. But she might also want to make the point that whatever is agreed must be consistent with the Government's existing commitments, in letter and spirit.

CONCLUSION

11. If the Prime Minister agrees, you might like to write to Mr Ridley's office on the following basis:

- i. endorsing the general structure of the revised transitional arrangements as the basis for an early announcement;
- ii. possibly commenting on one or both of the points in paragraph 6 above;
- iii. asking Mr Ridley and the Chief Secretary to meet to resolve their differences on the contractors basis of rating, in a way which is consistent with the letter and spirit of the Government's existing commitments.

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