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PART A

BUDGET BRIEFING 1983

DD 25 years N.Agig 15/7/94

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PART A

CLOSED

CONTINUED ON:-

PART B

TO BE RETAINED AS TOP ENCLOSURE

Cabinet / Cabinet Committee Documents

Reference	Date
C(83)	26/01/1983
C(83)	26/01/1983

The documents listed above, which were enclosed on this file, have been removed and destroyed. Such documents are the responsibility of the Cabinet Office. When released they are available in the appropriate **CAB** (CABINET OFFICE) CLASSES

Signed [signature] Date 7/6/16

CONFIDENTIAL

FROM: J.O. KERR
8 November 1982

cc: PS/Financial Secretary
PS/Economic Secretary
PS/Minister of State (C)
PS/Minister of State (R)
Sir Douglas Wass
Sir Anthony Rawlinson
Sir Kenneth Couzens
Mr. Burns
Mr. Middleton
Mr. Quinlan
Mr. Wilding
Mr. Kemp
Mr. Moore
Mr. Monger
Mr. Mountfield
Mr. Hall (4 copies)
Mr. Salveson (7 copies)
Mr Ridley
Mr French
Mr Hawtin

PS/CHIEF SECRETARY

AUTUMN STATEMENT

I attach a copy of the final version of today's Oral Statement in the House.

JOK.

J.O. KERR

With permission, Mr. Speaker, I should like to make a statement. As the House knows, it is customary at this time of year to publish outline public expenditure plans and proposed National Insurance changes for the year ahead, together with the economic forecast required under the Industry Act 1975. This year, as foreshadowed in the Government's reply to the Report of the Treasury and Civil Service Committee on Budgetary Reform, we are bringing these together, and publishing them in an Autumn Statement which I shall today be laying before the House. I am grateful to my rt. hon. Friend the Member for Taunton, and the Treasury Select Committee, for the initiative which has led to this development.

During the past year, monetary conditions have exerted downward pressure on price rises, and substantial progress has been made against inflation. In January the rate of inflation was 12 per cent; is now around 7 per cent; and we

/envisage a

envisage a 5 per cent rate early in 1983. Interest rates have fallen even more sharply, with bank base rates down a full 7 points from their peak of 16 per cent last year to 9 per cent today. The CBI have calculated that each percentage point fall benefits British industry by around £250 million in a full year. We shall continue to maintain downward pressure on the monetary aggregates, in order to achieve further success in the battle against inflation. Interest rates will continue to reflect the indicators of monetary conditions which I described in my Budget Speech.

As the Statement explains, the growth in output this year - in this country and throughout the Western world - has been lower than anticipated. For next year the Industry Act forecast now suggests a 1½ per cent increase in our GDP. That is close to what is expected for most other industrialised countries. Unemployment remains the nation's most distressing problem. As in other countries, further rises are expected to continue into next year,

/although they

although they should moderate as output picks up, in response to lower inflation and lower interest rates.

Public borrowing remains under firm control - which of course is one of the reasons for the fall in interest rates. We expect the PSBR this year to be within the figure of £9½ billion expected at the time of the Budget. Final decisions about the level of next year's borrowing requirement will not of course be taken until my 1983 Budget. The current forecast suggests that the scope for possible tax reductions in 1983-84 could be of the same order as was indicated at the time of the last Budget. This is on the basis of conventional assumptions as to the revalorisation of direct taxes and excise duties. It also assumes the same 1983-84 PSBR, as a percentage of GDP, as was assumed at the time of the last Budget, and takes account of the decisions which I am announcing today.

/The public expenditure

The public expenditure planning total for 1983-84 will be £120.06 billion. This is lower than the provisional figure for 1983-84 published on Budget Day this year. It is the first time since 1977 that a Government has been able to stop expenditure plans for a particular year rising with each annual review. Compared with the plans for the current year, the new total is a slight fall in cost terms (that is, in constant prices). The ratio of public expenditure to GDP will come down from 45 per cent to 44 per cent, reversing an upward trend which has continued since 1977.

Details of the changes in individual programmes are summarised in the Statement. Social Security Programmes have been adjusted to take account of the rapid reduction in inflation. This month's benefit uprating is 11 per cent. Even allowing for the 2 per cent extra to compensate for last year's shortfall, that is well over the current rate of inflation. We accordingly intend to make an adjustment to next year's uprating. Meanwhile,

/those in receipt

those in receipt of benefits will continue to receive payment at a rate above that needed to compensate for price rises in the last year. As is customary, the exact size of next year's uprating will not be decided before Budget time.

The House will be glad to hear that the resources we had planned to make available for a number of important programmes have been increased:-

- We plan additional gross expenditure of £260 million on two new special employment measures - the Community Programme and the Job Splitting Subsidy - which were announced earlier this year.

- For housing, the provision of an extra £49 million, and a continuing high level of receipts from council house sales, will allow gross capital spending to be at least 10 per cent higher than the expected level this year.

- More money will be

- More money will be made available for the urban capital programmes, to support the new Urban Development Grant programme and the Urban Development Corporations in London Docklands and Merseyside.

These two changes represent a significant new boost to the construction industry.

- £96 million more has been allocated to law and order programmes, mainly on police and prisons.

- In the Health Service we are providing an extra £80 million in England, which should continue the growth in the level of services which has already taken place under this Government.

Comparable increases will be made for the rest of the United Kingdom.

- Finally, provision

- Finally, provision for defence in 1983-84 has been increased by £622 million, because of extra costs following the Falkland Islands action. This increase is over and above our commitment to meet the NATO 3 per cent per annum real growth target. It will fund purchases of equipment to replace losses this year, and will ensure the future security of the Islands.

To find room for these increases within an unchanged total, we have been able to secure economies elsewhere. We have also transferred to programmes part of the provisional Contingency Reserve set aside in the 1982 White Paper. But we have left a substantial Contingency Reserve of £1.5 billion, which we shall review again nearer the Budget.

Full details of public spending plans for next year and for 1984-85 and 1985-86 will be set out in the Public Expenditure White Paper which we expect to publish early in the New Year.

/My rt. hon. Friend

My rt. hon. Friend the Secretary of State for Social Services is this afternoon announcing details of changes in National Insurance Contribution rates and limits for next year, and will be publishing the Report of the Government Actuary on the National Insurance Fund. If we were fully to balance the Fund for next year, increases in employers' and employees' contributions of nearly 0.4 per cent each would be required. But we are concerned both to minimise additional burdens on industry, and to diminish the effects of contribution increases for employees. So we have decided that the increases should be limited to 0.25 per cent each for employers and employees. The Upper Earnings Limit will go up only to £235, rather than £245 which would be the maximum permitted by Statute. Taken together these measures mean that contributors will pay a little over £200 million less next year than would have been required fully to balance the Fund. The cost to the PSBR has been taken into account in the forecast.

/I turn now to

I turn now to the National Insurance Surcharge, introduced, and then increased to 3½ per cent, by the previous Government. It has long been criticised, and rightly so, by commerce and industry. As I said in my last Budget, it raises production costs, it is not rebatable on exports, and it either puts up prices or cuts into profits. I was able in March to announce an effective reduction of 1 per cent in the rate for private sector employers, from 3½ per cent to 2½ per cent, for the year 1982-83. I am pleased to inform the House that we can now take another substantial step in the right direction, by reducing the rate for 1983-84 by a further 1 per cent, so bringing it down to 1½ per cent. The cost of this to the PSBR has been reflected in the forecast. The public sector will not gain from the change, but the benefit to private employers in 1983-84 will be around £700 million. Overall, this will more than offset the increase in their costs due to the new NIC rates and levels. (A table showing the overall effect for employers and employees of the NIC and NIS changes for next year has today been put in the Vote Office.)

/That is not all.

That is not all. I intend that for private sector employers ½ per cent of the NIS reduction from April 1983 should be brought forward and made effective for 1982-83 also. Hon. Members will know that to change the NIS rate at this time of year presents considerable administrative problems. But we have found a way of overcoming them. The equivalent of a ½ per cent reduction for the whole year will be given by reductions in employers' payments of National Insurance Surcharge and National Insurance Contributions for January, February and March next year. Details and guidance will be sent in due course to employers.

This further benefit will be worth £350 million in the current year. Legislation will be needed for the new arrangements both this year and next. A Bill will be introduced at an early date. I am sure it will commend itself warmly to the House as providing a substantial reduction in the costs faced by private sector commerce and industry.

/Mr. Speaker, the House will

Mr. Speaker, the House will want to study the Autumn Statement carefully. The format is new, and I hope helpful, and the scope rather wider than before. And it demonstrates that we are determined, within the framework of our monetary and fiscal policies, to continue to do what we can to relieve the burden of taxation so as so move towards renewed growth and more employment. I hope to be able to say rather more if I am fortunate enough to catch your eye later in the course of our current debate.

DEPARTMENT OF INDUSTRY
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TELEPHONE DIRECT LINE 01-212 3301
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Secretary of State for Industry

6 December 1982

The Rt Hon Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1

RECEIVED
-7 DEC 1982
Mr Kemp 7/12
CST, FST, EST, MST^C, MST^R
Sir D. Wass Sir A Rawlinson,
Mr Burns, Mr Bailey,
Mr Middleton, Mr Burgner,
Mr Lovell, Mr Moore, PS/IR,
PS/C+E.

Budget Folder

Dear Geoffrey,

1983 BUDGET

It may be helpful to you at this stage if I set out the main industrial measures I hope you will consider for the next Budget and give an indication of my priorities.

2 Both your last Budget and the further measures you announced on 8 November gave considerable help to industry. Both packages were well received - not just by industry itself, but by the public generally. Help to make industry more enterprising and more competitive is widely seen as helping to save and create jobs. I hope, therefore, you will feel it right to use the 1983 Budget to give further substantial help to industry. In my view the industrial situation and prospects would justify such an emphasis. Despite improvements in productivity and efficiency, profitability is still much too low. There is still a long way to go to recover lost competitiveness. Reports suggest that in a number of sectors British firms are too weak to take advantage of any upswing in demand.

3 My suggestions are grouped under 3 broad headings. First, I hope you will be able to include at least one major measure affecting industry as a whole, as you were able to do in this year's Budget with the NIS reduction. Second, I hope you will be able to repeat the concept of including in the Budget an "innovation" package which you successfully introduced this year. Third, I hope you will build on the momentum of previous Budgets by including a further package of measures to encourage enterprise and small firms.

4 In addition, I have already written proposing a review of motoring taxes and, subject to the outcome, this might possibly be a fourth area where useful measures could be taken.

Major Industrial Measures

5 I intend to write to you again in the New Year with more detailed proposals under this heading when the convergence may be a little clearer. Developments on interest rates and the exchange rate will need to be carefully watched. The fall of interest rates (and of course of inflation) during the year has brought considerable benefit to industry and I certainly would not urge any measure which could put these helpful developments in jeopardy. Subject to that important point, I believe that so far as room for manoeuvre allows, the policy of reducing the costs imposed on industry remains the most valuable contribution we can make. The successive reductions of NIS to $1\frac{1}{2}\%$ from next April have been very welcome. My preliminary judgement is that to make further reductions of this tax should be the highest priority. Indeed, I hope you will consider announcing in the Budget the abolition of the NIS from the earliest convenient date in 1983. NIS adds directly to costs; it is a tax on exports as well as on employment; its abolition would be a further direct enhancement by Government of industry's competitiveness.

6 You are obviously considering full revalorisation of the personal income tax allowances in the Budget, and the possibility of going further on this or related fronts. I would not wish to argue against these measures in any way on their own merits. But despite the improvement to personal disposable income such measures would bring, I would not regard them as the best available way of helping industry at this stage. Industry's main problems remain on the supply side, as we appreciated before 1979, and our principal industrial measures should, I suggest, continue to be directed there. I have been impressed by the number of industrialists who reject the view that income tax cuts are likely to make a significant difference to wage settlements.

7 The main alternatives to further action on NIS are perhaps a reduction of the Corporation Tax rate (or the introduction of new allowances, eg on commercial buildings) or some action on non-domestic rates. On Corporation Tax, I believe we should have a reduction in mind for the longer term. But in present circumstances it would not substantially help many of the sectors facing the greatest competitive gaps. On rates, while we still await Michael Heseltine's proposals, I have reserved my position on cutting or capping non-domestic rates, which are now the biggest tax paid by industry and commerce. At this stage I believe action on the NIS should continue to have priority.

Energy Prices

8 Despite the useful measures announced on 8 November, this remains an area we must keep a close watch on. If by next spring it seems clear that further action is required to keep British industry's energy costs in line with competitors, I would hope you would give the necessary measures high priority.

INNOVATION

9 Under this heading I hope you will consider repeating the successful format you adopted this year of a combined package of tax and expenditure measures. I would certainly like to propose as a high priority that you announce a revival of the Small Engineering Firms Investment Scheme (SEFIS) in the Budget. This would be very well received in industry and would help this important sector to modernise itself. Some detailed changes to the previous scheme would probably be made and I will let you have these separately.

10 If you are willing to pursue the combined package approach, I should like to make further proposals for measures involving expenditure. The possibilities I am considering include:

i support for other innovation - linked investment in addition to SEFIS;

ii an expansion of our support for R&D, possibly including a response to the Alvey proposals;

iii increased support for technology transfer;

iv support for the development and improvement of management skills.

If you could let me know whether you favour this approach, I will develop these proposals further into more precise suggestions.

11 On the tax side I should like you to consider a further extension of the 100% first year capital allowance for rented teletext receivers. While recognising the general case for removing preferential capital allowances for rented consumer goods I believe special consideration should continue to be given to the position on teletext receivers. I am especially concerned to maintain the growth in the market in this area where British products compete successfully with imports, because it may prove to be the first stage in a succession of technological developments leading to cable TV, direct broadcasting by

satellite and interactive home terminal uses. Teletext and viewdata lost their marketing advantage over other sets with the removal of HP controls. An extension for a further year of the 100% first year allowance for teletext would bring it into line with viewdata. You will recall that I proposed a two year extension before this year's Budget with the same object in mind, but you only felt able to grant an extension for one year at that time.

12 My officials have prepared a paper setting out the arguments on teletext in more detail and will be in touch with yours shortly.

ENTERPRISE AND SMALL FIRMS

13 For convenience I am dividing my proposals under this important heading into major and minor items. I list the major items below in order of priority, and Annex A carries further details. The minor items are set out in Annex B. This distinction is purely for convenience and does not imply that I regard all the minor items as lower priority than the major. Some of the minor items should, I believe, have a high priority, as indicated in Annex B.

Share Option and Incentive Schemes

14 I attach the highest priority to improving the tax treatment of share option and incentive schemes. The present relatively unfavourable treatment of such arrangements is a major obstacle to the development of "growth" companies in the UK and contrasts unfavourably with the position in the US. The existing schemes are useful but they are tied to comparatively low limits and must be widely available to employees. I should like to see companies able to offer substantial schemes restricted, if they wish, to key executives to give them a real interest in the success of the company without incurring heavy income tax charges. I am convinced that this would give a strong incentive to executives to improve the performance of their companies. It would also help growing companies attract key managers by being able to offer attractive overall renumeration terms even though they may only be able to provide a modest salary in the early years.

15 I know that some companies are offering such schemes despite the present tax position. Even in such cases I believe a more generous tax treatment would so enhance the incentive effect of these schemes that the loss of revenue will in no sense be "wasted".

16 More details on this proposal are at Annex A. It goes beyond the small firms sector, of course, and could I believe form a major element in your Budget in its own right.

Encouraging Investment in Equity Capital

17 My second priority is that you should develop the valuable measures you have already introduced to encourage outside investment in the equity capital of small firms. The Business Start-Up Scheme is now proving its worth but is still being taken up relatively slowly. I hope you will announce in your next Budget that the scheme will be continued beyond its present expiry date in 1984, otherwise the uncertainty surrounding the scheme's future will inevitably affect it badly during 1983/84. I also hope you will be able substantially to increase the annual maximum allowed under the scheme and introduce the other improvements detailed at Annex A.

18 In parallel with this improvement to the Start-up Scheme, I believe we should extend the incentives to equity investment in established unquoted companies. This would simultaneously ease the provision of finance to established companies aiming to expand (and reduce their dependence on bank borrowing) and help to avoid the criticism that too many of our measures are directed towards start-ups.

19 I am attracted by the CBI's proposals on Small Firms Investment Companies which I know you have already considered. I hope you will consider introducing a scheme on the lines of these proposals. This would, I think, be particularly helpful if we are unable to meet the CBI on reducing the burden of non-domestic rates substantially, which is likely to be another of their main Budget proposals.

Loan Guarantee Scheme

20 The existing allocation to this valuable scheme is likely to be exhausted in February or March 1983. I am sure we should extend the scheme at least until its original 3-year term is completed, though we may wish to make some detailed adjustment to the scheme. This might require a further £150m, though I would need to re-examine this estimate nearer the time. This is, of course, an expenditure measure, subject to the normal conventions governing the treatment of guarantees for public expenditure survey purposes.

Stamp Duty

21 I consider that stamp duties on property conveyance should be reviewed again, both because a reduction would give a welcome boost to the construction industry and because it would assist labour mobility. I see particular merit in the suggestion that

stamp duty should be reduced for first-time buyers, to assist the buyers themselves and to provide a stimulus to the construction of smaller "starter" homes.

22 While on the subject of stamp duty, I would like to put on record my view that the tax bias against holding industrial shares and in favour of other forms of saving is something we must examine in the longer term. I am sure that this is one of the reasons for the decline of the individual investor in favour of the institutional investor.

The Self Employed and Agency Workers

23 I hope you will agree not to re-introduce the draft 1981 legislation on agency workers operating through companies. I am becoming concerned that current Inland Revenue policy is giving the wrong signal to the self-employed about Government attitudes towards them. The Inland Revenue must, of course, administer the law correctly as it sees it but I believe we must take care not to harass the self-employed and press-gang them into Schedule E unless this is fully justified by the facts.

Enterprise Bonds

24 The preceding three items I would rank as equal third in priority after the first two under this broad heading. Finally, I hope you will consider the proposal for "enterprise bonds" raised by John Loveridge, Graham Bright and others last year, though I believe it is of less importance than the previous measures. It is widely acknowledged that expenditure is sometimes incurred which may not be commercially justifiable in timing simply for the purposes of saving tax in a particular year. Enterprise bonds would be tax-deductible but taxable on redemption. In this way expenditure could be deferred until the most opportune time but the Treasury would have had use of the money meanwhile.

Minor Items

25 These are listed at Annex B, with an indication of my priorities between them.

CONCLUSION

26 I very much hope you will be able to include items from each of the broad headings I have suggested. I shall write to you again about possibilities for major industrial measures in the new year. In addition I shall develop detailed proposals for a

package of "innovation" expenditure measures if, as I hope, you see advantage in this course; and I may wish to return to the question of motoring taxes subject to the outcome of the review I have suggested.

27 I am copying this letter to the Prime Minister, Sir Robert Armstrong and John Sparrow.

Yours ever
Patrick

ENTERPRISE AND SMALL FIRMS

Further Detail of "Major" Measures Proposed

Share Option and Incentive Schemes

1 My detailed proposals are as follows:

- i a new scheme increasing the permitted maximum of approved share incentive or option schemes to £10,000pa or £50,000 overall.

- ii companies to be able to restrict eligibility for approved schemes to key executives if they wish.

- iii deferral until the shares are sold of any charge to tax arising on exercise of an option. Such charge to be to capital gains rather than income tax.

- iv a review of the rules relating to the growth in value charge particularly the definition of "restrictions" and the application of this charge to transactions involved in management buy-outs.

- v particular consideration to be given to charges facilitating shemes within groups of companies.

- vi particular consideration to be given to relaxing the present tax treatment of "partly-paid" schemes which can at present be adversely affected by the 1972 and 1976 Finance Acts. In most cases the employee in a "partly-paid" scheme is at risk from the value of shares going down as well as up, which would seem to justify capital gains treatment (I do not seek to disturb the "stop-loss" arrangements in the 1976 Finance Act).

Business Start-Up Schemes

2 I propose the following improvements:

- i increase the annual limit qualifying for relief to £50,000;

- ii increase the maximum shareholding permitted to any individual to 49%;

- iii abolish any restriction on the proportion of a company's shareholding eligible for relief;

iv relaxation of the relationship rules which determine who are connected persons. I think it is especially important, given our commitment to the family which has emerged from the Family Policy Group, that lineal antecedents and descendants should be eligible for relief;

v abolition of the requirement for a trading company to have traded for at least four months before relief can be granted (to be replaced by a mechanism to withdraw relief retrospectively if the company turns out to be non-qualifying). Experience shows that the existing requirement has a severe disincentive effect;

vi companies which license out a process not to be treated as disqualified. Particularly important in the new technology field;

vii extension of relief to trustees of family and similar settlements;

viii allow differentiation into classes of share capital other than merely as to voting rights; and admit participating preference shares and redeemable fixed rate preference shares;

ix abolition of the requirement that subsidiary companies of the qualifying company must be wholly owned provided the departure relates only to minority shareholdings taken by company employees.

ENTERPRISE AND SMALL FIRMS

"Minor" Items

1 The first two items listed below are high priority:

i) Small Firms' Corporation Tax

Much has already been done to bring down the rate in the marginal field; but this remains a continuing source of complaint. It is suggested that the marginal rate should be reduced still further by widening the band to £475,000 (upper) and £95,000 (lower) producing a marginal rate of 55%.

ii) VAT Threshold

Revalorisation would suggest a new main VAT registration limit of around £17,850. It is proposed that the limit be raised to £18,000 with suitable increases in the other limits.

2 The next group of items are roughly of equal importance, lower in priority than the first group:

iii) Scientific Research Allowances: Definition

At present these allowances are restricted to 'activities in the field of natural or applied science for the extension of knowledge'. This definition is too restrictive and uncertain, and excludes, for example, much expenditure of development (as opposed to original research) character; yet development is precisely the field in which our industries' efforts are often found lacking. It is proposed that the allowance should be suitably redefined along the lines of research and development, as many of our overseas competitors do.

iv) Interest Relief

Useful relaxations in the provisions relating to interest on loans taken out for the purpose of investing in a close company have been made over the last few years but these do not go far enough. It is proposed that the requirement that the company be close should be replaced by its merely being unquoted; and that all full-time employees (not merely managers) should potentially qualify for relief. Further, now that sleeping partners can qualify for interest relief on loans for partnership investment there seems to be no reason why limited partners should be discriminated against and this should be removed.

v) Business Formation and other Legal Costs

Relief should be made available to those relatively minor capital costs which are incurred for reasons such as setting up the framework of a business or establishing an

incentive scheme. These are legitimate business costs and there seems to be no reason why they should not be allowed.

vi) Capital Gains Tax Rollover Relief

It is unfortunate that, while relief is available on disposal of business assets which are replaced, no similar relief is available on disposal of shares in unquoted trading companies even though these may be replaced by other unquoted trading company shares or business assets. The proposal is that rollover relief should be extended to include rollover into or out of unquoted trading company shares, subject to safeguards similar to those which apply to retirement relief.

vii) Loss Relief Carry Back for new Companies

At present the special relief for losses sustained in the first few years of a new business is available only to unincorporated traders. It is undesirable that normal commercial considerations as between incorporation and non-incorporation should be affected by fiscal distortions. I propose that the relief should be available according to participants' interests in a newly-trading company.

3 Finally, the following item is lower priority but has nevertheless caused problems in particular cases:

viii) Assets Acquired in a Series of Transactions

A problem sometimes arises, particularly with family company shares, that a series of disposals to a connected person falls foul of the special capital gains tax rules such that the value to the disposers is taken to be the (higher) proportionate majority holding value rather than the (lower) minority holding value. This can result in excessive CGT burdens on the disposing minority holders, and this should be remedied.

JH 447

CONFIDENTIAL

Secretary of State for Industry

DEPARTMENT OF INDUSTRY
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(1)

C

This is very clear, timely and helpful. Would you like to send a quick letter saying so?

+ JOM?

saying *, ‡

(All our points are to [illegible] ... constraints – [illegible] & priorities)

EXCHEQUER
-7 DEC 1982
ACTION: Mr Kemp 7/12
COPIES TO: CST, FST, EST, MST C, MST R, Sir D Wass, Sir A Rawlinson, Mr Burns, Mr Bailey, Mr Middleton, Mr Burgner, Mr Lovell, Mr Moore, PS/IR, PS/C&E.

6 December 1982

The Rt Hon Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1

Dear Geoffrey,

1983 BUDGET

It may be helpful to you at this stage if I set out the main industrial measures I hope you will consider for the next Budget and give an indication of my priorities.

2 Both your last Budget and the further measures you announced on 8 November gave considerable help to industry. Both packages were well received - not just by industry itself, but by the public generally. Help to make industry more enterprising and more competitive is widely seen as helping to save and create jobs. I hope, therefore, you will feel it right to use the 1983 Budget to give further substantial help to industry. In my view the industrial situation and prospects would justify such an emphasis. Despite improvements in productivity and efficiency, profitability is still much too low. There is still a long way to go to recover lost competitiveness. Reports suggest that in a number of sectors British firms are too weak to take advantage of any upswing in demand.

3 My suggestions are grouped under 3 broad headings. First, I hope you will be able to include at least one major measure affecting industry as a whole, as you were able to do in this year's Budget with the NIS reduction. Second, I hope you will be able to repeat the concept of including in the Budget an "innovation" package which you successfully introduced this year. Third, I hope you will build on the momentum of previous Budgets by including a further package of measures to encourage enterprise and small firms.

4 In addition, I have already written proposing a review of motoring taxes and, subject to the outcome, this might possibly be a fourth area where useful measures could be taken.

Major Industrial Measures

5 I intend to write to you again [early] in the New Year with more detailed proposals under this heading when the convergence may be a little clearer. Developments on interest rates and the exchange rate will need to be carefully watched. The fall of interest rates (and of course of inflation) during the year has brought considerable benefit to industry and I certainly would not urge any measure which could put these helpful developments in jeopardy. Subject to that important point, I believe that so far as room for manoeuvre allows, the policy of reducing the costs imposed on industry remains the most valuable contribution we can make. The successive reductions of NIS to 1½% from next April have been very welcome. My preliminary judgement is that to make further reductions of this tax should be the highest priority. Indeed, I hope you will consider announcing in the Budget the abolition of the NIS from the earliest convenient date in 1983. NIS adds directly to costs; it is a tax on exports as well as on employment; its abolition would be a further direct enhancement by Government of industry's competitiveness.

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Energy Prices

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INNOVATION

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10 If you are willing to pursue the combined package approach, I should like to make further proposals for measures involving expenditure. The possibilities I am considering include:

- i support for other innovation - linked investment in addition to SEFIS;
- ii an expansion of our support for R&D, possibly including a response to the Alvey proposals;
- iii increased support for technology transfer;
- iv support for the development and improvement of management skills.

If you could let me know whether you favour this approach, I will develop these proposals further into more precise suggestions.

11 On the tax side I should like you to consider a further extension of the 100% first year capital allowance for rented teletext receivers. While recognising the general case for removing preferential capital allowances for rented consumer goods I believe special consideration should continue to be given to the position on teletext receivers. I am especially concerned to maintain the growth in the market in this area where British products compete successfully with imports, because it may prove to be the first stage in a succession of technological developments leading to cable TV, direct broadcasting by

without commitment

satellite and interactive home terminal uses. Teletext and viewdata lost their marketing advantage over other sets with the removal of HP controls. An extension for a further year of the 100% first year allowance for teletext would bring it into line with viewdata. You will recall that I proposed a two year extension before this year's Budget with the same object in mind, but you only felt able to grant an extension for one year at that time.

12 My officials have prepared a paper setting out the arguments on teletext in more detail and will be in touch with yours shortly.

ENTERPRISE AND SMALL FIRMS

13 For convenience I am dividing my proposals under this important heading into major and minor items. I list the major items below in order of priority, and Annex A carries further details. The minor items are set out in Annex B. This distinction is purely for convenience and does not imply that I regard all the minor items as lower priority than the major. Some of the minor items should, I believe, have a high priority, as indicated in Annex B.

Share Option and Incentive Schemes

14 I attach the highest priority to improving the tax treatment of share option and incentive schemes. The present relatively unfavourable treatment of such arrangements is a major obstacle to the development of "growth" companies in the UK and contrasts unfavourably with the position in the US. The existing schemes are useful but they are tied to comparatively low limits and must be widely available to employees. I should like to see companies able to offer substantial schemes restricted, if they wish, to key executives to give them a real interest in the success of the company without incurring heavy income tax charges. I am convinced that this would give a strong incentive to executives to improve the performance of their companies. It would also help growing companies attract key managers by being able to offer attractive overall renumeration terms even though they may only be able to provide a modest salary in the early years.

15 I know that some companies are offering such schemes despite the present tax position. Even in such cases I believe a more generous tax treatment would so enhance the incentive effect of these schemes that the loss of revenue will in no sense be "wasted".

16 More details on this proposal are at Annex A. It goes beyond the small firms sector, of course, and could I believe form a major element in your Budget in its own right.

Encouraging Investment in Equity Capital

17 My second priority is that you should develop the valuable measures you have already introduced to encourage outside investment in the equity capital of small firms. The Business Start-Up Scheme is now proving its worth but is still being taken up relatively slowly. I hope you will announce in your next Budget that the scheme will be continued beyond its present expiry date in 1984, otherwise the uncertainty surrounding the scheme's future will inevitably affect it badly during 1983/84. I also hope you will be able substantially to increase the annual maximum allowed under the scheme and introduce the other improvements detailed at Annex A.

18 In parallel with this improvement to the Start-up Scheme, I believe we should extend the incentives to equity investment in established unquoted companies. This would simultaneously ease the provision of finance to ~~established~~ companies aiming to expand (and reduce their dependence on bank borrowing) and help to avoid the criticism that too many of our measures are directed towards start-ups.

19 I am attracted by the CBI's proposals on Small Firms Investment Companies which I know you have already considered. I hope you will consider introducing a scheme on the lines of these proposals. This would, I think, be particularly helpful if we are unable to meet the CBI on reducing the burden of non-domestic rates substantially, which is likely to be another of their main Budget proposals.

Loan Guarantee Scheme

20 The existing allocation to this valuable scheme is likely to be exhausted in February or March 1983. I am sure we should extend the scheme at least until its original 3-year term is completed, though we may wish to make some detailed adjustment to the scheme. This might require a further £150m, though I would need to re-examine this estimate nearer the time. This is, of course, an expenditure measure, subject to the normal conventions governing the treatment of guarantees for public expenditure survey purposes.

Stamp Duty

21 I consider that stamp duties on property conveyance should be reviewed again, both because a reduction would give a welcome boost to the construction industry and because it would assist labour mobility. I see particular merit in the suggestion that

stamp duty should be reduced for first-time buyers, to assist the buyers themselves and to provide a stimulus to the construction of smaller "starter" homes.

22 While on the subject of stamp duty, I would like to put on record my view that the tax bias against holding industrial shares and in favour of other forms of saving is something we must examine in the longer term. I am sure that this is one of the reasons for the decline of the individual investor in favour of the institutional investor.

The Self Employed and Agency Workers

23 I hope you will agree not to re-introduce the draft 1981 legislation on agency workers operating through companies. I am becoming concerned that current Inland Revenue policy is giving the wrong signal to the self-employed about Government attitudes towards them. The Inland Revenue must, of course, administer the law correctly as it sees it but I believe we must take care not to harass the self-employed and press-gang them into Schedule E unless this is fully justified by the facts.

Enterprise Bonds

24 The preceding three items I would rank as equal third in priority after the first two under this broad heading. Finally, I hope you will consider the proposal for "enterprise bonds" raised by John Loveridge, Graham Bright and others last year, though I believe it is of less importance than the previous measures. It is widely acknowledged that expenditure is sometimes incurred which may not be commercially justifiable in timing simply for the purposes of saving tax in a particular year. Enterprise bonds would be tax-deductible but taxable on redemption. In this way expenditure could be deferred until the most opportune time but the Treasury would have had use of the money meanwhile.

Minor Items

25 These are listed at Annex B, with an indication of my priorities between them.

CONCLUSION

26 I very much hope you will be able to include items from each of the broad headings I have suggested. I shall write to you again about possibilities for major industrial measures in the new year. In addition I shall develop detailed proposals for a

package of "innovation" expenditure measures if, as I hope, you see advantage in this course; and I may wish to return to the question of motoring taxes subject to the outcome of the review I have suggested.

NB 27 I am copying this letter to the Prime Minister, Sir Robert Armstrong and John Sparrow.

✓? A pity about JS; but this could be rather a useful shot across the bows of [illegible] to sell on "The Thresholds" School.

[illegible]

✓✓

Yours ever

Peter

ENTERPRISE AND SMALL FIRMS

Further Detail of "Major" Measures Proposed

Share Option and Incentive Schemes

1 My detailed proposals are as follows:

- i a new scheme increasing the permitted maximum of approved share incentive or option schemes to £10,000pa or £50,000 overall.

- ii companies to be able to restrict eligibility for approved schemes to key executives if they wish.

- iii deferral until the shares are sold of any charge to tax arising on exercise of an option. Such charge to be to capital gains rather than income tax.

- iv a review of the rules relating to the growth in value charge particularly the definition of "restrictions" and the application of this charge to transactions involved in management buy-outs.

- v particular consideration to be given to charges facilitating shcmes within groups of companies.

- vi particular consideration to be given to relaxing the present tax treatment of "partly-paid" schemes which can at present be adversely affected by the 1972 and 1976 Finance Acts. In most cases the employee in a "partly-paid" scheme is at risk from the value of shares going down as well as up, which would seem to justify capital gains treatment (I do not seek to disturb the "stop-loss" arrangements in the 1976 Finance Act).

Business Start-Up Schemes

2 I propose the following improvements:

- i increase the annual limit qualifying for relief to £50,000;

- ii increase the maximum shareholding permitted to any individual to 49%;

- iii abolish any restriction on the proportion of a company's shareholding eligible for relief;

CONFIDENTIAL

iv relaxation of the relationship rules which determine who are connected persons. I think it is especially important, given our commitment to the family which has emerged from the Family Policy Group, that lineal antecedents and descendants should be eligible for relief;

v abolition of the requirement for a trading company to have traded for at least four months before relief can be granted (to be replaced by a mechanism to withdraw relief retrospectively if the company turns out to be non-qualifying). Experience shows that the existing requirement has a severe disincentive effect;

vi companies which license out a process not to be treated as disqualified. Particularly important in the new technology field;

vii extension of relief to trustees of family and similar settlements;

viii allow differentiation into classes of share capital other than merely as to voting rights; and admit participating preference shares and redeemable fixed rate preference shares;

ix abolition of the requirement that subsidiary companies of the qualifying company must be wholly owned provided the departure relates only to minority shareholdings taken by company employees.

ENTERPRISE AND SMALL FIRMS

"Minor" Items

1 The first two items listed below are high priority:

i) Small Firms' Corporation Tax

Much has already been done to bring down the rate in the marginal field; but this remains a continuing source of complaint. It is suggested that the marginal rate should be reduced still further by widening the band to £475,000 (upper) and £95,000 (lower) producing a marginal rate of 55%.

ii) VAT Threshold

Revalorisation would suggest a new main VAT registration limit of around £17,850. It is proposed that the limit be raised to £18,000 with suitable increases in the other limits.

2 The next group of items are roughly of equal importance, lower in priority than the first group:

iii) Scientific Research Allowances: Definition

At present these allowances are restricted to 'activities in the field of natural or applied science for the extension of knowledge'. This definition is too restrictive and uncertain, and excludes, for example, much expenditure of development (as opposed to original research) character; yet development is precisely the field in which our industries' efforts are often found lacking. It is proposed that the allowance should be suitably redefined along the lines of research and development, as many of our overseas competitors do.

iv) Interest Relief

Useful relaxations in the provisions relating to interest on loans taken out for the purpose of investing in a close company have been made over the last few years but these do not go far enough. It is proposed that the requirement that the company be close should be replaced by its merely being unquoted; and that all full-time employees (not merely managers) should potentially qualify for relief. Further, now that sleeping partners can qualify for interest relief on loans for partnership investment there seems to be no reason why limited partners should be discriminated against and this should be removed.

v) Business Formation and other Legal Costs

Relief should be made available to those relatively minor capital costs which are incurred for reasons such as setting up the framework of a business or establishing an

incentive scheme. These are legitimate business costs and there seems to be no reason why they should not be allowed.

vi) Capital Gains Tax Rollover Relief

It is unfortunate that, while relief is available on disposal of business assets which are replaced, no similar relief is available on disposal of shares in unquoted trading companies even though these may be replaced by other unquoted trading company shares or business assets. The proposal is that rollover relief should be extended to include rollover into or out of unquoted trading company shares, subject to safeguards similar to those which apply to retirement relief.

vii) Loss Relief Carry Back for new Companies

At present the special relief for losses sustained in the first few years of a new business is available only to unincorporated traders. It is undesirable that normal commercial considerations as between incorporation and non-incorporation should be affected by fiscal distortions. I propose that the relief should be available according to participants' interests in a newly-trading company.

3 Finally, the following item is lower priority but has nevertheless caused problems in particular cases:

viii) Assets Acquired in a Series of Transactions

A problem sometimes arises, particularly with family company shares, that a series of disposals to a connected person falls foul of the special capital gains tax rules such that the value to the disposers is taken to be the (higher) proportionate majority holding value rather than the (lower) minority holding value. This can result in excessive CGT burdens on the disposing minority holders, and this should be remedied.

RESTRICTED

FROM: D R NORGROVE

7 December 1982

1. MR ~~KEMP~~
2. CHANCELLOR

I have slightly amended the draft letters. G

c c Chief Secretary
Sir Douglas Wass
Sir Anthony Rawlinson
Mr Burns
Mr Middleton
Mr Bailey
Mr Burgner
Mr Moore
Mr Wicks
Mr Ridley
Mr Harris
Mr French

BUDGET REPRESENTATIONS

You asked for draft letters to send to the Secretary of State for Energy and Trade to seek their ideas for the 1983 Budget. These I attach. The second paragraph of each letter is there simply to warn that other colleagues have not been sent similar letters.

The DOE have been told that we would like to have Mr Heseltine's representations before Christmas if possible.

D R Norgrove

D R NORGROVE

Personal + Confidential ✓ 10/12

~~DRAFT~~ LETTER FOR THE CHANCELLOR OF THE EXCHEQUER TO SEND TO :

The Rt. Hon Lord Cockfield,
Secretary of State for Trade
1 Victoria Street
London SW1

At about this time of year - as you well know - I start to receive a flood of representations about the next Budget. ~~I would be very glad if you felt able to add your own to them fairly soon~~. You have already written about the tourist industry. But I would welcome views and suggestions from you in other areas, as an ex Treasury Minister, - though by the same token you will know I may not be able to accept them! And I know I need not stress ~~Anything you might to let me have would be welcome earlier rather than later.~~ The importance of ~~letting me~~ ensuring that ~~telling me have~~ any points you wish me to take into account reach me as early as possible in the New Year.

I am sending a similar letter to Nigel Lawson.

GH.

Pl. type
(and see one below)

LP

Personal & Confidential,

√10/12

~~DRAFT LETTER~~ FOR THE CHANCELLOR OF THE EXCHEQUER TO SEND TO :

The Rt. Hon Nigel Lawson MP,
Secretary of State for Energy
Thames House South
Millbank
London SW1

At about this time of year - as you well know - I start to receive a flood of representations about the next Budget. I ~~would be very glad if you felt able to add some of your own to them fairly~~ soon. I am of course already fully in the picture about the North Sea Tax Regime. But I would welcome views and suggestions from you, in other areas, as ~~coming from~~ an ex Treasury Minister, - though by the same token you will know I may not be able to accept them! ~~Anything you may like to contribute would be welcome earlier rather than later.~~ And I know I need not stress the importance of ensuring that any points you wish me to take into account reach me as early as possible in the New Year.

I am sending a similar letter to Arthur Cockfield.

GH

3.43

CONFIDENTIAL

(mwp)
Budget

FROM: J O KERR
DATE: 8 December 1982

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir D Wass
Sir A Rawlinson
Mr Burns
Mr Bailey
Mr Middleton
Mr Burgner
Mr Lovell
Mr Moore

MR KEMP

BUDGET: MR JENKIN'S LETTER OF 6 DECEMBER

The Chancellor finds Mr Jenkin's letter of 6 December very helpful, and believes that all the points in it deserve serious consideration. In the meantime, he would like to send a quick reply, which would - as a minimum -

a. express his thanks for clear, timely and helpful advice;

b. ask that the promised letter with more detailed proposals on "major industrial measures" (paragraph 5) should arrive very early in the New Year;

c. say that he does not exclude the kind of combined "innovation" package, involving some expenditure measures, suggested in paragraph 10, and would therefore be content to receive, without commitment, the more precise suggestions which Mr Jenkin is considering working up.

You may think that it might also be appropriate for the reply to note and agree with the third sentence of paragraph 5 of Mr Jenkin's letter.

2. Could you let me have an early draft?

J O KERR

pwp with Budget MPs
File

8 December 1982

PERM. SEC'S. OFFICE

Copies to

Sir Douglas Wass GCB
HM Treasury
Parliament Street
London
SW1P 3AG

MR KEMP
MR TURNBULL
MR KERR

My dear Douglas

Thank you for your letter of 6 December. I shall certainly let the Chancellor have a paper in the week beginning 10 January.

Yours ever

[illegible]

CONFIDENTIAL

FROM: JOHN GIEVE

DATE: 9 December 1982

~~PRINCIPAL~~ PRIVATE SECRETARY

cc Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir D Wass
Sir A Rawlinson
Mr Burns
Mr Bailey
Mr Middleton
Mr Kemp
Mr Burgner
Mr Lovell
Mr Moore
PS/IR
PS/C&E

1983 BUDGET

The Chief Secretary has read Mr Jenkin's letter of 6 December. At this stage the only comment he would make is that he is very strongly opposed indeed to the approach suggested in paragraph 10 of the letter. In his view, we should do absolutely nothing to encourage expenditure proposals. At the very most we should contemplate a revival of SEFIS but should certainly not encourage a second round of out of season public expenditure bids.

JG

JOHN GIEVE

CONFIDENTIAL

FROM: E P KEMP
9 December 1982

PRINCIPAL PRIVATE SECRETARY

cc PS/Chief Secretary
Mr Bailey
Mr Middleton
Mr Lovell
Mr Mountfield
Mr Norgrove

1983 BUDGET - MR JENKIN'S LETTER

I saw Mr Gieve's minute to you of today about paragraph 10 of Mr Jenkin's letter of 6 December after I had put forward to you earlier today a draft reply for the Chancellor to send. On the question of paragraph 10 of Mr Jenkin's letter, and the possibility of "packages" at Budget time including a public expenditure component, the draft reply I have submitted lined up with your minute to me of yesterday, and indeed with the view, as I recollect it, that the Chancellor took when the point came up at a meeting with Mr Jenkin, at which the Chief Secretary was present, last September. My recollection is very clearly that the Chancellor then, in Mr Jenkin's presence, did not rule out the possibility of public expenditure measures at Budget time, and not just in the SEFIS context.

2. The Chancellor and the Chief Secretary may like to consider together the line to take in the reply to Mr Jenkin, and whether paragraph 3 of my draft goes too far. It certainly was not intended to encourage a whole round of out of season public expenditure bids, but merely to endorse the possibility of mixed packages. Perhaps the Chief Secretary's point would be met by rewording the second sentence of paragraph 3 of my draft as follows :-

> "In principle, the right time for public expenditure decisions to be taken is in the context of the public expenditure round, and not out of season, so to speak, in the context of the Budget. But that said, I accept that there can be areas when, as last year, a modest public expenditure component can add to the worthwhileness and attractiveness of various packages, and I would not therefore rule out repeating last year's format. Without

necessarily committing myself to agreeing with what you have in mind, therefore, I shall be glad to have your more worked up proposals for the possibilities you mention in paragraph 10."

EPK

E P KEMP

FROM: E P KEMP
9 December 1982

PRINCIPAL PRIVATE SECRETARY

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir Douglas Wass
Sir Anthony Rawlinson
Mr Burns
Mr Bailey
Mr Middleton
Mr Burgner
Mr Lovell
Mr Mountfield
Mr Moore
Mr Ridley
Mr Norgrove

BUDGET - MR JENKIN'S LETTER OF 6 DECEMBER

Here is a draft reply for you to send to Mr Jenkin, responding to his letter of 6 December. This reply takes account of the points made in Mr Kerr's minute to me of yesterday.

2. So far as the handling of the individual proposals in Mr Jenkin's letter goes, the relatively detailed points will be included in the marshalling of candidates for "Budget packages", which FP are expecting to submit to you very shortly. Thereafter, they will be carried forward as part of consideration of the various packages to which they seem to belong. The major more strategic points (for instance Mr Jenkin's paragraphs 5 to 7) will of course come in for consideration when looking at the strategy of the Budget overall, which will start to take full shape in the drafting of the papers for discussion at Chevening.

E P KEMP

Confidential.

Pl. type

DRAFT LETTER FOR THE CHANCELLOR OF THE EXCHEQUER TO SEND TO :

The Rt. Hon Patrick Jenkin MP,
Secretary of State for Industry
1 Victoria Street
Millbank Tower
London SW1

1983 BUDGET

The clear, timely and helpful advice in

I am writing to thank you for the your letter of 6 December. ~~This was~~ the ~~clear, timely and helpful, and I shall certainly be studying what you say.~~

~~2.~~ I look forward to the further ~~letter~~ advice on major industrial measures & which you ~~refer to~~ mention in your paragraph 5 ~~of your letter.~~ I hope that you will be able to let me have ~~this~~ it very early in the New Year.

2. You mentioned that ~~3. In paragraphs 9 and 10 of your letter you refer to the format that was adopted in~~ my last Budget ~~in certain areas whereby a~~ contained ~~a number of~~ "packages", some of which ~~combined package of tax and expenditure measures was devised and presented. In principle~~ I certainly ~~would~~ do not rule out repeating this ~~format, and, without necessarily committing myself to agreeing to what you have in mind I shall be glad to have your more worked up proposals for the possibilities you mention~~ arrangement in the 1983 Budget, and I should be happy to receive the worked up proposals mentioned in your paragraph 10. You will of course ~~The sooner~~ ~~The~~ The sooner that they too can be made available, the better - though I ~~[illegible]~~

a package of fiscal and expenditure measures to encourage innovation.

3. You would not I think expect me to go very far now in expressing a view on the sort of broad issues ~~which you~~ set out ~~, for instance~~ in your paragraphs 5 to 7. ~~of your letter. As you know, whether and if so how far I shall have~~ How much, if any, room for manoeuvre I shall have ~~in my forthcoming Budget~~ is as yet unclear; as is the way in which any such scope might be used - for instance, as between measures directly affecting industry or measures directly affecting individuals. But I ~~would~~ certainly ~~endorse the important point you make towards the start of your paragraph 5 about the way the recent~~ agree with you on the benefits to industry from falls in interest and inflation rates ~~have brought benefit to industry,~~ and the crucial importance of not taking measures which might put these benefits ~~in jeopardy~~ at risk.

~~be able to let you know until close to the time of the Budget whether I shall adopt all or any of them~~

may not be able to let you know until close to the time of the Budget whether I shall be able to adopt all or any of them

JM

PERSONAL AND CONFIDENTIAL

PWP

Budget

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

cc CST
Sir D Wass
Sir A Rawlinson
Mr Burns
Mr Middleton
Mr Bailey
Mr Burgner
Mr Moore
Mr Wicks
Mr Ridley
Mr Harris
Mr French
Mr Kemp
Mr Norgrove

10 December 1982

The Rt. Hon. Nigel Lawson MP
Secretary of State for Energy

Dear Nigel

At about this time of year - as you well know - I start to receive a flood of representations about the next Budget. I am of course already fully in the picture about the North Sea Tax Regime. But I would welcome views and suggestions from you, as an ex-Treasury Minister, in other areas, - though by the same token you will know I may not be able to accept them! And I know I need not stress the importance of ensuring that any points you wish me to take into account reach me as early as possible in the New Year.

I am sending a similar letter to Arthur Cockfield.

GEOFFREY HOWE

4.47

PERSONAL AND CONFIDENTIAL

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

10 December 1982

The Rt. Hon. Lord Cockfield
Secretary of State for Trade

Dear Arthur

At about this time of year - as you well know - I start to receive a flood of representations about the next Budget. You have already written about the tourist industry. But I would welcome views and suggestions from you, as an ex-Treasury Minister, in other areas - though by the same token you will know I may not be able to accept them! And I know I need not stress the importance of ensuring that any points you wish me to take into account reach me as early as possible in the New Year.

I am sending a similar letter to Nigel Lawson.

Yours ever,

Geoffrey

GEOFFREY HOWE

FROM: JOHN GIEVE
DATE: 10 December 1982

PRINCIPAL PRIVATE SECRETARY

cc Mr Bailey
Mr Middleton
Mr Kemp
Mr Lovell
Mr Mountfield
Mr Norgrove

1983 BUDGET - MR JENKIN'S LETTER

The Chief Secretary has seen Mr Kemp's two minutes of 9 December. He does not think that the revised wording in the second minute meets his point. He suggests the following:

> "The right time for public expenditure decisions to be taken is in the context of the Public Expenditure Survey and not in the context of the Budget. I accept that SEFIS is something of a special case but beyond that I doubt whether there should be extra expenditure measures in the packages we envisage."

2. This would not preempt Budget decisions nor stop Mr Jenkin putting forward bids for extra expenditure where he thought those most justified but it would sound the right discouraging note.

JG

JOHN GIEVE

FROM: E P KEMP
10 December 1982

PRINCIPAL PRIVATE SECRETARY

cc PS/Chief Secretary

1983 BUDGET - MR JENKIN'S LETTER

At the risk of being caught up in a nasty maul, can I just comment on the revised paragraph 2 of the draft letter to Mr Jenkin which you have circulated today.

2. I am not sure it is a very good idea simply to limit the reference to innovation. To start with, Mr Jenkin might well say why is SEFIS a special case while the rest he may propose on innovation is not. He might go on to wonder, on the basis of the draft as it stands, whether it is just innovation (apart from SEFIS) where we don't want to see more public expenditure, or whether this is a general proposition. If it is the former, he would, as I say, wonder why pick on innovation, and if it is the latter he might well find, come the Budget, that we have introduced some more expenditure measures (in quite different fields - for instance perhaps unemployment measures or possibly a non-achievement of the full £180 million on social security), and think then that he had been a bit misled. I wonder too about the reference to the Public Expenditure Survey and the statement that "public expenditure decisions should of course be taken in that context". This is absolutely true, of course, (and I think it was me who first introduced the phrase into this round of drafting) but when I look at it again I wonder whether this would not encourage Mr Jenkin to come back on the whole principle of the public expenditure round, "Armstrong" and the like - which as you know he earlier showed signs of doing.

3. It would be helpful if we could identify, if only for ourselves, just what our position actually is. As I see it, it is indeed that public expenditure decisions should be taken in the context of the public expenditure round; but that, as last year, some modest additions between the public expenditure round and the Budget would not be inadmissible where they make good sense in economic, political, etc terms, and subject to any overriding consideration as to totals on the public expenditure side - thus, for instance, clearly no

additional public expenditure could be admitted which took the totals for 1983-84 above those set out in Cmnd 8494 for that year.

4. Taking account of these considerations, I wonder if I could try my hand at yet another draft of paragraph 2 of the letter to Mr Jenkin, as follows :-

> "You mention that my last Budget contained a package of tax and expenditure measures to encourage innovation. I am, of course, always reluctant to add to public expenditure, and particularly when we have just completed a public expenditure round, given our overriding policy objective that expenditure should be restrained and reduced.
>
> Thus Leon Brittan and myself would require a great deal of convincing before we could agree to extra expenditure measures in the packages we envisage. Nevertheless, I should be prepared to have a look at the worked up proposals mentioned in your paragraph 10. The sooner they can be made available, the better - though I may not be able to let you know until close to the time of the Budget whether I shall be able to adopt all or any of them."

E P KEMP

FROM: J O KERR
10 December 1982

PS/CHIEF SECRETARY

cc - Mr Kemp

1983: MR JENKIN'S LETTER OF 6 DECEMBER

Thank you for your minutes of 9 and 10 December about how the Chancellor should reply to Mr Jenkin.

2. It strikes me that it might help us achieve an agreed text if the "packages" paragraph in the reply deals only with "innovation". Could you let me know today whether the Chief Secretary would be content with the attached revised draft?

JOK.

J O KERR

A DRAFT LETTER FROM THE CHANCELLOR TO:-

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry

1983 BUDGET

Many thanks for the clear, timely and helpful advice in your letter of 6 December. I look forward to the further suggestions on major industrial measures which you mention in your paragraph 5: I hope that you will be able to let me have these very early in the New Year.

2. You mention that my last Budget contained a package of fiscal and expenditure measures to encourage innovation. Public expenditure decisions should of course be taken in the context of the Public Expenditure Survey, and not that of the Budget. I accept that SEFIS is something of a special case, but beyond that I am inclined to doubt whether there should be extra expenditure measures in any 1983 Innovation package. Nevertheless, I should be prepared to have a look at the worked-up proposals mentioned in your paragraph 10. The sooner that they can be made available, the better - though I may not be able to let you know until close to the time of the Budget whether I shall be able to adopt all or any of them.

3. You would not I think expect me to comment substantively ~~now~~ at this stage on the broad issues set out in paragraphs 5 to 7 of your letter. How much, if any, room for manoeuvre I shall have at Budget-time is as yet unclear; as is the way in which any such scope might be used - for instance, between measures directly affecting industry and measures directly affecting individuals. But I certainly agree with you on the benefits to industry from falls in the interest and inflation rates; and on the crucial importance of not taking measures which might put these benefits at risk.

Further compromise text agreed with PS/CST

PPS
The Chief Secretary was still a little unhappy with the draft and has proposed the marked amendments
JG.

FROM: J O KERR
10 December 1982

~~PS/~~CHIEF SECRETARY

cc - Mr Kemp

1983: MR JENKIN'S LETTER OF 6 DECEMBER

Thank you for your minutes of 9 and 10 December about how the Chancellor should reply to Mr Jenkin.

2. It strikes me that it might help us achieve an agreed text if the "packages" paragraph in the reply deals only with "innovation". Could you let me know today whether the Chief Secretary would be content with the attached revised draft?

JOK.

J O KERR

Carg — Pl. type.

~~A~~ DRAFT LETTER FROM THE CHANCELLOR TO:-

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry

1983 BUDGET

Many thanks for the clear, timely and helpful advice in your letter of 6 December. I look forward to the further suggestions on major industrial measures which you mention in your paragraph 5: I hope that you will be able to let me have these ~~at any rate the proposals~~ very early in the New Year.

2. You mention that my last Budget contained a package of fiscal and expenditure measures to encourage innovation. Public expenditure decisions should of course be taken in the context of the Public Expenditure Survey, and not that of the Budget. I accept that SEFIS is something of a special case. ~~but~~ Beyond that I ~~am inclined to~~ doubt whether there should be extra expenditure measures in any 1983 Innovation package, ~~although I will, of course, consider any proposals you bring forward.~~ ~~Nevertheless, I should be prepared to have a look at the worked-up proposals mentioned in your paragraph 10.~~ ~~The sooner that they can be made available, the better~~ you can let me have them - though I may not be able to let you know until close to the time of the Budget whether I shall be able to adopt all or any of them.

although I am still willing to have a look at the ideas mentioned in your paragraph 10. If you want to pursue them,

3. You would not I think expect me to comment substantively ~~now~~ at this stage on the broad issues set out in paragraphs 5 to 7 of your letter. How much, if any, room for manoeuvre I shall have at Budget-time is as yet unclear; as is the way in which any such scope might be used - for instance, between measures directly affecting industry and measures directly affecting individuals. But I certainly agree with you on the benefits to industry from falls in the interest and inflation rates; and on the crucial importance of not taking measures which might put these benefits at risk.

[initials]

CONFIDENTIAL

CST: FST: EST:
MSTC: MSTR.
SIR D. WASS
SIR A. RAWLINSON.
MR BURNS
MR BAILEY.
MR MIDDLETON.
MR BURGNER.
MR LOVELL
MR MOORE.
MR KEMP.
PS/IR: PS/C&E

(PW)

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

10 December 1982

The Rt. Hon. Patrick Jenkin, MP
Secretary of State for Industry

Dear Patrick

1983 BUDGET

Many thanks for the clear, timely and helpful advice in your letter of 6 December. I look forward to the further suggestions on major industrial measures which you mention in your paragraph 5: I hope that you will be able to let me have these very early in the New Year.

You mention that my last Budget contained a package of fiscal and expenditure measures to encourage innovation. Public expenditure decisions should of course be taken in the context of the Public Expenditure Survey, and not that of the Budget. I accept that SEFIS is something of a special case. Beyond that I doubt whether there should be extra expenditure measures in any 1983 Innovation package although I am willing to have a look at the ideas mentioned in your paragraph 10. If you want to pursue them, the sooner you can let me have them, the better - though I may not be able to let you know until close to the time of the Budget whether I shall be able to adopt all or any of them.

You would not I think expect me to comment substantively at this stage on the broad issues set out in paragraphs 5 to 7 of your letter. How much, if any, room for manoeuvre I shall have at Budget-time is as yet unclear; as is the way in which any such scope might be used - for instance, between measures directly affecting industry and measures directly affecting individuals. But I certainly agree with you on the benefits to industry from falls in the interest and inflation rates; and on the crucial importance of not taking measures which might put these benefits at risk.

Geoffrey

GEOFFREY HOWE

Christmas Box

FROM: D J L MOORE
DATE: 22 December 1982

2

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State (R)
Minister of State (C)
Sir Douglas Wass
Mr Burns
Mr Middleton
Mr Bailey
Mr Byatt
Mr Kemp
Mr Cassell
Mr Evans
Mr Pestell
Mr G Smith
Mr Robson
Mr Griffiths
Mr Ridley
Mr French
Mr Harris
PS/Inland Revenue
Mr Green)
Mr Battishill) IR
Mr Painter)

* is important
‡ is obviously pressing
19(1) ← may be unfair

I assume that this, & other papers, is being knocked into a memo for Chancellor?

CORPORATE TAXATION: BACKGROUND TO THE BUDGET

... The attached paper does not seek decisions but sets out some of the background on corporate taxation which will be relevant to pre-Budget discussions.

2. It first looks at the position in recent years of the company sector and the main taxes paid by companies. A paper which will be put to you this week by the Industrial Finance Group on company sector prospects is relevant here.

3. It then discusses, in particular, corporation tax (paragraphs 14-24), the National Insurance Surcharge (25-28) and industrial derating (29-33). Although the MISC 79 Ministerial Group is recommending against action in industrial derating, we thought that it would be helpful, in view of the continuing representations from the CBI and others, to include a section summarising the issues and constraints.

4. The main points are summarised in paragraph 39.

DJLM

D J L MOORE

CORPORATE TAXATION: BACKGROUND TO THE BUDGET

This paper sets out some of the background for decisions on corporate taxation in the Budget. It examines the position of the company sector and the tax take and reviews some of the considerations involved in the main tax issues.

A. POSITION OF THE COMPANY SECTOR

2. Real rates of return have been falling since the early 1960s. At that time they averaged 10-12 per cent. The position in recent years is set out in Table 1.

Table 1: Net pre-tax Real Rates of Return(1)

	All industrial and commercial companies	Industrial and commercial companies excluding North Sea	Manufacturing companies
1960	13.2	13.2	13.2
1965	11.2	11.2	10.6
1970	8.7	8.7	7.5
1971	8.9	9.0	7.7
1972	9.3	9.3	8.1
1973	9.0	9.1	8.0
1974	5.9	6.1	4.3
1975	4.6	4.9	3.5
1976	4.8	4.9	3.9
1977	7.8	7.1	6.5
1978	8.2	7.7	6.8
1979	6.9	5.3	4.3
1980	6.2	4.0	3.4
1981	6.2	3.2	2.1
1982 (estimated)	7.0	3.8	n.a.(2)

(1) Gross operating surplus less stock appreciation and capital consumption at replacement cost as a percentage of net capital stock of fixed assets (excluding land) at replacement cost plus value of stock.

(2) Figure not available. Return almost certainly lower than in 1980 but higher than 1981.

Outside the North Sea, despite the minor recovery in 1982, profitability remains at its lowest levels for the past 20 years. It is about two-thirds of the level to which it fell in the last downturn in 1974-75. The position of manufacturing companies continues to be somewhat worse than industrial and commercial companies generally (excluding the North Sea).

3. While real rates of return have declined steadily over the past twenty years, they have in the past always been higher than real interest rates; the gap was greatest in 1974-75 when real interest rates were substantially negative. What makes the current situation different is that real interest rates are presently higher than real rates of return and seem likely to remain so in the near future.

4. As well as declining profitability, companies have faced periodic problems of liquidity. Table 2 shows the gross (ie inclusive of bank borrowing) and net liquidity ratio in recent years.

<u>Table 2: Liquid Assets of all Industrial and Commercial Companies[1] as a Percentage of Total Final Expenditure (fourth quarter)</u>

	Gross Liquidity	Net Liquidity
1978	8.7	-5.1
1979	7.7	-6.0
1980	7.8	-5.9
1981	9.2	-5.7
1982 (estimated)	9.6	-7.6

(1) includes North Sea companies

5. Gross liquidity recovered in 1981 from the rather low levels of 1980 and 1979 to about the levels of the mid 1960s. This recovery was partly the result of borrowing from the banks. There is no ready explanation of the high level of bank borrowing. The net liquidity measure, which excludes bank borrowing, has shown a much smaller improvement. In 1982 net liquidity is expected to be almost as low as the -8 per cent recorded in the 'crisis' year of 1974-75.

6. The extent to which companies have relied on outside sources of funds (notably banks and shareholders) is partly illustrated by their financial deficit. The main components of the position are set out in Table 3.

Table 3: Financial Position of Industrial and Commercial Companies (excluding North Sea) £ billion

	Income(1)	Short-term interest payment	UK taxes on income	Fixed Investment	Stock-building	Deficit (-) Surplus (+)
1979	26.6	4.4	2.8	12.3	2.7	-3.0
1980	26.8	6.5	3.2	13.8	-2.4	-1.5
1981	27.3	6.6	3.6	12.8	-3.4	+0.9
1982 (estimated)	30.2	6.7	4.4	13.1	-0.6	-1.4

(1) Gross trading profits (excluding stock appreciation) plus rent, non-trading income and income from abroad.

While company income has risen in cash terms, in real terms the 1982 figure is below that of 1979. Companies have been squeezed between high wages and interest rates and - at least in the exposed sector - a high exchange rate. In an attempt to protect their profits and financial position companies reduced stocks and employment on an unprecedented scale. In conjunction with a fairly flat level of fixed investment, this eliminated the large deficits of 1979 and 1980 and in 1981 companies recorded a financial surplus of almost £1 bn. They are expected to slip back into a deficit of around £1½ bn in 1982 as the turnround in stockbuilding and slight growth in investment outstrip the increase in savings.

B. TAXES PAID BY COMPANIES

7. The main taxes paid by companies in recent years are set out in Table 4.

Table 4: Tax Paid by Industrial and Commercial Companies (Excluding North Sea) £ billion

	Taxes on(3) companies' income	Employers(1) NIC	NIS(1)	Rates(2)	Total	Total in constant prices (4)
1978	2.8	3.3	1.0	2.3	9.4	9.4
1979	2.8	3.8	1.6	2.5	10.7	9.3
1980	3.2	4.6	1.9	3.2	12.9	9.7
1981	3.6	4.9	2.1	4.0	14.6	10.0
1982 (estimated)	4.4	5.2	1.9	4.7	16.2	10.2

(1) estimates of proportion paid by industrial and commercial companies.
(2) includes North Sea and unincorporated business.
(3) includes mainstream corporation tax, ACT, and tax on company investment income.
(4) deflated by total final expenditure deflator (1978 = 100)

Comparing Table 1 and 4, it is notable that, while ability to pay has been falling, the total of the main taxes for which companies have to account - which includes taxes on costs and taxes on profits - has remained pretty well constant in real terms.

8. Table 4 also shows a shift in the balance between taxes. There have been increases in real and nominal terms in the yield of taxes which are related to business costs - employers' NIC, NIS and rates - rather than to company income. In the case of NIC and NIS, these increases largely reflect increases in wages (apart from the increase in the NIS rate in October 1978). In 1982 NIS payments fell, and they will be lower still next year because of recent decisions. Corporation tax, which is more closely related to taxable capacity, has been relatively stable in nominal terms and in real terms has fallen somewhat.

C. THE OUTLOOK FOR 1983-84

9. The company sector appears likely to show some improvement in 1983 on 1982. Income and profitability will probably improve partly as a result of the reduction in National Insurance Surcharge announced in the Autumn Statement and as companies reap the benefits of gains on efficiency. Short term interest payments are likely to be somewhat lower in real terms in 1983. Savings are likely to grow faster than investment and stockbuilding so that the deficit is likely to fall to something approaching balance. But companies are expected to restrain their real expenditure in the light of a tighter underlying financial position than is usual at this stage of the recovery. The problem of profitability also has worrying longer term implications.

10. In these circumstances general <u>increases</u> in taxes on companies would appear to be unattractive. Payments of local authority rates will be higher in nominal terms but possibly much the same as this year in real terms. In nominal terms, the combined yield of NIS and employers' NIC is expected to rise by about £170 million, or 2 per cent, in 1983-84; in other words the combined effect of cutting NIS and raising NIC is a fall in real terms in total payments. Special considerations apply to banks and these are not covered further in this paper.

11. The options for tax reductions can be viewed as falling into two broad categories:-

(a) across-the-board relief

(b) targeted relief

Across-the-board relief will tend to be favoured if it is felt that there are financial constraints on company performance which are pretty general in the sector. Targeted relief is directed to more specific problems or themes such as the construction industry or small businesses.

D. ACROSS-THE-BOARD RELIEF

12. Companies would, of course, benefit from reductions in personal taxes, as well as reductions in taxes on the corporate sector. NIS, corporation tax and industrial derating are examples of the latter with wide coverage. Table 5 shows the way in which the immediate benefit of a reduction in corporation tax and NIS would be distributed between section of industry and commerce.

Table 5: Immediate distribution of tax reductions by Sector (%)[4]

	Corporation Tax[1]	NIS [2] (a) general reduction	NIS [2] (b) reduction limited to private sector
Manufacturing	27%	28%	43%
Distribution	12%	10%	15%
Financial	12%	7%	11%
North Sea	8%	-	-
Public Corporations	4%	12%	-
Central and Local Government	-	23%	-
Other private sector[3]	37%	20%	31%
	100	100	100

(1) Mainstream tax and ACT

(2) NIS is more widely levied than CT, being paid for example by unincorporated businesses and the whole public sector.

(3) Includes construction, mining, agriculture, transport services and property.

(4) based on yield in 1981-82.

On the assumption that, as previously, the private sector would not be allowed to benefit from any NIS reduction the final column of table 5 shows the distribution of a NIS cut restricted to the private sector; a considerably higher proportion of the money accrues to the manufacturing sector than with a cut in corporation tax.

13. It is not possible to present information on non-domestic rates on the basis as table 5. Table 6 shows such information as is available.

Table 6: Immediate distribution of relief on non-domestic rates (%)

Industrial buildings	20%
Commercial buildings	49%
Utility buildings	10%
Other	21%
	100

The categories "utility" and "other" mainly cover the public sector.

(i) Corporation Tax

14. It is useful to distinguish between structural changes and changes in tax rates.

15. The former is the subject matter of the Green Paper on which the bulk of representations have now been received. The majority of these have opposed any major structural changes. Views expressed on behalf of industry and commerce have stressed the importance to corporate planning of stability and certainty.

16. A number of more specific structural changes have been pressed. Some of these, in particular changes in the treatment of ACT, raise important issues, and a number could be quite costly. Detailed consideration must await Ministers' decisions on the future structure of corporation tax, but the Minister of State (R) is considering with the Inland Revenue whether certain specific matters might be tackled to which industry attached priority.

17. On tax rates, the main rate is 52 per cent, and the rate for companies earning small profits is 40 per cent. Reducing these rates would be of no direct benefit to the 30 per cent of companies that seldom or never pay corporation tax, mainly because of large accumulated tax losses. It would be of some help to the 30 per cent of companies who sometimes pay tax and would clearly help the 40 per cent or so companies that are still paying on a regular basis. For that reason it would

be good for business confidence. The costs of reduction are:

Table 7: Cost of reduction in corporation tax

	1983-84	(£million) Full year		
Reducing 52 per cent rate by 1 point	65	125	x2	= 250
Reducing 40 per cent rate by 1 point	10	15	x5	= 75
				325

18. A cut in the 52 per cent rate would immediately benefit some 30,000 or so medium and large sized companies who pay at that rate, plus perhaps another 20,000 or so whose profits lie above the small profits limit but below £225,000 and who are in the marginal band. Of the major revenue raisers, the corporation tax rate alone remains at the level inherited by the Government in 1979.

19. Reducing the rate of tax would be more attractive than further general increases in relief and allowances, such as stock relief or capital allowances:

(a) A cut in the rate would be broadly neutral as between types of activity and types of company. It would have a marginally helpful effect in reducing the relative attractiveness of debt rather than equity financing, whilst leaving the broad structure of investment incentives unchanged.

(b) In contrast, increases in existing capital allowances would tend to erode the tax base, without necessarily producing additional investment. About two-thirds of all new investment already attracts 100 per cent first year allowances as plan and machinery. Increasing the industrial buildings allowance still further would widen the already sharp disparity with commercial buildings. There might, however, be some scope for action on minor elements in the allowance structure. ?

(c) The revenue effect of a cut in rates would build up over the next two years, with no unwelcome contingent effects on the future tax yield from companies. By sharp contrast, while part of any increase in tax reliefs or allowances would be quickly enjoyed by taxpaying companies, much of it would simply add to the overhang of "tax losses"

(now approaching £40 billion) available to the company sector as a whole (including North Sea companies); this brings no immediate relief to companies, but further prejudices yield of revenue in future years when company profits recover.

20. Turning to small companies, the great majority of companies that pay corporation tax do so at the small companies rate of 40 per cent. This was reduced from 42 per cent in 1980 and now applies to companies with profits below £90,000, with marginal relief on profits up to £225,000. There are two ways of helping small companies:

(a) by reducing the small companies rate below 40 per cent; and/or
(b) by raising the profit levels over which the rate operates.

21. Much the same considerations apply to reductions in the small companies rate as to the 52 per cent paid by the larger companies. The rate could be reduced below 40 per cent, though not perhaps much below 35 per cent, whilst income tax rates remain at their present level, without creating structural problems. A reduction in the small companies rate has the advantage of being simple and, in contrast with many special tax incentives, readily perceived by small businessmen.

22. Too large a gap between the main rate and the small companies rate would invite charges of unfairness towards the largest companies, particularly in current conditions. Moreover, there is a technical problem. The wider the gap between the two rates, the more difficult it is to make the transition between the small companies rate and the full 52 per cent rate, and to have a satisfactory marginal band. At present, the benefit of the lower 40 per cent rate is withdrawn between profits of £90,000 and £225,000 by charging tax at 60 per cent. Reducing the small companies rate to 35 per cent (without a corresponding reduction in the 52 per cent rate) would increase the marginal rate to over 63 per cent; or, to keep the marginal rate unchanged, the profits limit would need to go up from £225,000 to over £280,000. This would cost another £90 million.

23. Aside from changes in the rate, there is a good case for keeping the profits limits for the small companies rate broadly revalorised from year to year. Depending on the extent to which allowances are revalorised generally, the limits might be increased by somewhat more than the rate of inflation - perhaps, in

round figures, from £90,000 to £100,000 and from £225,000 to £250,000. The marginal rate would stay at 60 per cent. This is probably as far as it is reasonable to go. There was a sizeable real increase in the upper limit in 1981. Such increases can do nothing to help the smallest companies, and would now benefit companies which by most standards are pretty large. A company with taxable profits at even the present upper limit of £225,000 could have assets worth many millions in its balance sheet.

24. Action on corporation tax would work through with some delay, as the tax is not generally paid until 9 months after the end of the company's accounting period. While table 5 shows the immediate pattern of direct beneficiaries, there are considerable uncertainties about the longer term incidence of a reduction in corporation tax.

(ii) National Insurance Surcharge

25. A further reduction in the NIS rate announced in the Budget would not take effect before the beginning of August. It would be possible to repeat the 1982 Budget procedure so that there was an additional, temporary, reduction between August 1983 and March 1984 to give employers the full year benefit of the proposed cut. But this would have the disadvantage of building up a presumption of consolidation from April 1984 of the temporary cut and would add to the 1983-84 costs. Assuming full offset of benefits to the public sector, the costs of a ½ per cent reduction and of abolition of the 1½ per cent rates would be:

Table 8: Cost of reductions in NIS (£ million)

	1983-84	full year
½ per cent from August 1983	200	400
½ per cent for the whole of 1983-84	350	400
Abolition from August 1983	650	1200

26. A reduction in the NIS rate, or complete abolition of the tax, have been canvassed as a leading candidate by the CBI, the Engineering Employers Association, the Association of British Chamber of Commerce and the National Federation of the Self-Employed. By contrast, the Institute of Directors do not put further action

on NIS at the top of their priorities. A reduction in NIS would directly reduce employers' labour costs and so encourage employment. In the short run it will improve UK industry's competitiveness. There is a danger that the benefit would leak into wages but the present best economic assessment is that nominal wages are likely to be little affected, partly as a result of a NIS cut leading to lower prices.

27. Since the NIS is paid by all employers the reduction in costs would not be limited to the corporate sector, or within that to the minority of companies paying corporation tax. Manufacturing industry accounts for over 40 per cent of total NIS payments by the private sector. With corporation tax under 30 per cent of the benefit of a cut would go to manufacturing. With both taxes a significant part of any reduction would go to service industries, including e.g. banking and insurance which have been less exposed to international competition. (See table 5)

28. With both corporation tax and NIS, the benefits of a tax reduction depend crucially on the accompanying monetary stance. If interest rates had to be increased to counteract the effects on monetary growth, gains to competitiveness would probably be lost quite quickly through the associated appreciation in the exchange rate. As far as companies are concerned, an increase in interest rates would quite quickly cancel out, and probably more than cancel out, the financial benefit of the tax reductions. On the other hand, if monetary policy were accommodating, the tax reduction would improve company cash flow and competitiveness, but the risks of higher future inflation would be greater.

(iii) Industrial derating

29. The CBI and others argued for a measure of industrial derating before this year's Budget, and are likely to repeat their request. Total non-domestic rates are estimated at about £7,000 million in 1982-83, of which rates on industrial property account for £1,400 million. It would be possible to confine derating to the latter in order to keep down costs and target the relief at manufacturing industry. On that basis, each 10 per cent derating would result in a loss of rate income of about £140 million. This would have to be made good either by an increase in rates falling on other ratepayers or by additional Exchequer support through the Rate Support Grant.

30. Derating would particularly benefit companies which use land and building-intensive methods of production or which are located in areas of high rate poundages. The reduction in rates would reduce production costs, and so like NIS could lead to reduced prices and greater competitiveness. In the longer-run, it would give an incentive to firms to use more land and buildings. The benefits to companies would also depend on how the reduction in local authorities rate revenue was made up and whether this involved additional taxation.

31. This measure has more geographical variation in its effects than reductions in NIS and corporation tax, partly as a result of the wide variations in poundages between local authorities. As there has not been a non-domestic revaluation since 1973 in England and Wales some of the relativities in rateable value between classes of property could also be out of line and this would affect the distribution of the benefit.

32. MISC 79 has decided to recommend against industrial derating as part of the package of rate reforms for announcement later in the session and no legislation on rates is envisaged in this Parliament. If Ministers wished to reopen this decision, the Secretary of State for the Environment and the Business Managers would need to be consulted urgently about the feasibility of introducing the necessary legislation in 1982-83. (Parliamentary Counsel has confirmed that industrial derating is outside the scope of the Finance Bill.) It would be necessary to review and bring up to date the definition of industrial property in the pre-1963 legislation and the Inland Revenue Valuation Office would require 6 months and the equivalent of about 100 staff to identify the qualifying properties.

33. Even if it were wished to take action in 1983-84 it seems unlikely, therefore, that any relief could be implemented before the second instalment of 1983-84 rates is due to be paid at the beginning of October. This would require a system of refunds to be set up. Central Government financing would be inevitable in 1983-84. But in subsequent years the relief could be taken into account at the time of the RSG discussions and before local authorities' rating decisions and one option then would be to let the cost of industrial derating fall on other ratepayers.

E. TARGETED ACTION

34. There are a number of areas for which more closely targeted tax reductions in 1982 might be considered appropriate. One area that springs to mind are the companies most exposed to foreign competition. Unfortunately, there are no tax reliefs which would hit this target.

35. A second area would be entrepreneurial activity and enterprise. A number of relevant measures are currently under discussion. Some of the measures fall outside the immediate area of corporate taxation. The Chancellor has asked the Financial Secretary to oversee further work in this area.

36. Third, long term corporate borrowing. The Grylls Group have proposed that corporate investment would be significantly increased by an arrangement under which companies paid interest net of tax on loans of more than five years. A possible scheme is being worked up which would provide subsidised interest rates for long term borrowing by small companies. The Financial Secretary is overseeing work on the taxation of zero and deep discount stock - including the possibility of moving to an accruals basis for taxation.

37. Fourth, help for particular industries. The construction industry is a perennial case for special treatment. The Secretary of State for Trade has proposed special help to tourism. The Chancellor has asked the Chief Secretary and the Economic Secretary to oversee work on these areas.

38. On the motor car industry, a separate paper has been prepared. Abolition of car tax would cost £650 million in a full year. A major concession here would eat a good way into any fiscal adjustment.

SUMMARY

39. The main points in this paper are:-

1. The corporate sector has a chronic problem of declining profitability. Outside the North Sea profitability is at its lowest level in the past 20 years.

2. A liquidity crisis has been averted in the past two years mainly by massive destocking and labour shedding. This adjustment may well have left companies in a healthier position for the future.

3. The yield of the main taxes paid by companies (excluding the North Sea) has about remained constant in real terms. Within this there has been an increase in the taxes on business costs and a fall in receipts of corporation tax.

4. Looking to 1983, preliminary indications are of some recovery in income and profitability but the companies are not likely to move back into f[illegible]cial surplus.

5. Increases in taxes on companies in 1982 do not seem attractive at this stage.

6. Any reduction in taxes falling directly on companies could be made across-the-board or in more closely targeted areas. Reductions in taxes on persons would also be of benefit to companies.

7. Following MISC 79's recommendation, industrial derating is not on the stocks for 1983-84. If that decision were reopened room would have to be found for a special Bill in the present Session. A reduction could be targeted on manufacturing industry alone.

8. Reductions in corporation tax would benefit the 40 per cent of companies regularly paying tax and, although relatively slow acting, would help confidence.

9. Reductions in NIS would be quick working and be spread more widely. It would give more benefit to manufacturing industry than a reduction in corporation tax.

10. The effect of a reduction in either NIS or corporation tax depends critically on the accompanying monetary stance. With derating much would depend on the way the reduction in local authorities revenue is financed.

11. On targeted action, work is in hand on various measures.

CONFIDENTIAL

FROM: JILL RUTTER
DATE: 29 December 1982

MR D J L MOORE

cc: Chief Secretary
Financial Secretary
Economic Secretary
Minister of State (R)
Minister of State (C)
Sir Douglas Wass
Mr Burns
Mr Middleton
Mr Bailey
Mr Byatt
Mr Kemp
Mr Cassell
Mr Evans
Mr Pestell
Mr G Smith
Mr Robson
Mr Griffiths
Mr Ridley
Mr French
Mr Harris
PS/IR
Mr Green)
Mr Battishill) IR
Mr Painter)

CORPORATE TAXATION: BACKGROUND TO THE BUDGET

The Chancellor is most grateful for the paper attached to your minute of 22 December. He hopes that this with other papers, is being incorporated into the "menu" for Chevening.

The Chancellor has commented on the paper that the point on ability to pay at the end of paragraph 7 is important. The MST(R)s review alluded to in paragraph 16 is clearly pressing. The Chancellor thought that the suggestion canvassed in paragraph 19b of scope for action on minor elements in the allowance structure might prove useful.

JLR

JILL RUTTER
29 December 1982

B 1983

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

CH/EXCHEQUER
REC. 29 DEC 1982
ACTION FST

ECONOMIC SECRETARY
REC'D 31 DEC 1982
ACTION Mr Griffiths
COPIES TO PPS, CST, FST, MST(R)
Mr DJL Moore
Mr Kemp, Mr Lovell
Mr FK Jones
ASJ/C&E

FST to deal

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
LONDON SW1P 3AG

Dear Geoffrey

LORRY TAXATION 1983

I expect that you will be thinking soon about the part which the motoring taxes might play in your revenue raising plans for next year. I thought it would be helpful if I were to suggest a possible framework which I think could serve both our interests. I should say that I am limiting myself in this letter to the taxation of heavy lorries.

The key issue from my viewpoint is that we must be seen next year to have taken positive steps to get closer to achieving full road cost coverage on the present top weight lorries. The proposed new heavy lorries are, as you know, to start off in a position of full cost coverage; this is an important 'selling' point in my package of Armitage proposals. We have the advantage of the new structure of lorry taxation which we implemented this year. This will enable us to be highly selective in the way in which we tackle the new lorries and the present undertaxed groups.

The part which VED will play in meeting my track cost objectives depends crucially on your treatment of DERV duty. I envisage that your starting point will be revalorisation and I would strongly support this. Indeed, from my

viewpoint anything less would be very awkward, since it would mean loading even more onto VED levels to achieve the level of cost coverage I am advocating. That would mean very high increases in VED: about 35% on the 32.5 tonnes lorry. It would also seem perverse to put more emphasis on a tax which, by its nature, takes no account of the wide variations in mileages run by vehicles.

However, DERV revalorisation alone would not tackle the deficit on the undertaxed lorries. The present top weight lorries are currently about 16% short of full cost coverage on average. I would hope we can halve this deficit next year. Based on the present best estimates of road cost allocations, halving the deficit would require an increase of about 26% on the present VED rate of the 32.5 tonnes lorry. This would represent a real increase of about 21%, assuming an inflation rate of 5%. On the one other undertaxed group, the 30 tonne rigid lorry, the increase needed would be about 11%.

The total VED from heavy lorries originally expected from the rates set in the 1982 Budget was some £360m. To maintain this position in real terms would involve aiming for a total of about £378m, assuming an inflation rate of 5%. However, the increase that I have indicated above for the undertaxed lorries, together with retaining VED rates on the lightest less damaging lorries at the present level (a decrease of 5% in real terms) would yield a total of some £395m in VED ie an additional £17m. This £17m would enable the VED rates of the lighter lorries to be reduced by some 10-15% whilst still leaving these lorries paying more than their road costs. VED reductions of this order would still result in a package which would be broadly revenue neutral in real terms and you may think it would be wise to aim for this in order to avoid any overall

increase in the VED burden on industry. The reductions on the lighter lorries would help to offset criticism of the 26% increase on the 32.5 tonner, and show that we are switching the tax burden from less damaging to more damaging lorries.

I suggest our officials might consider these options further. If you see any particular problems it would be helpful if you could let me know.

Yours ever

David

DAVID HOWELL

B 1983

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

CH/EXCHEQUER
REC. 29 DEC 1982
ACTION FST

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
LONDON SW1P 3AG

ECONOMIC SECRETARY
REC'D 31 DEC 1982
Mr Griffiths
COPIES TO PPS CST FST MST(R)
Mr D J L Moore
Mr Kemp Mr Lovell
Mr F K Jones
FS/CE

FST to deal

Dear Geoffrey

LORRY TAXATION 1983

I expect that you will be thinking soon about the part which the motoring taxes might play in your revenue raising plans for next year. I thought it would be helpful if I were to suggest a possible framework which I think could serve both our interests. I should say that I am limiting myself in this letter to the taxation of heavy lorries.

The key issue from my viewpoint is that we must be seen next year to have taken positive steps to get closer to achieving full road cost coverage on the present top weight lorries. The proposed new heavy lorries are, as you know, to start off in a position of full cost coverage; this is an important 'selling' point in my package of Armitage proposals. We have the advantage of the new structure of lorry taxation which we implemented this year. This will enable us to be highly selective in the way in which we tackle the new lorries and the present undertaxed groups.

The part which VED will play in meeting my track cost objectives depends crucially on your treatment of DERV duty. I envisage that your starting point will be revalorisation and I would strongly support this. Indeed, from my

viewpoint anything less would be very awkward, since it would mean loading even more onto VED levels to achieve the level of cost coverage I am advocating. That would mean very high increases in VED: about 35% on the 32.5 tonnes lorry. It would also seem perverse to put more emphasis on a tax which, by its nature, takes no account of the wide variations in mileages run by vehicles.

However, DERV revalorisation alone would not tackle the deficit on the undertaxed lorries. The present top weight lorries are currently about 16% short of full cost coverage on average. I would hope we can halve this deficit next year. Based on the present best estimates of road cost allocations, halving the deficit would require an increase of about 26% on the present VED rate of the 32.5 tonnes lorry. This would represent a real increase of about 21%, assuming an inflation rate of 5%. On the one other undertaxed group, the 30 tonne rigid lorry, the increase needed would be about 11%.

The total VED from heavy lorries originally expected from the rates set in the 1982 Budget was some £360m. To maintain this position in real terms would involve aiming for a total of about £378m, assuming an inflation rate of 5%. However, the increase that I have indicated above for the undertaxed lorries, together with retaining VED rates on the lightest less damaging lorries at the present level (a decrease of 5% in real terms) would yield a total of some £395m in VED ie an additional £17m. This £17m would enable the VED rates of the lighter lorries to be reduced by some 10-15% whilst still leaving these lorries paying more than their road costs. VED reductions of this order would still result in a package which would be broadly revenue neutral in real terms and you may think it would be wise to aim for this in order to avoid any overall

increase in the VED burden on industry. The reductions on the lighter lorries would help to offset criticism of the 26% increase on the 32.5 tonner, and show that we are switching the tax burden from less damaging to more damaging lorries.

I suggest our officials might consider these options further. If you see any particular problems it would be helpful if you could let me know.

Yours ever

David

DAVID HOWELL

SECRETARY OF STATE FOR THE ENVIRONMENT

EXCHEQUER
- 5 JAN 1983
ACTION MR KEMP
COPIES TO CST, FST, EST, MST(C), MST(R), Sir D Wass, Mr Burns, Sir A Rawlinson, Mr Byatt, Mr Bailey, Mr Wilding, Mr Moore, Mr Pestell, Mr Lovell, Miss Kelley, Mr Battishill, PS / C+E, PS/IR, Mr Ridley, Mr French, IR

2 MARSHAM STREET
LONDON SW1P 3EB

My ref: H/PSO/18722/82

Your ref:

- 6 JAN 83

Dear Chancellor of the Exchequer

BUDGET 1983

I am writing to you with a number of suggestions which I and my colleagues here would like to see considered for the budget next year. They are arranged by topic.

HOUSING

In this field I would like to see, as you know, the extension of capital allowances to shared ownership. This form of tenure is at present wholly confined to the public sector. If this is to become a more widely used method of assisting people into home ownership then we must find a source of private sector funding for the rented element. The best way of stimulating this would be to extend capital allowances to the rented element of shared ownership, on the lines of the provision made for assured tenancies in this year's Finance Act. There is already outstanding correspondence on this between us on the subject and I am hopeful that you will feel able to respond in a positive way.

As you are also aware the 1980 Finance Act gave only partial relief to resident landlords. The tax is still payable on gains on the let part of homes if in excess of £10,000 or on the gain of the unlet part. Also resident landlords with a self-contained part of their home let do not qualify. We regard such lettings as providing a most important form of flexibility in the housing market and leading to a fuller use of housing stock. Providing this relief will give a valuable incentive to increasing the availability of such lettings.

Landlords are of course taxed on rental income either through income tax at the marginal rate or through corporation tax depending on their status. They are able to offset against the tax on rental income, repair and maintenance expenditure as well as interest and loans for improvement. A greater incentive could be given by enabling repair costs to be offset against <u>all</u> income, not just that from rents. This would be of particular help to landlords faced with major repairs, and could be achieved at very little financial or administrative cost.

40/1

Lastly, on the housing side I would like to see repairs grants extended to dwellings built before 1945. I have already written to the Chief Secretary on this subject. You will recall that in the Housing Act 1980 we extended eligibility for repairs grants to substantial and structural repairs to "old dwellings" - this means at present before 1919. The English House Conditions Survey results however show that there are over a million dwellings built between 1919 and 1945 needing at least one essential repair. This trend is a matter of concern. I believe we must act now therefore before the problem gets any worse.

COMMERCIAL AND INDUSTRIAL BUILDINGS

I would very much like to see the introduction of a system of capital allowances for the refurbishment of industrial and commercial buildings. This would be modelled on the current successful industrial allowances for commercial and industrial premises in Enterprise Zones, but would apply to the major refurbishment of existing industrial and commercial property.

Such a scheme would have a number of advantages. It would provide work for the hard-pressed construction industry; re-furbishment is labour intensive; and in common with most construction has a low import content. It would be of particular benefit to our inner cities, when there are substantial amounts of vacant old commercial and industrial premises which nonetheless represents a sizeable existing resource and contributes significantly to the townscape. The scheme would encourage modernisation and enhanced efficiency of this stock. It would also give a positive response to the representations of the Joint Taxation Committee, on an issue to which they attach some priority, at a time when I am not supporting many of their other major proposals, such as mortgage relief and stamp duty.

Our estimates for the costs of such a scheme are very tentative, in a range of £125-500 millions depending on scope and the rate of allowance. The immediate costs could be reduced by adopting a writing - down approach, though that of course builds up the level in later years.

The proportion of office space in an industrial building which qualifies for an Industrial Building Allowance should be increased from 10% to 25%. The 10% level represents the traditional proportion for manufacturing industry, but is now out-of-date. The usual proportion now in own-user building is in the range of 20-50%, reflecting a growing need for industrialists to require accommodation which integrates head office operations with the factory. High technology firms particularly tend to want to combine various parts of their operation (R & D, production, services, offices) under one roof. However, almost all speculative development is now rather artificially built within the 10% limit, which causes unnecessary inconvenience and delay for more sophisticated clients. An increase to 25% would make a significant contribution to removing this distortion at a limited cost (which

we estimate at £50m pa) and would encourage speculative developers to be much more responsive to market needs. It would thereby tend to help the more rapidly growing sectors of industry by enabling them to find more suitable ready made accommodation. The JTC will be proposing this in their Budget representations.

HERITAGE EXPENDITURE

My first suggestion here would be to give exemption from VAT in respect of works of art accepted in lieu of tax. It is the Custom and Excise's present view that the Government's acceptance in lieu of tax of a work of art which has been on public display represents a taxable supply and that the transaction is therefore subject to VAT. This seems something of an anomaly and particularly when the object is to remain in situ after its acceptance, and at odds with Government policy. The relevant Finance Act provisions (para 17, Schedule 4 Finance Act 1975) could be amended to make the acceptance of property in lieu of tax exempt from VAT. The tax loss, we think, would be negligible - well under £1m.

Secondly I suggest that there should be tax concessions for gifts to Preservation trusts or other environmental trusts. This is a simple concept but would require acceptance of the policy that contributions made towards non-business orientated objectives are justified by the importance of the objectives. It would extend the sort of principle embodied in Section 48 of the Finance Act 1982.

THE BUSINESS START-UP SCHEME

I wrote to you on 6 April with a number of suggestions made by the Financial Institutions Group (FIG) for changes to the business start-up scheme. I think this scheme is an important one which could have significant benefits for the local economies of inner cities and other areas, and I am concerned that it does not seem to have been going as well as had been hoped when it was introduced. It seems sensible to consider now whether there are any changes which could usefully be made to stimulate the scheme, and you might like to reconsider some of the FIG suggestions in that context. I do not discount the arguments you put forward against them in your letter of 30 April; and nor do I think that these may be the only possible improvements. You or John McGregor may well have others. I refer particularly to FIG's suggestions that:

(i) it might be possible to develop a scheme for more immediate relief whereby the investor would pay to the company capital net of a notional rate of tax, subsequently adjusted.

(ii) potential investors may be discouraged by the anti-avoidance penalties on disposals of shares within 5 years, and a tapering of withdrawal of relief in these circumstances should be explored.

(iii) further increases in the level of relief available in any one tax year should be considered.

(iv) further provisions for "roll-over" of relief should be made.

TAX RELIEF FOR ENTERPRISE AGENCIES

The tax relief on contributions to approved enterprise agencies given under S48 of the 1982 Finance Act has been very welcome. The permissible objectives of enterprise agencies entitled to this relief were, however, drawn quite tightly to limit relief to agencies (or separate funds of agencies) promoting or encouraging industrial and commercial activity. I understand that your officials were concerned that the provisions should not breach the principle that relief ought only to be available for contributions that were for business purposes (in the broadest sense).

I would like you to reconsider whether there is scope for widening the permissible objectives to include the undertaking of environmental works, the managing of community projects, etc (the precise functions, if there is need for precision, can be discussed after the principle is settled). I feel strongly that local environmental and community activities of this sort are beneficial to the businesses of the companies who contribute towards them, perhaps just as much as the counselling of small businesses that is the standard fare of enterprise agencies.

TAX RELIEFS FOR CHARITIES

Again, the recent fiscal concessions given to charities have been welcome. However, Ed Berman, my Special Advisor on inner cities (with special reference to the voluntary sector), has put forward one suggestion in particular that has been considered before, notably in the Inter-Ministerial Group on the Voluntary Sector, but which we still find attractive.

It concerns relief for companies seconding staff to charities. Secondments of this sort are a very worthwhile activity and ought to be given official encouragement, as we have recognised for secondments to enterprise agencies. I believe that the cost of secondments to charities is not normally considered to be expenditure by businesses "wholly and exclusively" for the purpose of their trade, and is therefore normally paid for out of taxed income. On a similar argument to that used above for enterprise agencies, I would suggest that this be reconsidered. The ways forward would seem to be a re-interpretation by you of what is considered to be expenditure for the purpose of trade (which could possibly cover enterprise agencies as well, thus rendering part at least of the specific relief to them unnecessary); or alternatively a specific legislative item for charities (or perhaps "approved" charities) paralleling in part the concession given last year to enterprise agencies - which would of

course involve a similar shift in principle to that proposed above in the case of enterprise agencies with wider objectives.

A broader issue, which raises the same issues of principle and was considered in the same forum, is to make any donation up to, say 5% of a company's previous year's pre-tax profits as shown in their accounts, tax deductible. This would have considerable benefit in encouraging private sector firms to exercise the sort of corporate responsibility policies that are common-place in America.

Another, rather smaller, issue raised is the possibility of abolishing the limit (at present £250,000) on the exemption from Capital Transfer Tax of gifts to charity made on death or within a year before death. There does seem to be very little justification for this limit, and its abolition would not appear to have much revenue consequence, nor to breach any taxation principles.

My final suggestion concerns the charitable status of Sport and Recreation. The broad base of this increasingly important part of our social fabric lies with the voluntary sports clubs and agencies who have long pressed for charitable status and the fiscal relief this brings. At present the promotion of sport in itself is not deemed to be charitable except where there is an educational element eg the Football Association Youth Trust gained charitable status since its activities form part of an educational curriculum.

The 1976 Report of the Goodman Committee on Charity Law and Voluntary Organisations took the view that a non-profit distributing body having the purpose of developing and controlling a sport or recreational activity for public benefit should enjoy tax exemption. It was also of the opinion that the encouragement of sport and recreation should be recognised as an independent charitable objective provided the necessary elements of altruism and benefits to a sufficient section of the community were present. There would of course be difficulties in definition (eg the exclusion of professional sports), but such a change in the law would be welcomed throughout the world of sport.

I am copying this letter to John MacGregor in DOI. No doubt you will come back to me if you need further information from me or my Department about any of these suggestions.

Yours sincerely

MICHAEL HESELTINE
(Letter approved by the Secretary of State and signed in his absence).

CONFIDENTIAL

Start on summaries i a letter to King?

CHANCELLOR

BUDGET PROPOSALS FROM DOE

You asked what proposals had been put forward by DoE Ministers and where we now stood on them:

Mr Heseltine of 6 January 1983

(i) extension of capital allowances to shared ownership

Discussed in FPG ~~yesterday~~ on Monday. You promised colleagues a note.

(ii) full relief to resident landlords

IR advised would further complicate the law & lead to other demands for parity of treatment.

(iii) repair costs to be set against all income (not just rents)

IR recommended against

(iv) repairs grants extended to dwellings built before 1945

Improvement grants extended to like war period in context of construction package

(v) capital allowances for refurbishment of industrial and commercial buildings

IR advised should be considered in context of commercial buildings allowance generally — for a Green Paper rather than Budget

(vi) increase in disregard for industrial building allowance to 25%

Agreed in context of construction package.

(vii) exemption from VAT on works of art accepted in lieu of tax

Mr Knox will be submitting further advice.

(viii) tax concessions for gifts to preservation and other environmental trusts

Rejected

[illegible]

[illegible]

(ix) Business Start Up Scheme

Business Expansion Scheme agreed at today's meeting in enterprise package

(x) Widening permissible objectives of enterprise agencies

Rejected

(xi) Tax relief for companies seconding staff to charities

Agreed in context of caring package

(xii) Donations of up to 5% of company's previous year's pre-tax profits to be tax deductible

Tax deductibility for one-off donations generally has been rejected.

(xiii) Abolition of exemption limit for CTT of gifts to charity made on death

Agreed as part of caring package.

(xiv) tax relief for voluntary sports clubs & agencies based on giving them charitable status

Change in status would have to provide tax relief

Lord Bellwin's letter of 18 January

(i) income tax and corporation tax allowances for repairs to listed buildings

Rejected

(ii) tax relief for contributions to preservation & environmental trusts

Rejected

Mr King's letter of 11 February

Capital allowances for new commercial buildings in inner cities

Not for Budget but to be considered in Regional Policy context.

[illegible]

16/2

DEPARTMENT OF [illegible]
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

= PS/C+E
PS/ EST MST(C)
CST MST(R)
Sir D Wass
Mr Middleton
Mr Moore
Mr Mc[illegible]
Mr Griffiths
Mr Martin (Mr French)
Mr [illegible]

JF2501
Secretary of State for Industry

January 1983

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
LONDON SW1

31 JAN 1983

AST. 31/1.

Dear Geoffrey,

[illegible] OF [illegible] RATING [illegible] SHOWERS

I enclose a letter sent to me by the Association of Manufacturers of Domestic Electrical Appliances covering a detailed case they have made for maintaining zero-rating for VAT when an instantaneous shower is supplied and installed in a room for the first time.

2 I understand that, subject to the outcome of a current appeal, such work would become subject to VAT at the standard rate following the implementation of a House of Lords' judgement given last year. Geoffrey Howe recognised that full implementation of the judgement would have imposed an extra tax burden of £[illegible]m on industry and he announced in his Budget statement last year his intention of relieving £[illegible]m of the extra tax burden by means of an Order to continue zero-rating for some of the most commonly recognised forms of building alterations, other than instantaneous showers.

3 There seems to me to be a good case for according the showers equivalent treatment, should that in fact prove to be necessary when the current litigation is concluded. In terms of size, although the instantaneous shower market is much smaller than that for double glazing, it is bigger than those for cavity wall insulation, loft insulation, or damp-proof coursing for which the maintenance of zero-rating has been agreed. If energy conservation considerations should have been a factor in that decision, then these apply to instantaneous showers at least as strongly as to (say) double-glazing. Zero-rating for the showers could also presumably be given without jeopardising clarity in the law to any greater extent than zero-rating of the other industries for which it has been agreed.

/4 Finally ..

4 Finally, the domestic electrical appliance industry, which has shed 30% of its workforce in 3 years, has been having quite a tough time recently. It would be anomalous if instantaneous showers, which at present is one of the more encouraging sub-sectors, were now to be depressed by a tax change which is not being specifically sought in order to raise revenue but is simply one almost unintended outcome of a desirable clarification of the law in an important but difficult area.

5 I should therefore be glad if you could consider the AMDEA request sympathetically.

Yours ever
Peter

The [illegible] of Manufacturers of Domestic [illegible]

AMDEA

From the Director General
J. P. Collis

Leicester House
8 Leicester Street
London WC2H 7BN

tel: 01-437 0678
telex 263536

Rt Hon Patrick Jenkin MP
Secretary of State for Industry
Department of Industry
Ashdown House
123 Victoria Street
London SW 1

24th January 1983

Mr Pulston [illegible] TO
15/1/83
15/JB
15/SC
Mr Pooth
Mr Dell
Mr Wright
[illegible] CHARGE,
PLEASE BY:
25/1/83

Dear Mr Jenkin

[illegible] ON [illegible] SHOWERS

We [illegible] writing to you as the [illegible] Minister for our industry [illegible] you [illegible] forward the enclosed proposal to the Treasury on our behalf.

We have [illegible] the matter with your officials and also, in order to keep [illegible] informed, with officials from Customs and Excise. We should [illegible] stress that we are not seeking to deprive the Revenue of any [illegible] which they are currently obtaining. We are seeking [illegible] of a [illegible] policy which has been [illegible], as the Chancellor has recognised, by legal [illegible].

The Chancellor has stated that he wishes to relieve the [illegible] industry of most the tax which the House of Lords judgement would otherwise impose on industry, and Customs and Excise have stated that there is no primary intention to raise revenue as a result of the judgement. We ask therefore that a specific reference be made to instantaneous showers by a Treasury Order to prevent a serious setback to an industry that is solely catered for by UK manufacturers.

Yours sincerely

J P Collis

J P Collis
Director General

INSTANTANEOUS SHOWER PROPOSAL

1. PROPOSAL

That the supply and installation of an instantaneous shower in a room for the first time be zero-rated by a Treasury Order as has been passed in the case of double glazing and committed in respect of loft and cavity wall insulation and damp-proof coursing.

This could be achieved by amending item 2 of group 8, schedule 4 FA 1972 to insert as follows:

Item 2 (c) (The supply) "in the course of the installation of an instantaneous shower for the first time in a particular location in,"

2. SUMMARY OF CURRENT SITUATION

The supply of an instantaneous shower installed in a room for the first time has, ever since the introduction of VAT, been treated as a zero-rated supply. The decision of the House of Lords in the matter of Customs and Excise v. ACT Construction Ltd has now cast doubt upon the interpretation of [illegible] for [illegible] works and buildings. The Chancellor of the Exchequer recognised the problem caused by the House of Lords decision in his Budget Speech of 9th March 1982 (see Appendix IV).

The change in interpretation has been held up pending the hearing by the Court of Appeal by the VIVA Gas Appliances Ltd case. The Commissioners of Customs and Excise lost this case in the High Court in a judgement which challenged several of the assumptions made following the ACT case. If the Commissioners eventually win the VIVA Gas case it is probable that in future the supply and installation of an instantaneous shower in a room for the first time will have to be treated as standard rated. We are therefore asking for a Treasury Order to zero-rate such supplies as has been done in the case of double glazing and promised with regard to cavity wall and loft insulation and damp-proof courses.

3. REASONS FOR PROPOSAL

(i) As about 85% of all installations have previously been zero-rated, a change will be a major disruption to the industry. Previous experience suggests such a change would cause the market to decline significantly. It is now generally recognised that the frequent changes in purchase tax levels experienced under previous administrations were a major cause in the weakening of the domestic electrical appliance industry which led to growth of imports.

(ii) The market has a value of £95 million (installed value) encompassing an estimated 431,000 units (see Appendix I). The market is met solely by UK manufacturers. Around 1100 people work directly on the manufacture of showers, a number increased by a further 2-3000 working for component suppliers. Further, some 2000 workers are employed in installation work, plus an equal number in external sales, marketing and distribution. Not only is the UK market dominated by UK manufacturers but, due to the steady

growth of the market, these manufacturers have also been able to exploit overseas markets. It is estimated that exports in the year 1982 were worth around £3 million (see Appendix II).

(iii) The installations named by the Chancellor for specific zero-rating all relate to energy saving. The installation of instantaneous showers should also be encouraged on the grounds of energy and water conservation. It is estimated that energy savings of £5.2 million per annum will be at risk if standard rating proceeds (see Appendix III). Installation of showers is certainly as effective in energy saving terms as the other items listed.

(iv) The addition of instantaneous showers to the Treasury Order would not cause a loss of revenue to the government. The Chancellor indicated that he wishes to relieve most of the tax which the House of Lords judgement would have imposed on the industry. The additional tax revenue produced by showers, based on the current market size, would realise £11.35 million (see Appendix I) which is more than would be produced by cavity wall insulation, loft insulation or draughtproofing individually (see Appendix IV).

4. [illegible]

This proposal is submitted by AMDEA (The Association of Manufacturers of Domestic Electrical Appliances) on behalf of the companies concerned in the manufacture of electric showers (see Appendix II).

J P Collis
Director General

14th January 1983

Appendix I

The figures in this appendix relate to Electrical Instantaneous Showers only. It is estimated that this accounts for 95% of the total market, the other 5% being gas installations.

1. a) Market Size

Units (12 months to 30.6.82) = 431,000.

Installer	Market Share (Units) %	Installed value £000
Builder/plumber	33	28,446
Shower Manufacturer	14	26,550
Electricity Board	17	15,533
D I Y	19	9,827
Others	17	14,654
	100	95,000

The installed value per unit is highest at £140 for shower manufacturers, [illegible] of the high price units, and lowest for D I Y at £[illegible] per unit. The other installers' prices are c. £[illegible] per unit.

b) VAT yield if Standard Rating proceeds: £'000

Total Market		95,000
Less D I Y (current standard rated)	9,827	
Less still zero-rated (new or reconditioned houses)	9,500	
Total		19,327
Value becoming subject to Standard Rating		75,673
VAT thereon @ 15%		11,350

c) Market assumptions for 1983:

If zero-rating continues + 10% = 474,000 units

If standard-rating enforced - 10% = 388,000 units

Source for above figures: AMDEA, Electricity Council, AGB Research

[illegible] III

ENERGY USAGE

Based upon A G B Research figures and manufacturers' returns to AMDEA, 431,000 instantaneous shower units were installed during the year ended 30th June 1982.

The imposition of standard rating is estimated to reduce installations by 10-15% per annum.

It is assumed that shower buyers will use the shower instead of a bath once per day.

Based on an estimated loss of shower installations of 10% per annum, resulting from standard rating, 43,000 baths would be taken daily instead of showers (see below).

In KW terms, this extra demand would be:

43,000 x 2376 KW = 102 million KW

The annual cost of the extra demand measured in terms of the average of Area Electricity Boards' selling price of 5.1p per KW is £5.2 million.

No growth in the market has been assumed in these calculations although 10% per annum growth is projected by the industry if current [illegible] rating were to continue.

Appendix IV

i) Extract from Chancellor's Budget Speech - 9th March 1982

"I also propose to deal with the liability to VAT of certain kinds of building alterations, where there has in the past been serious doubt about what was liable to charge. A recent judgement of the House of Lords would have led, if applied in its entirety, to VAT being charged at the standard rate on a range of non-structural building alterations which had previously been free of charge. Though clarifying the law, this judgement would have imposed an extra £80 million of tax on the industry, which it can ill afford at present.

So I intend to re-establish the clarity needed, but in a way which will relieve the industry of all but £10 million of the extra tax burden. I shall, in due course, lay before the House an Order, which will have the effect of continuing to zero-rate three important kinds of alterations which might otherwsie be adversely affected by the House of Lord's judgement.

These are the most commonly recognised forms of double glazing, loft and cavity wall insulation and damp-proof coursing. This useful simplification of the law will cost the revenue about £70 million a year.

The other kinds of non-structural alteration covered by the judgement will become subject to VAT but, pending the completion of discussions with the industry, no steps will be taken to apply the tax before about the beginning of September."

Note: Full changes held up by Court of Appeal hearing relating to VITA Gas.

ii) Estimates of items covered by Chancellor's Speech

	Market Size £000	Estimated Potential VAT Revenue
Double glazing	400,000	60,000
Cavity Wall insulation	69,000	10,350
Loft insulation	30,000	2,250
Damp-proof coursing	30,000	4,500
Instantaneous showers (as Appendix I)	95,000	11,350

JF2501

Secretary of State for Industry

= PS/C+E
PS/ EST MSTC
CST MSTR
SIR D WASS
Mr MIDDLETON
Mr MOORE
Mr [illegible]
Mr GRIFFITHS
Mr MARTIN Mr FRENCH
Mr [illegible] KEMP

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

January 1983

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
LONDON SW1

31 [illegible] 83

AST. 31/1.

Dear Geoffrey,

[illegible] OF ZERO-RATING IN [illegible]STANTANEOUS SHOWERS

I [illegible] a letter sent to me by the Association of [illegible] of Domestic Electrical Appliances covering a detailed case they have made for maintaining zero-rating for VAT when an instantaneous shower is supplied and installed in a room for the first time.

2 I understand that, subject to the outcome of a current appeal, such work would become subject to VAT at the standard rate following the implementation of a House of Lords' judgement given last year. Geoffrey Howe recognised that full implementation of the judgement would have imposed an extra tax burden of £[illegible]0m on industry so he announced in his Budget statement last year his intention of relieving £[illegible]0m of the extra tax burden by means of an Order to continue zero-rating for some of the most commonly recognised forms of building alterations, other than instantaneous showers.

3 There seems to me to be a good case for according the showers equivalent treatment, should that in fact prove to be necessary when the current litigation is concluded. In terms of size, although the instantaneous shower market is much smaller than that for double glazing, it is bigger than those for cavity wall insulation, loft insulation, or damp-proof coursing for which the maintenance of zero-rating has been agreed. If energy conservation considerations should have been a factor in that decision, then these apply to instantaneous showers at least as strongly as to (say) double-glazing. Zero-rating for the showers could also presumably be given without jeopardising clarity in the law to any greater extent than zero-rating of the other industries for which it has been agreed.

/4 Finally ..

4 Finally, the domestic electrical appliance industry, which has shed 30% of its workforce in 3 years, has been having quite a tough time recently. It would be anomalous if instantaneous showers, which at present is one of the more encouraging sub-sectors, were now to be depressed by a tax change which is not being specifically sought in order to raise revenue but is simply one almost unintended outcome of a desirable clarification of the law in an important but difficult area.

5 I should therefore be glad if you could consider the AMDEA request sympathetically.

Yours ever

Patrick

The Association of Manufacturers of Domestic Electrical Appliances

AMDEA

From the Director General
J. P. Collis

Leicester House
8 Leicester Street
London WC2H 7BN

tel: 01-437 0678
telex 263536

Rt Hon Patrick Jenkin MP
Secretary of State for Industry
Department of Industry
Ashdown House
123 Victoria Street
London SW 1

14th January 1983

Mr Preston ... TO
25/1/83 [illegible] ... 25/1/83
... 25/1/83
... 25/1/83
Mr Perth
Mr Dell
Mr Wright

Dear Mr. Jenkin

PROPOSAL TO RETAIN ZERO-RATING ON INSTANTANEOUS SHOWERS

We are writing to you as the sponsoring Minister for our industry to ask you to put forward the enclosed proposal to the Treasury on our behalf.

We have discussed the matter with your officials and also, in order to keep them informed, with officials from Customs and Excise. We should perhaps stress that we are not seeking to deprive the Revenue of any monies which they are currently obtaining. We are seeking the continuation of a current policy which has been thrown into doubt, as the Chancellor has recognised, by legal judgements.

The Chancellor has stated that he wishes to relieve the construction industry of most the tax which the House of Lords judgement would otherwise impose on industry, and Customs and Excise have stated that there is no primary intention to raise revenue as a result of the judgement. We ask therefore that a specific reference be made to instantaneous showers by a Treasury Order to prevent a serious setback to an industry that is solely catered for by UK manufacturers.

Yours sincerely

J P Collis

J P Collis
Director General

INSTANTANEOUS SHOWER PROPOSAL

1. PROPOSAL

That the supply and installation of an instantaneous shower in a room for the first time be zero-rated by a Treasury Order as has been passed in the case of double glazing and committed in respect of loft and cavity wall insulation and damp-proof coursing.

This could be achieved by amending item 2 of group 8, schedule 4 FA 1972 to insert as follows:

Item 2 (c) (The supply) "in the course of the installation of an instantaneous shower for the first time in a particular location in,"

2. SUMMARY OF CURRENT SITUATION

The supply of an instantaneous shower installed in a room for the first time has, ever since the introduction of VAT, been treated as a zero-rated supply. The decision of the House of Lords in the matter of Customs and Excise v. ACT Construction Ltd has now cast doubt upon the interpretation of zero-rated for small works and buildings. The Chancellor of the Exchequer recognised the problem caused by the House of Lords decision in his Budget Speech of 9th March 1982 (see Appendix IV).

The change in interpretation has been held up pending the hearing by the Court of Appeal by the VIVA Gas Appliances Ltd case. The Commissioners of Customs and Excise lost this case in the High Court in a judgement which challenged several of the assumptions made following the ACT case. If the Commissioners eventually win the VIVA Gas case it is probable that in most cases the supply and installation of an instantaneous shower in a room for the first time will have to be treated as standard rated. We are therefore asking for a Treasury Order to zero-rate such supplies as has been done in the case of double glazing and promised with regard to cavity wall and loft insulation and damp-proof courses.

3. REASONS FOR PROPOSAL

(i) As about 85% of all installations have previously been zero-rated, a change will be a major disruption to the industry. Previous experience suggests such a change would cause the market to decline significantly. It is now generally recognised that the frequent changes in purchase tax levels experienced under previous administrations were a major cause in the weakening of the domestic electrical appliance industry which led to growth of imports.

(ii) The market has a value of £95 million (installed value) encompassing an estimated 431,000 units (see Appendix I). The market is met solely by UK manufacturers. Around 1100 people work directly on the manufacture of showers, a number increased by a further 2-3000 working for component suppliers. Further, some 2000 workers are employed in installation work, plus an equal number in external sales, marketing and distribution. Not only is the UK market dominated by UK manufacturers but, due to the steady

growth of the market, these manufacturers have also been able to exploit overseas markets. It is estimated that exports in the year 1982 were worth around £3 million (see Appendix II).

(iii) The installations named by the Chancellor for specific zero-rating all relate to energy saving. The installation of instantaneous showers should also be encouraged on the grounds of energy and water conservation. It is estimated that energy savings of £5.2 million per annum will be at risk if standard rating proceeds (see Appendix III). Installation of showers is certainly as effective in energy saving terms as the other items listed.

(iv) The addition of instantaneous showers to the Treasury Order would not cause a loss of revenue to the government. The Chancellor indicated that he wishes to relieve most of the tax which the House of Lords judgement would have imposed on the industry. The additional tax revenue produced by showers, based on the current market size, would realise £11.35 million (see Appendix I) which is more than would be produced by cavity wall insulation, loft insulation or damp-proof coursing individually (see Appendix IV).

4. SUBMITTING BODY

This proposal is submitted by AMDEA (The Association of Manufacturers of Domestic Electrical Appliances) on behalf of the companies concerned in the manufacture of electric showers (see Appendix II).

J P Collis
Director General

14th January 1983

Appendix I

The figures in this appendix relate to Electrical Instantaneous Showers only. It is estimated that this accounts for 95% of the total market, the other 5% being gas installations.

1. a) Market Size

Units (12 months to 30.6.82) = 431,000.

Installer	Market Share (Units) %	Installed value £000
Builder/plumber	33	28,446
Shower Manufacturer	14	26,550
Electricity Board	17	15,533
D I Y	19	9,827
Others	17	14,654
	100	95,010

The installed value per unit is highest at £440 for shower manufacturers, who install most of the high price units, and lowest for D I Y at £120 per unit. The other installers' prices are c. £200 per unit.

b) VAT raised if Standard Rating proceeds:

		£000
Total Market		95,010
Less D I Y (current standard rated)	9,827	
Less still zero-rated (new or reconditioned houses)	9,500	
Total		19,327
Value becoming subject to Standard Rating		75,683
VAT thereon @ 15%		11,350

c) Market assumptions for 1983:

If zero-rating continues + 10% = 474,000 units

If standard-rating enforced - 10% = 388,000 units

Source for above figures: AMDEA, Electricity Council, AGB Research

Appendix III

ENERGY USAGE

Based upon A G B Research figures and manufacturers' returns to AMDEA, 431,000 instantaneous shower units were installed during the year ended 30th June 1982.

The imposition of standard rating is estimated to reduce installations by 10-15% per annum.

It is assumed that shower buyers will use the shower instead of a bath once per day.

Based on an estimated loss of shower installations of 10% per annum, resulting from standard rating, 43,000 baths would be taken daily instead of showers (see below).

In KW terms, this extra demand would be:

43,000 x 2376 KW = 102 million KW

The annual cost of the extra demand measured in terms of the average of Area Electricity Boards' selling price of 5.1p per KW is £5.2 million.

No growth in the market has been assumed in these calculations although 10% per annum growth is projected by the industry if current VAT zero rating were to continue.

Appendix IV

i) Extract from Chancellor's Budget Speech - 9th March 1982

"I also propose to deal with the liability to VAT of certain kinds of building alterations, where there has in the past been serious doubt about what was liable to charge. A recent judgement of the House of Lords would have led, if applied in its entirety, to VAT being charged at the standard rate on a range of non-structural building alterations which had previously been free of charge. Though clarifying the law, this judgement would have imposed an extra £80 million of tax on the industry, which it can ill afford at present.

So I intend to re-establish the clarity needed, but in a way which will relieve the industry of all but £10 million of the extra tax burden. I shall, in due course, lay before the House an Order, which will have the effect of continuing to zero-rate three important kinds of alterations which might otherwsie be adversely affected by the House of Lord's judgement.

These are the most commonly recognised forms of double glazing, loft and cavity wall insulation and damp-proof coursing. This useful simplification of the law will cost the revenue about £70 million a year.

The other kinds of non-structural alteration covered by the judgement will become subject to VAT but, pending the completion of discussions with the industry, no steps will be taken to apply the tax before about the beginning of September."

Note: Full changes held up by Court of Appeal hearing relating to VIVA Gas.

ii) Estimates of items covered by Chancellor's Speech

	Market Size £000	Estimated Potential VAT Revenue
Double glazing	400,000	60,000
Cavity Wall insulation	69,000	10,350
Loft insulation	30,000	2,250
Damp-proof coursing	30,000	4,500
Instantaneous showers (as Appendix I)	95,000	11,350

PERSONAL AND CONFIDENTIAL

EXCHEQUER
12 JAN 1983
CST FST EST
MST(C) MST(R)
Sir D. Wass
Mr Middleton
Mr Kemp
Mr Ridley

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ
01-211 6402

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
Treasury Chambers
Parliament Street
London
SW1P 3AG

10th January 1983

Dear Geoffrey

To summarise, with ...

You wrote to me on 10 December about the next Budget.

Let me start where you, presumably, will start - with the appropriate size of the 1983-84 PSBR. I hope you will cleave firmly - and explicitly - to the MTFS. Last year's Red Book indicated a PSBR for 1983-84 of $2\frac{3}{4}$ per cent of GDP. However, it is now clear that the level of activity next year will be lower than was envisaged at the time of your last Budget, which implies a consequential upward adjustment of the PSBR. In the circumstances, a 'target' PSBR of 3 per cent of GDP would be perfectly acceptable. Assuming (in line with Table 1.8 of the Autumn Statement) a 1983-84 GDP of £294 billion, this translates into a PSBR of some £8.8 billion. The markets will be well content with any figure that begins with an 8, even up to £8.9 billion. I realise that what I am suggesting implies a PSBR larger than this year's likely outturn, perhaps by a sizeable margin; but there is no reason whatever why an unplanned shortfall this year should oblige you to abjure the perfectly proper scope you have for much needed tax cuts in 1983-84. By any objective standard-including international comparisons, I suspect - a PSBR of 3 per cent of GDP at this stage of the cycle is pretty good going, and sufficiently austere to present no threat to the attainment of the 7%-11% monetary growth target already foreshadowed for 1983-84. (I would certainly not advocate any relaxation there).

This would seem to leave you with scope for at least £2 billion of tax cuts. But whatever the precise figure I have no doubt that the centrepiece of your Budget should be an increase in the income tax threshold to a point where it is clearly higher in real terms than it was when we took office. In other words, you should announce at least a 'double indexation' of the

PERSONAL AND CONFIDENTIAL

personal allowances (and other thresholds etc). The political and economic case for this, not least on employment grounds, is well known to you and I will not waste space by repeating it. It would also transform our overall record on income tax where at present the reduction in the real level of the tax threshold is the one serious blot. Do not be put off by fears of the money you thus put back into the pockets of the people being spent on imports: British industry is now as well placed to meet home demand as it will ever be. Our objective is to keep monetary demand under firm control: it is emphatically not to use excessive taxation to suppress real demand and to enforce austerity for its own sake (or for that of the balance of payments). In any event, there is a good chance that any further weakening of sterling against the Continental currencies will be offset by some strengthening against the dollar.

As for the rest of the Budget, I doubt if I can think of anything that you have not already thought of and studied in some depth. In general, I would offer the following guidelines:

(i) give a high priority to alleviating the burden of the North Sea tax regime;

(ii) do <u>not</u> make any further reduction in the NIS;

(iii) do <u>not</u> seek to massage the RPI by a Healeyesque cut in indirect tax;

(iv) do a large number of small things, each of which costs relatively little, but which remedy long-standing grievances or at least display imagination and understanding.

I hope all this is of some help.

Yours ever
Nigel

NIGEL LAWSON

PS I would be happy to have a word with you at some stage about the separate but crucial question of the handling of a pre-election 'political' run on the pound.

N.

FROM: E KWIECINSKI
DATE: 10 January 1983

b/f for Chevening discussion

PS/CHANCELLOR — 2
(Miss Rutter)

cc Chief Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir D Wass
Mr Burns
Mr Middleton
Mr Bailey
Mr Byatt
Mr Kemp
Mr Cassell
Mr Evans
Mr Pestell
Mr G Smith
Mr Robson
Mr Griffiths
Mr Ridley
Mr French
Mr Harris
Mr Green)
Mr Battishill) IR
Mr Painter)
PS/IR
Mr Moore

CORPORATE TAXATION: BACKGROUND TO THE BUDGET

The Financial Secretary has seen Mr Moore's submission to the Chancellor of 22 December, and your minute of 29 December.

He found Mr Moore's paper very interesting and well put together.

He would go for reductions in:-

1) NIS
2) Industrial Rates and
3) CT

(in the above order).

Although he thinks the options for the first two are virtually closed.

E KWIECINSKI
10 January 1983

CONFIDENTIAL

From: J F Williams
12 January 1983

Pup

MR KEMP

cc PS/Chancellor
Mr Burns
Mr Littler
Mr Middleton
Mr Monck

BUDGET 1983

In early December Sir Douglas Wass invited the Governor of the Bank of England to submit to the Chancellor a paper setting out the Bank's views on monetary policy and related matters. The Deputy Governor today mentioned to Sir Douglas that this paper was almost ready and should be despatched shortly and before Chevening. The Bank had had to dilute their prescriptions somewhat because of recent developments in the markets and we should not be expecting anything earth-shattering.

JW

J F WILLIAMS

CONFIDENTIAL

DEPARTMENT OF TRADE 1 VICTORIA STREET LONDON SW1H 0ET Telephone 01-215 7877

From the Secretary of State

PWP

EXCHEQUER
12 JAN 1983

CST, FST, EST, MSTC, MSTR, Sir D Wass, Mr Middleton, Mr Bailey, Mr Kemp, Mr Lovell, Mr Moore, Mr Carey, Mr Ridley, Mr French, PS/IR, PS/C&E.

PERSONAL AND CONFIDENTIAL

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
London
SW1P 3AG

12th January 1983

Dear Geoffrey,

SPRING 1983 BUDGET

You wrote to me on 10 December asking any views I might have about the next Budget.

May I start with matters directly affecting my own Department.

Tourism and the Holiday Industry

I have already written to you about this. I can only re-emphasise what I have already said - which has been supported by other colleagues.

The Service Industries

The Service Industries are disadvantaged both in taxation terms and elsewhere. The main disadvantage in the tax field relates to allowances on buildings but - leaving aside the question of hotels and other tourist projects - I can well understand your reluctance to do anything here pending the outcome of the general review of the Corporation Tax. But where you do take new initiatives, I would press that they should be even-handed and help services as well as manufacture. We did in the end do this in the case of the Business Start-Up Scheme. But it is a point which needs to be kept in mind all the time.

There is also the question of regional assistance. This surely ought to be generally available and not confined to manufacture. I can understand the reasons for excluding retail shops but where service industries generate additional employment they ought to receive equality of treatment.

From the Secretary of State

PERSONAL AND CONFIDENTIAL

not Budgetary

Aid and Trade Provision (ATP)

The ATP provision is inadequate and was accepted by E as inadequate. I have already made the point that if we are going to give money away anyway it is better to give it away in a form in which we got some return rather than in a form in which we were not guaranteed of any. To this extent, the erudite calculations advanced by the Treasury are irrelevant.

If an adequate supply of ATP funds cannot be found within the existing Overseas Aid Budget, there is a case for considering a specially ear-marked additional provision. Here again, what matters is not whether an economic return can be seen on the expenditure - although we would argue that it can - but whether the return is better than would emerge from the other forms of Government expenditure which may be contemplated. If one wants a scheme for keeping people off the unemployment register, ATP is a much better bargain than Community Work Schemes, or devices of that sort. It is better to supply power stations to China or even steel works to the Philippines, than to pay people to find unnecessary jobs to pay somebody else to do.

VAT

There is a specific point which relates to my Department's insolvency responsibilities. At present creditors can secure VAT relief on bad debts only if the debtor company is put into liquidation. Some creditors petition for a winding up order against a company which is only in receivership in order to obtain VAT relief. Extending this relief to receivership would tend to counteract this practice and avoid some liquidations. This in turn would reduce the staff pressures on the Official Receiver Service.

May I now turn to more general taxation matters.

Capital Taxation

So far as structure is concerned, there is nothing much I now need to say. But this will be our last chance to reduce rates in this Parliament. This is particularly true of the Investment Income Surcharge. I invented it - as I invented the Excess Profits Levy. May I now look to you to demolish it, as Rab Butler demolished the EPL? An index-linked pension is worth far more than investment income. If we are not prepared to do anything about index-lined pensions, at least we should ensure that investment income is not treated more harshly for tax purposes than such a pension. You will find this point made

PERSONAL AND CONFIDENTIAL

From the Secretary of State

forcibly in our last Election Manifesto. If we were to phase out the investment income surcharge we should at least find ourselves on the same side as our own supporters.

Corporation Tax

I have, as you know, always favoured reducing the rate of Corporation Tax. But this is an item which more than once has been squeezed out at the last moment.

The small companies rate now has an increasingly absurd marginal band - up to £225,000 - with a correspondingly high marginal rate. We have always resisted changing over to a slice basis under which the first £100,000 or so would be charged at 40%, on the grounds that this would benefit the larger companies. But if, in principle, one wishes to reduce the rate of Corporation Tax generally, this ceases to be much of an objection: and it would remove the marginal problem altogether. If you were able to be sufficiently generous, a reduction to 35% on the first £100,000 would also give a substantial relief to the smallest companies.

Yours,

Arthur

LORD COCKFIELD

From: W.R. Rees-Davies, Q.C., M.P.

Received

TOP COPY

HOUSE OF COMMONS
LONDON SWIA OAA

EXCHEQUER
REC. 10 JAN 1983
ACTION ~~DR A BUDGET~~ 12/1
COPIES TO cc CST, FST, EST, MST(C), MST(R) Mr Middleton, Mr Moore, Mr Kemp PS/IR, PS/C&E 1905

6th January, 1983.

Dear Geoffrey

Thank you for your letter of 23rd December. With regard to any financial recommendations, bearing in mind the Budget timetable we will certainly let you have our collective recommendations, in writing to you and Arthur Cockfield, at the end of the first week in February, as you suggest.

With regard to the other recommendations, we will seek to give you a realistic statement of policy needs without having to summon any special outside witnesses or hold special meetings for outsiders for such purposes. I feel sure that you will be persuaded that there are a number of changes within the industry greatly needed to secure the successful expansion in an industry which is so labour intensive.

Yours Sincerely
Billy

The Rt. Hon. Sir Ceoffrey Howe, Q.C., M.P.
House of Commons,
London, S.W. 1.

PS/CST
PS/FST
PS/EST
PS/MST(C)
PS/MST(R)
Sir D Wass
Sir A Rawlinson
Mr Littler
Mr Burns
Mr Middleton
Mr Moore
Mr Evans
Mr Cassell
Mr Kemp
Mr Hall
Mr Allen
Mr Salveson
Mr Ridley
Mr French
Mr Harris
Mr Norgrove

PS/C&E
PS/IR

CONFIDENTIAL

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

12 January 1983

Michael Scholar Esq
No 10
Downing Street
LONDON SW1

Dear Michael,

1983 BUDGET DAY

We have as you know been working towards a Budget on 15 March, and the Prime Minister earlier indicated that she was content with this (your letter of 1 October). Our consultations show no major difficulties in terms of overseas visits, awkward announcements of economic statistics and so on. If the Prime Minister remains content, the Chancellor is inclined to think that the date of 15 March should be announced - as in the last two years - in the first Business Statement after the Christmas Recess, which is likely to be Thursday, 20 January this year. I understand that the normal form is for the announcement to be made in reply to a Question by the Leader of the Opposition, who is prompted in advance by the Chief Whip.

I am sending copies of this letter to David Heyhoe and to Murdo Maclean. If the Lord President also agrees to an announcement being made on 20 January, I should be grateful if the Chief Whip's Office could make the necessary arrangements.

Yours ever,

J O Kerr

J O KERR

cc PS/CST
PS/FST
PS/EST
S/MST(C)
S/MST(R)
Sir D Wass
Sir A Rawlinson
Mr Littler
Mr Burns
Mr Middleton
Mr Moore
Mr Evans
Mr Cassell
Mr Kemp
Mr Hall
Mr Allen
Mr Salveson
Mr Ridley
Mr French
Mr Harris
Mr Norgrove

PS/C&E
PS/IR

CHANCELLOR OF THE EXCHEQUER

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

Michael Scholar Esq
No 10
Downing Street
LONDON SW1

12 January 1983

Dear Michael,

1983 BUDGET DAY

We have as you know been working towards a Budget on 15 March, and the Prime Minister earlier indicated that she was content with this (your letter of 1 October). Our consultations show no major difficulties in terms of overseas visits, awkward announcements of economic statistics and so on. If the Prime Minister remains content, the Chancellor is inclined to think that the date of 15 March should be announced - as in the last two years - in the first Business Statement after the Christmas Recess, which is likely to be Thursday, 20 January this year. I understand that the normal form is for the announcement to be made in reply to a Question by the Leader of the Opposition, who is prompted in advance by the Chief Whip.

I am sending copies of this letter to David Heyhoe and to Murdo Maclean. If the Lord President also agrees to an announcement being made on 20 January, I should be grateful if the Chief Whip's Office could make the necessary arrangements.

Yours ever,

John Kerr.

J O KERR

CONFIDENTIAL

(PWP)

EXCHEQUER

14 JAN 1983 14/1

Action: Mr Kemp

COPIES TO: CST FST EST

MST(C) MST(R)

Sir D. Wass

Sir A. Rawlinson Mr Littler
Mr Burns Mr Middleton
Mr Moore Mr Evans Mr Cassell
Mr Hall Mr R.G. Allen Mr Salveson.
Mr Ridley Mr French
Mr Hartis Mr Norgrove
PS/C&E
PS/IR.

10 DOWNING STREET

From the Private Secretary

14 January 1983

Dear John,

1983 BUDGET DAY

Thank you for your letter of 12 January.

The Prime Minister does indeed remain content with 15 March for Budget Day. She is also content that this should be announced in the first Business Statement after the Christmas Recess.

I am sending copies of this letter to David Heyhoe (Lord President's Office) and Murdo Maclean (Chief Whip's Office).

Yours sincerely,

Michael Scholar

John Kerr, Esq.,
HM Treasury

CONFIDENTIAL

Mr Moore
CST, FST, EST, MST(C), MST(L)
Sir D. Wass, Mr Byrns
Mr Bailey, Mr Middleton
Mr Kemp, Mr Evans
Mr Lovell, Mr Ridley
Mr French, Mr Howard
PS/IR PS/C&E

Secretary of State

Northern Ireland Office
Stormont Castle
Belfast BT4 3ST

Mr Robson
Nothing beyond
JP's support

Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

17 January 1983

please B/9/5 and B/39

Dear Geoffrey

I have just seen a copy of Arthur Cockfield's letter to you of 29 October suggesting fiscal measures to assist in the tourist industry, and copies of Nicholas Edwards' and George Younger's letters on the same subject.

I fully support the views expressed by Arthur and have no doubt that his proposals would be of considerable benefit to the Northern Ireland tourist industry. As you will appreciate tourism in Northern Ireland has suffered greatly from the image of the Province created by the security situation. During the early and mid-1970s there was a substantial decrease in visitor numbers. Of recent years there have been distinct signs of an increased interest in the Province as a holiday destination and strenuous attempts are being made by the Northern Ireland Tourist Board and by local travel and holiday interests to restore the flourishing tourist industry which existed here in the late 1960s.

I believe that there is considerable potential for the development of tourism in Northern Ireland and that the industry is capable of making a very useful contribution to employment in the Province. The improvement in the building allowances for tourist accommodation, which is proposed in Arthur Cockfield's letter, would be particularly useful to us and should help to reduce the dependence of investors on Government grants.

I would add that I am convinced that there is an important link between these tourism promotional activities and our efforts to attract inward

26/96

industrial development to Northern Ireland. A successful tourist campaign can correct misconceptions about conditions here and provide valuable reassurance to potential investors and their managers, and their families.

I am copying this letter to the recipients of Arthur Cockfield's letter.

Yours

Tom

CONFIDENTIAL

DEPARTMENT OF THE ENVIRONMENT
2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

MINISTER FOR LOCAL GOVERNMENT
AND ENVIRONMENTAL SERVICES

EXCHEQUER
19 JAN 1983
ACTION: Mr Kemp
COPIES TO: CST, FST, EST, MST^C, MST^R, Sir D Wass, Mr Burns, Sir A Rawlinson, Mr Byatt, Mr Bailey, Mr Widdup, Mr Moore, Mr Pestell, Mr Hopkinson, PS/C+E, PS/IR, Mr Battishill (IR), Mr Rickley, Mr French.

18 January 1983

7 Hesitup

Dear Geoffrey,

BUDGET 1983

Michael Heseltine wrote to you on 6 January, submitting DOE ideas for possible inclusion in the 1983 budget. Two items concerning tax reliefs for owners of historic houses were deliberately excluded from his list, as he could have had a personal interest in the outcome of any discussions on them. As the same consideration also applies to Tom King, I have taken responsibility for these items and am writing about them separately in this letter.

The first proposal is for income and corporation tax allowances for repairs to listed buildings. Repairs to historic buildings are frequently more costly than repairs to other buildings, because they require the use of special materials, unusual techniques, specialised skills - or all three. Also, owners of historic buildings may not carry out new work (which is VAT-free) without Listed Building Consent, but conversely they may be served with a Repairs Notice if they seriously neglect their buildings. Offering some form of relief to owners for repairs, would encourage them to undertake necessary work which might otherwise be neglected, to the detriment of the heritage. It could also encourage ownership of listed buildings and so reduce the number likely to come into public ownership as the only means of saving them. The most straightforward relief would be an income and corporation tax allowance, equal to a set proportion of the rateable value of the historic house. Alternatively, the size of the tax allowance could be related to actual expenditure on repairs to the building, up to a prescribed maximum per annum. Either such relief would be very flexible, as its cost could be regulated by applying it to all listed buildings, to Grade I and II* buildings only, or just to Grade I buildings. I am, of course, prepared to work up these ideas in detail, if you are willing to accept the principle that there is a case for relief.

Secondly, I suggest that contributions to maintenance funds for historic buildings or gardens should qualify for tax

115 20/1

concessions. As the purpose of such funds is to provide for the maintenance and preservation of heritage property, contributions would rarely be related to any business objective; but they could greatly reduce the need for Government help in preserving historic buildings. The concession could be introduced quite simply as an extension of the kind of relief available under section 48 of the Finance Act, for contributions to local enterprise agencies. The cost would of course depend entirely upon the reaction of those willing to make contributions.

Yours Sincerely,
Irwin

LORD BELLWIN

The Rt Hon Sir Geoffrey Howe QC MP

CONFIDENTIAL

FROM: D R NORGROVE
DATE: 19 JANUARY 1983

1. MR KEMP
2. MR KERR

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir Douglas Wass
Sir Anthony Rawlinson
Mr Littler
Mr Burns
Mr Middleton
Mr Bailey
Mr Moore
Mr Mountfield
Mr Evans
Mr Cassell
Mr Monck
Mr Burgner
Mr Monger
Mrs Lomax
Mr Hall
Mr Allen
Mr Ridley
Mr Harris
Mr French

PS/Inland Revenue
Mr Painter
PS/Customs & Excise
Mr Howard

TIMETABLE TO THE BUDGET

Attached is a further timetable to the Budget, which is little changed from the versions you have seen before.

2. I am also attaching (not for all) an outline schedule of meetings. This is of course very tentative and unlikely to be followed in detail. For that reason I am not giving it wide circulation. But, as we have discussed, last year's overview meetings were generally thought to have provided useful fixed points in the proceedings. For this year we agreed that they would fit well into the weekly timetable if they were held each Tuesday at 11 am. You will be making arrangements for the holding of the first meeting.

3. The basis for the overview meetings would be reports on the state of Budget business to be made each Friday.

DRNorgrove

D R NORGROVE

JANUARY — FEBRUARY — MARCH — APRIL

21 | 28 | 4 | 11 | 19

17 Ecofin

7 Ecofin

8–10/11 Interim Committee

7 Ecofin

31 – 10 ? Easter Recess

E.R.

27 Paper circulated to Cabinet

1 Publish PEWP

3 E(?) Cab

15 Budget Day

25 Pre-Budget Forecast

21–23 Provisional post-Budget forecast

1–3 FSBR forecast finalised

15 IAF published

19 VAT and specific duties structural

25 – Decisions on tax rates

15 Announce tax changes

Discussions and decisions on upratings

15 Upratings announced

31 Probable last date for handling Finance Bill to House authorities

8 Probable last date for publication of Finance Bill

19–21 Likely slot for 2nd Reading Debate

11 First draft of Speech

25 (i) Outline FSBR (ii) Second draft of Speech

1 Third draft of Speech

15 Speech + FSBR

18 Ind prod

21 RPI PSBR

8 Money (provisional)

11 RPI

15 Ind prod

8 Money (provisional)

9 CGBR

15 Ind prod

18 RPI

Note: Timing of unemployment figures uncertain - possibly around first Tuesday of each month. The timing of the trade figures is also erratic at present.

(Pwp)

Board Room
H M Customs and Excise
King's Beam House
Mark Lane London EC3R 7HE

From: Sir Douglas Lovelock

Date: 24 January 1983

CHANCELLOR OF THE EXCHEQUER

cc: Chief Secretary
Financial Secretary
Economic Secretary
Minister of State(C)
Minister of State(R)
Sir Douglas Wass
Mr Burns
Mr Middleton
Mr Byatt
Mr Moore
Mr Kemp
Mr Cassell
Mr Griffiths
Mr Hall
Mr Ridley
Mr French
Mr Harris
Sir L Airey

BUDGET 1983: EXCISE DUTY OPTIONS

This paper deals with the main excise duty options for this year's Budget. Its form and layout is the same as that adopted for the last few years. Our starting point has been what you described in your Budget Statement last year as the "sensible presumption" (used as a conventional assumption in the NIF for some years) that the specific duties will be increased broadly in line with the rate of inflation in the previous calendar year. I understand that at the recent Chevening weekend you expressed the preliminary view that you would wish to go for something on these lines. As you know, the rate of inflation in the calendar year 1982 has now been announced, via the December RPI, as 5.4%.

Internal circulation: Mr Fraser, Mr Freedman, Mr Howard, Mr Middleton, Mr Jenkins, Mr Packman, Mr McGuigan, Mr Battle, Mr Smith, Mr de Berker, CPS

2. A revalorisation package, subject to sensible roundings of price changes, is illustrated in Annex 1. (All revenue figures in the Annexes include consequential VAT). It would yield additional revenue of about £590 million in 1983-84 and about £600 million in a full year, for an RPI impact effect of about 0.5%. Given the roundings, all duty increases lie in the range of 5%-6.25%. Annex 2 deals with each major duty in greater detail. It shows the effect of strict, unrounded revalorisation in line with the 5.4% increase in the RPI and tabulates illustrative rounded price changes including, where practicable, not only the price change shown in Annex 1 but possible alternatives on either side. It then lists the main arguments relating to each duty together with other relevant facts. A note of an inter-Departmental meeting we held with officials of the sponsoring Departments and DHSS about alcoholic drinks and tobacco is attached at Annex 3. In most cases the Ministers concerned are likely to write formally to you with their views.

3. Annexes 1 and 2 have been drafted without prejudice to the outcome of the inter-Departmental exercise in which officials are examining the case for abolishing or reducing car tax and possible recoupment of the cost from other taxes on motoring; a report on this will be made at about the end of the month. Separate sub-missions will also be made about consequential increases for tobacco products other than cigarettes and for minor alcoholic drinks and about rebated oils,, avgas etc and matches and mechanical lighters. Betting and gaming is the subject of a separate series of papers.

4. So far as VED is concerned, this paper (which incorporates the views of the official Treasury, who have the policy responsibility in this area) deals only with the rates on cars and light vans. Following the restructuring in last year's Finance Act, different considerations apply to VED on goods vehicles. The Secretary of State for Transport wrote to you recently suggesting a package of

measures to bring the taxation of heavy lorries more closely into line with road costs, and FP will be making a separate submission on this.

TAXABLE CAPACITY

5. In terms of taxable capacity, it is hard to identify any excise duty which could not bear revalorisation this year. Although a number of the excise duty industries have been experiencing a difficult time in the recession, the interim NIF suggests that revalorisation should not cause a volume fall in 1983-84. This reflects partly the forecast modest recovery in consumers' real expenditure, which would lead to more substantial increases if real prices were allowed to fall. The position is illustrated in the following table:-

	Approximate volume growth if no duty changes (ie real value allowed to fall)	Approximate volume change due to revalorisation	Overall approximate volume change 1983-84 compared with 1982-83 given revalorisation
	(%)	(%)	(%)
Beer	+1½	-½	+1
Spirits	+4½	-3	+1½
Wine	+7	-1½	+5½
Tobacco	+1½	-1½	0
Petrol	+4	-½	+3½
Derv	+4	-½	+3½

These volume changes can only be treated as broad orders of magnitude. The figures for beer are particularly uncertain, since the present equation does not account satisfactorily for the consumption pattern of recent years. It seems best to regard the net effect on beer consumption as broadly neutral. Otherwise, you will see

that the effect on the volume of tobacco consumption, where there is in any a case a long-term secular trend (taken account of in the table above) against smoking of the order of 1%-2% a year, would also be broadly neutral; but in the other cases, we would expect slight increases in consumption even with revalorisation.

6. Other considerations relating to each duty are detailed in Annex 2. These should assist you in deciding whether to go beyond, or to temper, the effects of revalorisation in each particular case, but there are certain key points which it may be helpful to summarise at this stage. In the field of alcoholic drinks and tobacco, these are as follows:-

(a) Beer Revalorisation would add approximately 0.9p, including VAT, to the cost of a typical pint. There appears to be no satisfactory alternative to 1p (5.9%) as the rounded price change since ½p (2.9%) and 1½p (8.8%) would represent either only about one-half or rather more than one-and-a-half times revalorisation respectively. In our view beer could comfortably stand 1p (on a typical price of 60p per pint it seems almost inconsequential), but if there were to be any question of a larger increase you will wish to bear in mind that the Brewers' Society have lobbied strongly against a real increase in the light of the substantial falls in consumption and output over the last three years. We also believe they would be likely to react much more vigorously this year than in the past if there should be further discrimination in the treatment of beer compared with spirits.

(b) Wine. Table wine is by far the most buoyant of all the excise duty goods in consumption terms and, in principle, is a candidate for a real increase. However, although they will not be concluded in time for the Budget,

the infraction proceedings in the European Court concerning our wine/beer ratio are now at an advanced stage, and any attempt to single out wine ahead of beer would be highly provocative. We therefore recommend identical increases in percentage terms on wine and beer this year. This means about 5½p on a 75cl bottle of table wine for 1p on beer.

(c) Spirits. The implication of the brewers' argument is that same percentage increase should be applied to spirits as to beer. Applied to the hilt, this would mean about 30p on a bottle of spirits - marginally more than strict revalorisation (27p) - for 1p on beer. On the other hand, the spirits industry is still in a fairly poor state, and MAFF officials have represented to us that the case for restraint on taxation of spirits is even greater than that for beer because of the unemployment factor in Scotland; hence they would be prepared to contemplate a further modest narrowing of the gap between spirits and beer. On balance, we think it would be justifiable to revalorise the duty on spirits this year, but the industrial considerations could point to a small element of shading down, to 25p (5%) as the rounded price change.

(d) Tobacco. The tobacco industry has suffered substantial falls in consumption, output and employment over the past two years, partly as a result of the significant real duty increases in 1981. Industrial considerations therefore argue against a real increase this year. On the other hand, the tobacco health lobby remains strong and we believe that, despite their calls for a standstill this year, the industry could stand revalorisation (3½p). (You will want to consider 4p, I think, but the rise is then as much as 6.4%). The use of a halfpenny in the price increase would be unusual but we would expect

manufacturers to adjust the prices of some brands by 3p and others by 4p.

7. As far as the motoring taxes are concerned, leaving aside any suggestions which emerge from the inter-Departmental review, the main points are:-

(a) Petrol. Petrol consumption is buoyant, assisted by the continued strong competition among the oil companies which has led to lower prices in the face of the general glut in the oil market. UK prices are now noticeably low by European Community standards. The duty could certainly stand revalorisation ($4\frac{1}{2}$p) and, while we are conscious of the Conservative backbench concern about the impact of duty increases on rural motorists, the general weight of argument suggests that it would probably be the prime candidate if selective real duty increases were required.

(b) Derv. You have yourself commented (Miss Rutter's undated minute received on 22 December) that this should be considered separately from petrol for industrial as well as environmental reasons, and we believe that the potential effect on business costs probably rules out a real increase this year. On the other hand, the Secretary of State for Transport has drawn attention to the importance of revalorising the derv duty in the context of the policy on heavy lorries. We would not recommend going beyond revalorisation (3.7p) and suggest that there could be a marginal shading down to $3\frac{1}{2}$p (5%) as the rounded price change.

(c) VED. It has been customary to fix the rate of duty in multiples of £5, which is marginally more convenient for the Department of Transport and their agents. Revalorisation of 5.4% on the present £80 licence would

strictly amount to £4.32. FP have discussed with DTp officials and established that a rounding to either £4 (5%) or the more conventional £5 (6.25%) is likely to be acceptable. For the present we have shown £5 in Annex 1 on revenue grounds, but there is a clear choice to be made here.

NEXT STEPS

8. You will wish to decide in the light of this submission and your approach to the Budget judgment whether to go for an across the board revalorisation package or whether to act more selectively. If in the latter event you can give us some indication of your thinking, we should be glad to provide further packages with appropriate weightings. Our deadlines for decisions are 18 February for decisions on structural changes, if any, and 25 February for rate changes.

DM

DOUGLAS LOVELOCK

ANNEX 1

REVALORISATION PACKAGE (SUBJECT TO SENSIBLE ROUNDING)

	Typical price change (a)	Specific duty increase %	Revenue full year (b) £m	RPI impact effect %
Beer	1 pence/pint (b)	5.9	90	0.1
Wine	5½ pence/75 cl light wine	5.9	25	neg
Spirits	25 pence/bottle	5.0	25	0.05
Tobacco	3½ pence/20 KS	5.6	115	0.15
Petrol	4½ pence/gallon	5.5	210	0.1
Derv	3½ pence/gallon	5.0	45	nil
VED	£5 car licence	6.25	90 (c)	0.05
			600	0.5 (d)

NOTES

(a) Price effect includes VAT except for VED.

(b) For a 15 March Budget first and full year revenue will be identical except for beer and tobacco where the first year revenue will be about £5 million less in each case.

(c) VED increases on heavy lorries, as proposed by the Secretary of State for Transport, would produce up to £20 million more without adding to the RPI impact effect.

(d) RPI effects do not sum because of rounding.

ANNEX 2

BEER DUTY

	Typical price effect pence per pint (VAT inclusive)	Duty increase %	Revenue* full year £m	RPI impact effect %
Revalorisation	0.9	5.4	80	less than 0.1
Rounded price change	1	5.9	90	less than 0.1

Typical current price: 60p per pint (on-licence price for non-premium bitter in a public bar)

Arguments

For

(i) Relatively low RPI effect per £m revenue.

(ii) Low price elasticity of demand. Traditionally a buoyant revenue-raiser, albeit a little less so in last three years. The biggest potential revenue-raiser in the drinks field. Should stand at least revalorisation.

(iii) March 1982 Budget broadly maintained duty in real terms at about Labour Government peak of 1975-76. Revalorisation would repeat this effect.

(iv) Health and social policy implications argue for at least revalorisation.

Against

(i) Production of beer fallen by 3% comparing the twelve months ended November 1982 with same period in 1981, on top of falls of about 4% and 5% in the previous two years. Previously the industry had enjoyed a steady expansion of 2% a year. Industry likely to be strongly opposed to any increase beyond sensibly rounded revalorisation.

* 1983-84 revenue will be about £5 million less than that for a full year.

(ii) Beer duty has increased in real terms under present Government. Brewers have blamed this for fall in consumption (although see comment (i) below). Could prove controversial to impose a real increaze this year.

(iii) The brewers have contrasted treatment of beer with more lenient treatment of spirits (although this reflects judgments as to respective taxable capacity, and substitutability is doubtful). Would be controversial to single out beer again ahead of spirits this year.

(iv) Presentational difficulty that duty is still widely regarded as regressive ("working man's pint") although recent analysis of FES data suggests neutral or only mildly regressive.

<u>Comment</u>

(i) Recent decline in consumption followed steady gentle expansion since the 1950s although the brewers had been concerned that the rate of growth was low by the standards of other drinks. Future of beer consumption now uncertain; but the decline probably due not so much to duty increases (pace the brewers) as to depth of recession and fall in consumers' real expenditure on drink and tobacco. Revalorisation would probably leave total consumption in 1983-84 at about its 1982-83 level.

(ii) The wine/beer infraction proceedings are currently before the European Court, and will need to be taken into account.

(iii) Because of relatively low weight of tax in price, increases in beer taxation represent only small addition to total price - for example, 1p rounded revalorisation would increase price of typical pint by less than 2%.

(iv) The Brewers Society have complained about unfair competition from cider which enjoys a duty rate of only 40% of that on the weakest beers. We agree that the cider industry is in a healthy state, benefiting from increased consumption (in contrast to beer), and that there is a strong case for a real increase in duty this year. This will be examined in detail in a separate submission.

WINE DUTY

	Typical price effect pence per 75 cl bottle of table wine (off-licence, VAT inclusive)	Duty increase %	Revenue 1983-84 and full year £m	RPI impact effect %
Revalorisation	5.0	5.4	25	neg
Rounded price change	5½	5.9*	25	neg

Arguments

For

(i) Relatively low RPI effect.

(ii) Consumption of table wine buoyant. Clearances currently much higher than in previous year.

(iii) Value of duty has fallen substantially in real terms from Labour Government peak of 1975. Considerable scope in principle for catching-up increases, but duty changes on table wine should not exceed those for beer (see below).

(iv) Duty is mildly progressive.

(v) Product largely imported.

(vi) Wine trade will have benefited from substantial boost to cash flow from duty deferment to be implemented from 15 February.

(vii) Health and social policy implications argue for at least revalorisation.

* Identical to beer. The legal duty rate will be determined by need not to increase wine/beer duty ratio.

Against

(i) Wine/beer infraction proceedings currently before European Court. Important not to increase duty ratio as between the two products. Effectively limits increase on wine to about 5½p for every 1p on beer.

(ii) Consumption of fortified wine falling. Clearances have continued to decline gradually from peak in 1979-80.

Comment

(i) Assuming that the duty on fortified wine is increased pro-rata to the duty on table wine, the price of a bottle of sherry will increase by 1.3p for each 1p on table wine.

(ii) Revenue estimates are based on the assumption that existing relativities will be maintained between different types of wine.

SPIRITS DUTY

	Typical price effect pence per bottle (off-licence, VAT inclusive	Duty increase %	Revenue 1983-84 and full year* £m	RPI impact effect %
Revalorisation	27	5.4	25	0.05
A	20	4.0	20	neg
B	25	5.0	25	0.05
C	30	6.0	30	0.05

Typical current price: £6.90 per bottle of whisky (off-licence)

Arguments

For

(i) Important to maintain real value of duty. Value of duty in real terms has fallen substantially in recent years from Labour Government peak of 1975. Increases have been less than the rise in the RPI and other excise duties in each of the last three years. Because of limited scope for catching-up increases failure to revalorise now could jeopardise chances of maintaining the real value over future period of years.

(ii) Duty is mildly progressive.

(iii) Industry will have benefited from substantial boost to cash flow from duty deferment to be implemented from 15 February.

(iv) Health and social policy implications argue for at least revalorisation.

---

* Despite the introduction of duty deferment in February 1983, the revenue effects in 1983-84 of any duty increase will be virtually identical with full year effects.

Against

(i) High sensitivity of demand for spirits to price changes and high tax content in price inevitably limits scope for additional revenue from this duty. Any increase in real terms could damage the UK industry at low point in cycle.

(ii) Spirits clearances in 1981-82 fell by about 10% compared with 1980-81, following 11% fall in previous year.

(iii) Major export industry affected by world recession (over 80% of whisky production ultimately exported); volume of exports has fallen gradually in recent years, on average by about 4 per cent a year. Industry is known to be running down its stocks (whisky takes a minimum of three years to mature) and is currently working at slightly less than one-half of its distilling capacity and about two-thirds of its bottling capacity.

(iv) Any duty increase much beyond revalorisation could add disproportionately to RPI impact of Budget package.

Comment

(i) Taxable capacity limited. Duty increased by less than revalorisation last year because of representations made to the Chancellor about the state of the Scotch whisky industry. Any decision not to give similarly favourable treatment this year would need to be defended, probably on the grounds that the low rate of inflation makes revalorisation easier to stand.

(ii) Each 10p increase beyond revalorisation could reduce consumption by about 1%, and vice versa.

(iii) As from 1 April 1983 duty will become payable on the contents of a bottle of spirits as labelled and not (as at present) often on a slightly lower actual quantity (within an accepted administrative tolerance). This will add about 2½p - 3p tax to the cost of a bottle. (It should be feasible if desired to increase the duty by, say, about 5.4% (27p) but still refer to an increase of about 30p per bottle thus making an "allowance" for the 2½p - 3p increase. However, duty deferment must be worth more than 4p per bottle to the industry, and it is for consideration whether this should be deemed to provide adequate compensation.)

TOBACCO PRODUCTS DUTY

	Typical price effect pence per 20 K.S. (VAT inclusive)	Increase in specific duty %	Increase in total tax (incl ad valorem) since post 1982 Budget %	Revenue full year* £m	RPI impact effect %
Revalorisation	3.4	5.4	6.2	110	0.15
Rounded	3	4.8	5.7	100	over 0.1
price	3½	5.6	6.4	115	0.15
changes	4	6.4	7.0	130	0.15

Typical current recommended price: 106p for 20 king size (but discounts of up to 7p readily available)

Arguments

For

(i) Revalorisation of 4p should leave total consumption in 1983-84 at broadly its 1982-83 level.

(ii) Despite increases in recent years real value of duty on king-size cigarettes remains well below Labour Government peak of 1975.

(iii) Government health policy points to at least a 4p price increase as a sensible rounding equivalent to revalorisation.

(iv) Traditionally low price elasticity of demand; trade have argued that the elasticity has risen in recent years, but no firm evidence to support this.

Against

(i) Relatively heavy RPI effect.

* 1983-84 revenue will be about £5 million less in each case.

(ii) Consumption is thought to have fallen by about 8% in 1981 compared with 1980 and a further fall, possibly of the order of 3% - 4%, is expected in 1982. Provisional estimates suggest that any Budget increase beyond revalorisation could lead to a further fall in consumption.

(iii) High proportion of manufacture of tobacco products in areas of high unemployment (about 15% of jobs in the industry are sited in Northern Ireland and about another 35% in assisted areas). The industry has had total job losses of around 3,500 over the last two years (although this can only be partly ascribed to duty changes). Imperial Tobacco have announced a phased programme of closures and redundancies for 1983 and 1984, affecting about 1700 jobs in factories to be closed at Stirling, Glasgow and Bristol; but some of these jobs are likely to be transferred to other factories.

(iv) Duty increased three times in last two years. 5p price change resulting from March 1982 Budget less than full revalorisation, but that decision took account of double increase in 1981 - in March Budget (14p price increase) and in July derv duty recoupment exercise (3p). Industry could be hard hit by any increase going beyond revalorisation.

<u>Comment</u>

(i) DoI Ministers have commented on the TAC Budget representations this year that they attach much greater priority to their own proposals for the 1983 Budget (which make no mention of tobacco).

(ii) This year, as in each of last three years, the industry has increased factor prices shortly before the Budget. In 1982 there were two increases: 2p before the Budget and 2p more in the summer. The industry has just applied a further 2p increase, in the second half of January 1983.

PETROL DUTY

	Typical price effect incl VAT (p. per gallon)	Duty increase %	Revenue 1983-84 and full year £m	RPI impact effect %
Revalorisation	4.4	5.4	205	over 0.1
Rounded price changes	4	4.9	190	0.1
	4½	5.5	210	over 0.1
	5	6.1	235	over 0.1
	6	7.3	280	0.15

Typical current price (London) = £1.69 a gallon

Arguments

For

(i) Relatively low impact on RPI per £ million revenue.

(ii) Low price elasticity of demand - a buoyant revenue raiser. In terms of taxable capacity could certainly stand at least revalorisation.

(iii) UK price low by EC standards (differences exacerbated by recent exchange rate movements).

(iv) March 1982 Budget left total tax in price (duty plus VAT) still below June 1970 level (when higher in real terms than subsequently under Labour). Revalorisation would repeat this effect.

(v) Current position in OPEC suggests that crude prices should not rise for some time.

(vi) Energy conservation.

Against

(i) Any increase beyond revalorisation likely to provoke opposition from Conservative backbenchers representing rural constituencies.

(ii) About a third of increase falls on business costs (but includes unquantifiable element attributable to private motoring on business account). However, VAT blocking of petrol has been ruled out for 1983.

Comment

(i) Since 1982 Budget petrol prices net of tax have increased (erratically) rather faster than inflation. However, the oil companies continue to sell petrol at a loss in the face of competitive pressures. In recent months their repeated attempts to increase prices have failed to stick, and most urban garages are currently being given subsidies equivalent to 10p - 15p per gallon off the economic price. Prices remain higher in rural garages, which do not have the same high-volume of turnover, and in the highlands and islands.

(ii) Effect of revalorisation or a modest real increase should still leave typical UK price well below those of most other EC countries (subject to exchange rate fluctuations).

DERV

	Typical price effect incl VAT (p. per gallon)	Duty increase %	Revenue 1983-84 and full year £m	RPI impact effect %
Revalori-sation	3.7	5.4	50	nil
Rounded	3	4.3	40	nil
price	3½	5.1	45	nil
changes	4	5.8	50	nil

Typical current retail price: £1.73 a gallon
(but see comment (i) below)

Arguments

For

(i) No impact effect on RPI.

(ii) Low price elasticity of demand encourages at least revalorisation.

(iii) Despite real increases in recent years value of duty in real terms has remained substantially below that of its June 1970 level (when higher in real terms than subsequently under Labour). Scope for catching-up increase limited (see below), but revalorisation could certainly be absorbed.

(iv) Revalorisation would contribute to transport policy objective of ensuring that all classes of road user cover their road track costs, and so avoid added burden on VED.

(v) Energy conservation.

Against

(i) Virtually whole burden of derv duty increase falls on businesses. Difficult to justify real increase to business sector.

(ii) UK derv duty and derv prices still highest in EC, although certain Member States impose higher VED on diesel-engined vehicles to equalise tax burden.

(iii) DoI officials have represented that UK truck manufacturing industry is in a poor state and would benefit from no change in derv duty this year.

Comment

(i) Typical retail prices fluctuated in the range of 158p - 165p for most of 1982, but increased sharply towards the end of the year. Most derv is, however, purchased by businesses under contractual arrangements which typically provide for discounts of up to 15p a gallon off the retail price. Business users can, of course, normally recover VAT on their purchases.

(ii) For illustrative package-making purposes we have assumed that the petrol/derv tax differential will be maintained in real terms, as in the 1982 Budget. The Secretary of State for Transport attaches importance to revalorisation as the starting point this year. On the other hand, DoI officials have indicated that the differential is unlikely to be a point of particular concern to their Ministers this year. While recognising the wider arguments for revalorisation, they would see a case for no change in derv duty this year.

VEHICLE EXCISE DUTY (CARS AND LIGHT VANS)

	Licence increase	Duty increase	Revenue 1983-84 and full year	RPI impact effect
	£	%	£m	%
Revalorisation	4.3	5.4	75	0.05
	4	5.0	70	0.05
Rounded price changes	5	6.25	90	0.05

Arguments

For

(i) Relatively low RPI impact effect per £m revenue.

(ii) By March 1983 real value of the duty on cars will be about 22% below Labour Government peak of 1975.

(iii) Marginally less burdensome for high mileage rural and business motorists than petrol taxation.

Against

(i) About 33% of total tax borne by business. It is estimated that in 1982/83 light vans will contribute £110 million (8%) towards the total, and cars £1,270 million (92%).

(ii) Cars and light vans cover three or more times their road track costs.

(iii) Energy and transport policy arguments point to concentration on fuel taxes. Also, given the fluctuations in petrol prices an increase in petrol duty might be less noticeable than a VED increase.

Comment

(i) VED on cars has been increased by £10 in each of last 3 years.

(ii) The VED rate for light vans was reduced last year to the same level as cars (£80). It would not now be desirable to treat them separately again, and a real increase in the duty would add to business costs, particularly in the small business sector which is a major user of light vans.

(iii) The equivalent of a £5 VED increase on cars and light vans would be about 1½p increase in petrol prices. The average rural motorist would pay little more per year if petrol prices rather than VED were increased.

ANNEX 3

TAXATION OF TOBACCO AND ALCOHOLIC DRINKS

Introduction

1. Customs and Excise convened an inter-departmental meeting of officials to discuss, as in previous years, the taxation of both tobacco products and alcoholic drinks. The report below summarises the views expressed by the Department of Health and Social Security, Department of Industry and Ministry of Agriculture, Fisheries and Food at the meeting on 23 December 1982 at which the official Treasury was also represented.

2. Apart from the views of DoI Ministers recorded in para 4 below, all views expressed in discussion were those of officials. In most cases Departmental Ministers were likely to write formally to the Chancellor of the Exchequer before the Budget.

A. TOBACCO PRODUCTS

(i) The levels of duty

3. DHSS said that their views remained essentially the same as those expressed at the previous meeting. All forms of smoking were bad for health, but about 40% of the population continued to smoke. Health Ministers' policy was still to discourage people from smoking, and they remained in no doubt that price was the most important factor affecting consumption. DHSS had welcomed the Chancellor's reference in his 1982 Budget Speech to the "sensible presumption", that the excise duties should be revalorised annually so as to maintain their real value. They supported the view of the Treasury and Civil Service Committee in its report on Budgetary Reform that maintenance of real values of duty should be presented as far as possible as a neutral tax change rather than a tax increase.

4. DoI drew attention to the continuing decline in consumption and in levels of employment in the tobacco industry, which had accelerated following the heavy duty increases imposed in 1981. Taken in isolation, this might point towards a tax standstill. It was, however, not possible to look at these factors in isolation from other arguments, and their Secretary of State had

taken the view that he must give greater priority to the other Budgetary matters discussed in his letter to the Chancellor of 6 December and not press for specially favourable treatment for tobacco, at least in the case of cigarettes.

(ii) Relative tax burdens

5. DHSS said that the health case against hand-rolled cigarettes was the same as that against manufactured cigarettes. Pipes and cigars were as dangerous as cigarettes only if inhaled. Their Secretary of State had said last year that he would not be unduly concerned if duty levels remained unchanged for pipe tobacco and cigars.

6. DoI said they thought there was a reasonable case for special treatment for the minor products, in particular pipe tobacco and cigars.

B. ALCOHOLIC DRINKS

(i) The levels of duty

7. As in the case of tobacco, DHSS said that their views remained unchanged from last year: the health and social implications of drinking were important and, since alcohol misuse was related to cost, it was undesirable that the real cost of alcohol should be allowed to fall. Over the last year the pressure for action on alcohol misuse had grown more vocal. They noted with approval, therefore, the Chancellor's reference in his last Budget Speech to the "sensible presumption" that the specific duties on alcoholic drinks would be increased in line with the general movement of prices and hoped that he would continue with this policy in 1983.

8. Customs and Excise noted that the CPRS had been unable to attend the meeting, but they had said that their views remained unchanged from last year when they had urged that the duties should be increased so as to maintain their real value.

9. MAFF pointed out that there was no agreed Government policy in favour of determining the level of alcohol consumption by means of taxation. It would be wrong to deal with the small number of

problem drinkers by penalising the large majority of moderate drinkers. Sales of beer, spirits and fortified wines were falling, and although some companies were maintaining their profitability, this was achieved partly through reducing employment. The problem was particularly severe among distilleries in Scotland. Moreover, spirits depended in part on a strong home base to compete effectively in foreign markets. MAFF did not accept the case for maintaining the current real values of duties but, if increases were unavoidable, they would prefer modest, regular increases to occasional, substantial jumps.

(ii) Relative tax burdens

10. The two drinks currently enjoying buoyant markets were table wine and cider. The duty on table wine was constrained pending the outcome of the wine/beer infraction proceedings. In discussion of the level of the duty on cider, Customs and Excise said that the Brewers' Society had complained to Treasury officials about unfair competition from cider and might develop this in their formal Budget representations to the Chancellor. In 1976 the level of duty on cider had been set at 50% of that on the weakest beers. It was now only 40%. MAFF said that it was necessary to remember that the initial imposition of the duty had had an adverse effect on the industry in 1976. Nevertheless, MAFF's initial reaction was to recognise that there could be a case for imposing the same absolute level of duty increase on both beer and cider this year. In relation to made-wine MAFF argued that any decision about the relative level of the duty should not be influenced by the prospect of defeat in the European Court for discriminating in favour of made-wine against wine. It would not be in the industry's interests to repeat the reduction made in the last Budget in the relativity between wine and made-wine. DHSS said that there were no health arguments justifying preferential rates of tax on cider or made-wine.

Board Room
H M Customs and Excise
King's Beam House
Mark Lane London EC3R 7HE

C. PA1.28.1

For separate discussion 2

Suggest — ie not included on the overview"

From: Sir Douglas Lovelock

Date: 24 January 1983

CHANCELLOR OF THE EXCHEQUER

cc: Chief Secretary
Financial Secretary
Economic Secretary
Minister of State(C)
Minister of State(R)
Sir Douglas Wass
Mr Burns
Mr Middleton
Mr Byatt
Mr Moore
Mr Kemp
Mr Cassell
Mr Griffiths
Mr Hall
Mr Ridley
Mr French
Mr Harris
Sir L Airey

BUDGET 1983: EXCISE DUTY OPTIONS

This paper deals with the main excise duty options for this year's Budget. Its form and layout is the same as that adopted for the last few years. Our starting point has been what you described in your Budget Statement last year as the "sensible presumption" (used as a conventional assumption in the NIF for some years) that the specific duties will be increased broadly in line with the rate of inflation in the previous calendar year. I understand that at the recent Chevening weekend you expressed the preliminary view that you would wish to go for something on these lines. As you know, the rate of inflation in the calendar year 1982 has now been announced, via the December RPI, as 5.4%.

Internal circulation: Mr Fraser, Mr Freedman, Mr Howard, Mr Middleton, Mr Jenkins, Mr Packman, Mr McGuigan, Mr Battle, Mr Smith, Mr de Berker, CPS

2. A revalorisation package, subject to sensible roundings of price changes, is illustrated in Annex 1. (All revenue figures in the Annexes include consequential VAT). It would yield additional revenue of about £590 million in 1983-84 and about £600 million in a full year, for an RPI impact effect of about 0.5%. Given the roundings, all duty increases lie in the range of 5%-6.25%. Annex 2 deals with each major duty in greater detail. It shows the effect of strict, unrounded revalorisation in line with the 5.4% increase in the RPI and tabulates illustrative rounded price changes including, where practicable, not only the price change shown in Annex 1 but possible alternatives on either side. It then lists the main arguments relating to each duty together with other relevant facts. A note of an inter-Departmental meeting we held with officials of the sponsoring Departments and DHSS about alcoholic drinks and tobacco is attached at Annex 3. In most cases the Ministers concerned are likely to write formally to you with their views.

3. Annexes 1 and 2 have been drafted without prejudice to the outcome of the inter-Departmental exercise in which officials are examining the case for abolishing or reducing car tax and possible recoupment of the cost from other taxes on motoring; a report on this will be made at about the end of the month. Separate submissions will also be made about consequential increases for tobacco products other than cigarettes and for minor alcoholic drinks and about rebated oils,, avgas etc and matches and mechanical lighters. Betting and gaming is the subject of a separate series of papers.

4. So far as VED is concerned, this paper (which incorporates the views of the official Treasury, who have the policy responsibility in this area) deals only with the rates on cars and light vans. Following the restructuring in last year's Finance Act, different considerations apply to VED on goods vehicles. The Secretary of State for Transport wrote to you recently suggesting a package of

measures to bring the taxation of heavy lorries more closely into line with road costs, and FP will be making a separate submission on this.

TAXABLE CAPACITY

5. In terms of taxable capacity, it is hard to identify any excise duty which could not bear revalorisation this year. Although a number of the excise duty industries have been experiencing a difficult time in the recession, the interim NIF suggests that revalorisation should not cause a volume fall in 1983-84. This reflects partly the forecast modest recovery in consumers' real expenditure, which would lead to more substantial increases if real prices were allowed to fall. The position is illustrated in the following table:-

	Approximate volume growth if no duty changes (ie real value allowed to fall)	Approximate volume change due to revalorisation	Overall approximate volume change 1983-84 compared with 1982-83 given revalorisation
	(%)	(%)	(%)
Beer	+1½	-½	+1
Spirits	+4½	-3	+1½
Wine	+7	-1½	+5½
Tobacco	+1½	-1½	0
Petrol	+4	-½	+3½
Derv	+4	-½	+3½

These volume changes can only be treated as broad orders of magnitude. The figures for beer are particularly uncertain, since the present equation does not account satisfactorily for the consumption pattern of recent years. It seems best to regard the net effect on beer consumption as broadly neutral. Otherwise, you will see

that the effect on the volume of tobacco consumption, where there is in any a case a long-term secular trend (taken account of in the table above) against smoking of the order of 1%-2% a year, would also be broadly neutral; but in the other cases, we would expect slight increases in consumption even with revalorisation.

6. Other considerations relating to each duty are detailed in Annex 2. These should assist you in deciding whether to go beyond, or to temper, the effects of revalorisation in each particular case, but there are certain key points which it may be helpful to summarise at this stage. In the field of alcoholic drinks and tobacco, these are as follows:-

(a) Beer Revalorisation would add approximately 0.9p, including VAT, to the cost of a typical pint. There appears to be no satisfactory alternative to 1p (5.9%) as the rounded price change since ½p (2.9%) and 1½p (8.8%) would represent either only about one-half or rather more than one-and-a-half times revalorisation respectively. In our view beer could comfortably stand 1p (on a typical price of 60p per pint it seems almost inconsequential), but if there were to be any question of a larger increase you will wish to bear in mind that the Brewers' Society have lobbied strongly against a real increase in the light of the substantial falls in consumption and output over the last three years. We also believe they would be likely to react much more vigorously this year than in the past if there should be further discrimination in the treatment of beer compared with spirits.

(b) Wine. Table wine is by far the most buoyant of all the excise duty goods in consumption terms and, in principle, is a candidate for a real increase. However, although they will not be concluded in time for the Budget,

the infraction proceedings in the European Court concerning our wine/beer ratio are now at an advanced stage, and any attempt to single out wine ahead of beer would be highly provocative. We therefore recommend identical increases in percentage terms on wine and beer this year. This means about 5½p on a 75cl bottle of table wine for 1p on beer.

(c) Spirits. The implication of the brewers' argument is that same percentage increase should be applied to spirits as to beer. Applied to the hilt, this would mean about 30p on a bottle of spirits - marginally more than strict revalorisation (27p) - for 1p on beer. On the other hand, the spirits industry is still in a fairly poor state, and MAFF officials have represented to us that the case for restraint on taxation of spirits is even greater than that for beer because of the unemployment factor in Scotland; hence they would be prepared to contemplate a further modest narrowing of the gap between spirits and beer. On balance, we think it would be justifiable to revalorise the duty on spirits this year, but the industrial considerations could point to a small element of shading down, to 25p (5%) as the rounded price change.

(d) Tobacco. The tobacco industry has suffered substantial falls in consumption, output and employment over the past two years, partly as a result of the significant real duty increases in 1981. Industrial considerations therefore argue against a real increase this year. On the other hand, the tobacco health lobby remains strong and we believe that, despite their calls for a standstill this year, the industry could stand revalorisation (3½p). (You will want to consider 4p, I think, but the rise is then as much as 6.4%). The use of a halfpenny in the price increase would be unusual but we would expect

manufacturers to adjust the prices of some brands by 3p and others by 4p.

7. As far as the motoring taxes are concerned, leaving aside any suggestions which emerge from the inter-Departmental review, the main points are:-

(a) Petrol. Petrol consumption is buoyant, assisted by the continued strong competition among the oil companies which has led to lower prices in the face of the general glut in the oil market. UK prices are now noticeably low by European Community standards. The duty could certainly stand revalorisation ($4\frac{1}{2}$p) and, while we are conscious of the Conservative backbench concern about the impact of duty increases on rural motorists, the general weight of argument suggests that it would probably be the prime candidate if selective real duty increases were required.

(b) Derv. You have yourself commented (Miss Rutter's undated minute received on 22 December) that this should be considered separately from petrol for industrial as well as environmental reasons, and we believe that the potential effect on business costs probably rules out a real increase this year. On the other hand, the Secretary of State for Transport has drawn attention to the importance of revalorising the derv duty in the context of the policy on heavy lorries. We would not recommend going beyond revalorisation (3.7p) and suggest that there could be a marginal shading down to $3\frac{1}{2}$p (5%) as the rounded price change.

(c) VED. It has been customary to fix the rate of duty in multiples of £5, which is marginally more convenient for the Department of Transport and their agents. Revalorisation of 5.4% on the present £80 licence would

strictly amount to £4.32. FP have discussed with DTp officials and established that a rounding to either £4 (5%) or the more conventional £5 (6.25%) is likely to be acceptable. For the present we have shown £5 in Annex 1 on revenue grounds, but there is a clear choice to be made here.

NEXT STEPS

8. You will wish to decide in the light of this submission and your approach to the Budget judgment whether to go for an across the board revalorisation package or whether to act more selectively. If in the latter event you can give us some indication of your thinking, we should be glad to provide further packages with appropriate weightings. Our deadlines for decisions are 18 February for decisions on structural changes, if any, and 25 February for rate changes.

DM

DOUGLAS LOVELOCK

ANNEX 1

REVALORISATION PACKAGE (SUBJECT TO SENSIBLE ROUNDING)

	Typical price change (a)	Specific duty increase %	Revenue full year (b) £m	RPI impact effect %
Beer	1 pence/pint (b)	5.9	90	0.1
Wine	5½ pence/75 cl light wine	5.9	25	neg
Spirits	25 pence/bottle	5.0	25	0.05
Tobacco	3½ pence/20 KS	5.6	115	0.15
Petrol	4½ pence/gallon	5.5	210	0.1
Derv	3½ pence/gallon	5.0	45	nil
VED	£5 car licence	6.25	90 (c)	0.05
			600	0.5 (d)

NOTES

(a) Price effect includes VAT except for VED.

(b) For a 15 March Budget first and full year revenue will be identical except for beer and tobacco where the first year revenue will be about £5 million less in each case.

(c) VED increases on heavy lorries, as proposed by the Secretary of State for Transport, would produce up to £20 million more without adding to the RPI impact effect.

(d) RPI effects do not sum because of rounding.

ANNEX 2

BEER DUTY

	Typical price effect pence per pint (VAT inclusive)	Duty increase %	Revenue* full year £m	RPI impact effect %
Revalori-sation	0.9	5.4	80	less than 0.1
Rounded price change	1	5.9	90	less than 0.1

Typical current price: 60p per pint (on-licence price for non-premium bitter in a public bar)

Arguments

For

(i) Relatively low RPI effect per £m revenue.

(ii) Low price elasticity of demand. Traditionally a buoyant revenue-raiser, albeit a little less so in last three years. The biggest potential revenue-raiser in the drinks field. Should stand at least revalorisation.

(iii) March 1982 Budget broadly maintained duty in real terms at about Labour Government peak of 1975-76. Revalorisation would repeat this effect.

(iv) Health and social policy implications argue for at least revalorisation.

Against

(i) Production of beer fallen by 3% comparing the twelve months ended November 1982 with same period in 1981, on top of falls of about 4% and 5% in the previous two years. Previously the industry had enjoyed a steady expansion of 2% a year. Industry likely to be strongly opposed to any increase beyond sensibly rounded revalorisation.

---

* 1983-84 revenue will be about £5 million less than that for a full year.

(ii) Beer duty has increased in real terms under present Government. Brewers have blamed this for fall in consumption (although see comment (i) below). Could prove controversial to impose a real increaze this year.

(iii) The brewers have contrasted treatment of beer with more lenient treatment of spirits (although this reflects judgments as to respective taxable capacity, and substitutability is doubtful). Would be controversial to single out beer again ahead of spirits this year.

(iv) Presentational difficulty that duty is still widely regarded as regressive ("working man's pint") although recent analysis of FES data suggests neutral or only mildly regressive.

Comment

(i) Recent decline in consumption followed steady gentle expansion since the 1950s although the brewers had been concerned that the rate of growth was low by the standards of other drinks. Future of beer consumption now uncertain; but the decline probably due not so much to duty increases (pace the brewers) as to depth of recession and fall in consumers' real expenditure on drink and tobacco. Revalorisation would probably leave total consumption in 1983-84 at about its 1982-83 level.

(ii) The wine/beer infraction proceedings are currently before the European Court, and will need to be taken into account.

(iii) Because of relatively low weight of tax in price, increases in beer taxation represent only small addition to total price - for example, 1p rounded revalorisation would increase price of typical pint by less than 2%.

(iv) The Brewers Society have complained about unfair competition from cider which enjoys a duty rate of only 40% of that on the weakest beers. We agree that the cider industry is in a healthy state, benefiting from increased consumption (in contrast to beer), and that there is a strong case for a real increase in duty this year. This will be examined in detail in a separate submission.

WINE DUTY

	Typical price effect pence per 75 cl bottle of table wine (off-licence, VAT inclusive)	Duty increase %	Revenue 1983-84 and full year £m	RPI impact effect %
Revalorisation	5.0	5.4	25	neg
Rounded price change	5½	5.9*	25	neg

Arguments

For

(i) Relatively low RPI effect.

(ii) Consumption of table wine buoyant. Clearances currently much higher than in previous year.

(iii) Value of duty has fallen substantially in real terms from Labour Government peak of 1975. Considerable scope in principle for catching-up increases, but duty changes on table wine should not exceed those for beer (see below).

(iv) Duty is mildly progressive.

(v) Product largely imported.

(vi) Wine trade will have benefited from substantial boost to cash flow from duty deferment to be implemented from 15 February.

(vii) Health and social policy implications argue for at least revalorisation.

* Identical to beer. The legal duty rate will be determined by need not to increase wine/beer duty ratio.

Against

(i) Wine/beer infraction proceedings currently before European Court. Important not to increase duty ratio as between the two products. Effectively limits increase on wine to about 5½p for every 1p on beer.

(ii) Consumption of fortified wine falling. Clearances have continued to decline gradually from peak in 1979-80.

Comment

(i) Assuming that the duty on fortified wine is increased pro-rata to the duty on table wine, the price of a bottle of sherry will increase by 1.3p for each 1p on table wine.

(ii) Revenue estimates are based on the assumption that existing relativities will be maintained between different types of wine.

Against

(i) High sensitivity of demand for spirits to price changes and high tax content in price inevitably limits scope for additional revenue from this duty. Any increase in real terms could damage the UK industry at low point in cycle.

(ii) Spirits clearances in 1981-82 fell by about 10% compared with 1980-81, following 11% fall in previous year.

(iii) Major export industry affected by world recession (over 80% of whisky production ultimately exported); volume of exports has fallen gradually in recent years, on average by about 4 per cent a year. Industry is known to be running down its stocks (whisky takes a minimum of three years to mature) and is currently working at slightly less than one-half of its distilling capacity and about two-thirds of its bottling capacity.

(iv) Any duty increase much beyond revalorisation could add disproportionately to RPI impact of Budget package.

Comment

(i) Taxable capacity limited. Duty increased by less than revalorisation last year because of representations made to the Chancellor about the state of the Scotch whisky industry. Any decision not to give similarly favourable treatment this year would need to be defended, probably on the grounds that the low rate of inflation makes revalorisation easier to stand.

(ii) Each 10p increase beyond revalorisation could reduce consumption by about 1%, and vice versa.

(iii) As from 1 April 1983 duty will become payable on the contents of a bottle of spirits as labelled and not (as at present) often on a slightly lower actual quantity (within an accepted administrative tolerance). This will add about 2½p - 3p tax to the cost of a bottle. (It should be feasible if desired to increase the duty by, say, about 5.4% (27p) but still refer to an increase of about 30p per bottle thus making an "allowance" for the 2½p - 3p increase. However, duty deferment must be worth more than 4p per bottle to the industry, and it is for consideration whether this should be deemed to provide adequate compensation.)

TOBACCO PRODUCTS DUTY

	Typical price effect pence per 20 K.S. (VAT) inclusive)	Increase in specific duty %	Increase in total tax (incl ad valorem) since post 1982 Budget %	Revenue full year* £m	RPI impact effect %
Revalorisation	3.4	5.4	6.2	110	0.15
Rounded	3	4.8	5.7	100	over 0.1
price	3½	5.6	6.4	115	0.15
changes	4	6.4	7.0	130	0.15

Typical current recommended price: 106p for 20 king size (but discounts of up to 7p readily available)

Arguments

For

(i) Revalorisation of 4p should leave total consumption in 1983-84 at broadly its 1982-83 level.

(ii) Despite increases in recent years real value of duty on king-size cigarettes remains well below Labour Government peak of 1975.

(iii) Government health policy points to at least a 4p price increase as a sensible rounding equivalent to revalorisation.

(iv) Traditionally low price elasticity of demand; trade have argued that the elasticity has risen in recent years, but no firm evidence to support this.

Against

(i) Relatively heavy RPI effect.

* 1983-84 revenue will be about £5 million less in each case.

(ii) Consumption is thought to have fallen by about 8% in 1981 compared with 1980 and a further fall, possibly of the order of 3% - 4%, is expected in 1982. Provisional estimates suggest that any Budget increase beyond revalorisation could lead to a further fall in consumption.

(iii) High proportion of manufacture of tobacco products in areas of high unemployment (about 15% of jobs in the industry are sited in Northern Ireland and about another 35% in assisted areas). The industry has had total job losses of around 3,500 over the last two years (although this can only be partly ascribed to duty changes). Imperial Tobacco have announced a phased programme of closures and redundancies for 1983 and 1984, affecting about 1700 jobs in factories to be closed at Stirling, Glasgow and Bristol; but some of these jobs are likely to be transferred to other factories.

(iv) Duty increased three times in last two years. 5p price change resulting from March 1982 Budget less than full revalorisation, but that decision took account of double increase in 1981 - in March Budget (14p price increase) and in July derv duty recoupment exercise (3p). Industry could be hard hit by any increase going beyond revalorisation.

<u>Comment</u>

(i) DoI Ministers have commented on the TAC Budget representations this year that they attach much greater priority to their own proposals for the 1983 Budget (which make no mention of tobacco).

(ii) This year, as in each of last three years, the industry has increased factor prices shortly before the Budget. In 1982 there were two increases: 2p before the Budget and 2p more in the summer. The industry has just applied a further 2p increase, in the second half of January 1983.

PETROL DUTY

	Typical price effect incl VAT (p. per gallon)	Duty increase %	Revenue 1983-84 and full year £m	RPI impact effect %
Revalori-sation	4.4	5.4	205	over 0.1
Rounded price changes	4	4.9	190	0.1
	4½	5.5	210	over 0.1
	5	6.1	235	over 0.1
	6	7.3	280	0.15

Typical current price (London) = £1.69 a gallon

Arguments

For

(i) Relatively low impact on RPI per £ million revenue.

(ii) Low price elasticity of demand - a buoyant revenue raiser. In terms of taxable capacity could certainly stand at least revalorisation.

(iii) UK price low by EC standards (differences exacerbated by recent exchange rate movements).

(iv) March 1982 Budget left total tax in price (duty plus VAT) still below June 1970 level (when higher in real terms than subsequently under Labour). Revalorisation would repeat this effect.

(v) Current position in OPEC suggests that crude prices should not rise for some time.

(vi) Energy conservation.

Against

(i) Any increase beyond revalorisation likely to provoke opposition from Conservative backbenchers representing rural constituencies.

ıat UK truck manufacturing industry
ɛfit from no change in derv duty

in the range of 158p - 165p for
ɔly towards the end of the year.
' by businesses under contractual
/ide for discounts of up to 15p a
siness users can, of course,
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.cular concern to their Ministers
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(ii) Relative tax burdens

10. The two drinks currently enjoying buoyant markets were table wine and cider. The duty on table wine was constrained pending the outcome of the wine/beer infraction proceedings. In discussion of the level of the duty on cider, Customs and Excise said that the Brewers' Society had complained to Treasury officials about unfair competition from cider and might develop this in their formal Budget representations to the Chancellor. In 1976 the level of duty on cider had been set at 50% of that on the weakest beers. It was now only 40%. MAFF said that it was necessary to remember that the initial imposition of the duty had had an adverse effect on the industry in 1976. Nevertheless, MAFF's initial reaction was to recognise that there could be a case for imposing the same absolute level of duty increase on both beer and cider this year. In relation to made-wine MAFF argued that any decision about the relative level of the duty should not be influenced by the prospect of defeat in the European Court for discriminating in favour of made-wine against wine. It would not be in the industry's interests to repeat the reduction made in the last Budget in the relativity between wine and made-wine. DHSS said that there were no health arguments justifying preferential rates of tax on cider or made-wine.

CONFIDENTIAL

FROM: A M W BATTISHILL
INLAND REVENUE
POLICY DIVISION
SOMERSET HOUSE

26 January 1983

1. MR GREEN 26/1
2. CHANCELLOR OF THE EXCHEQUER

CORPORATION TAX RATES

1. During the course of the Chevening discussions you indicated that you were attracted to the possibility of reducing the main corporation tax rate in the 1983 Budget by a couple of points from 52% to 50%. You asked us to look at the various Budget representations from industry to see what support they contained for this. We have also looked back at the responses to the Green Paper on Corporation Tax to see what was said about the burden of corporation tax.

Main corporation tax rate

2. To summarise briefly, the arguments in favour of cutting the corporation tax rate are that it:

a. would help those companies still paying tax despite current difficulties;

b. would be broadly neutral as between types of activity and types of company (unlike for example changes in capital allowances);

---

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State (R)
Minister of State (C)
Sir Douglas Wass
Mr Middleton
Mr Kemp
Mr Moore
Mr Robson
Mr French
Mr Ridley
Sir Lawrance Airey
Mr Green
Mr Lawrance
Mr Battishill
Mr Painter
Mr McConnachie
Mr Prescott
Mr Jones
PS/IR

c. would have a marginally helpful effect in reducing the relative attractiveness of debt rather than equity financing, whilst leaving the broad structure of investment incentives unchanged;

d. would be good for confidence and would reduce the one remaining major tax rate on income which still stands at the same level as when the Government came into office in 1979; and

e. would fit well with a statement in the Budget, as part of the response to the Green Paper, confirming that the existing corporation tax structure would remain unchanged (see separate note on Corporation Tax Green Paper to the Minister of State (R)).

The cost of cutting the corporation tax rate to 50% would be £m130 in 1983-84 and £m230 in a full year.

Burden of representations

3. As you thought, there is only limited support for a cut in the corporation tax rate in the main Budget representations this year. The CBI do not mention the rate of tax as such; nor do the ABCC. But those which do comment on the burden of the tax would like to see the rate reduced. It is the Institute of Directors who press this most strongly. As they say:

> "A rate of 52% is historically and absolutely high and especially anomalous at a time when a large proportion of companies are fiscally exhausted and not paying mainstream corporation tax or perhaps even advance corporation tax at all".

They want the rate reduced to 50% and further reductions in the longer term, particularly if the basic rate of income tax were reduced below 30%.

The Corporation Tax Green Paper was of course concerned with e structure and not the burden of the tax. Nevertheless the CBI their detailed response to the Green Paper, did make some complain bout the burden of the tax. Although in the end they came down in favour of reducing other business costs they did not rule out, give that profitability was so depressed, retaining the present structur of corporation tax and reducing the rate. Furthermore, many of the detailed suggestions, which they pick up in their Budget representations, are very much concerned with alleviating the substantive burden of corporation tax. A cut in the rate might take some of the sting out of these complaints - particularly if combined with some relief on ACT.

<u>Small companies' rate</u>

5. If the main corporation tax rate were to be cut from 52% to 50%, you will want to consider what if anything should be done about small companies. The small companies' rate of 40% applies to companies with profits below £90,000 with marginal relief on profits up to £225,000. Strictly speaking, it is a preferential rate on small <u>profits</u> rather than on small <u>companies</u>. Marginal relief is given by charging profits in the band between £90,000 and £225,000 at 60%; the effect of this is gradually to withdraw the benefit of the small companies' rate on the first slice of profits. The marginal relief runs out completely at profits of £225,000 and companies with profits above this level pay corporation tax at 52% on their total profits.

6. The great majority of companies currently still paying corporation tax do so at the small companies' rate of 40% or are in the marginal band; but the 5% or so of companies which pay tax at the full rate of 52% include many of the large household names.

7. At Chevening I believe your inclination was to leave the small companies' rate at 40% even if the 52% rate were to be reduced. There are perhaps two main arguments which could point to leaving the small companies' rate unchanged:

a. the small companies' rate was in fact cut from 42% to 40% as recently as 1980 and the argument would be that the main rate was now following suit; and

b. a main corporation tax rate reduced to 50% and a small companies' rate left unchanged at 40% would provide an attractive - and readily perceived - rate structure of 30% (basic rate of income tax), 40% (small companies' rate), 50% (corporation tax rate), and 60% (top rate on earnings).

Other small companies measures

8. Against this there is the obvious difficulty of not seeming to help the smallest companies with a rate cut this year. One answer to this may be the package of other enterprise and small business measures, including the important extensions to the business start-up scheme, which are designed to be particularly targeted at the broad range of smaller unquoted companies.

9. But there are other possibilities, including further increases in the profits levels for the small companies' rate. This would be of particular help to companies expanding out of the "small profits" range. It could also appear especially attractive if it enabled you to further reduce the 60% marginal rate, which has already come down from $66\frac{2}{3}$% in previous Budgets. As Ministers know, the marginal rate still attracts a lot of criticism from industry, because of its discouraging effect on companies wishing to expand.

10. There are various possibilities, listed in ascending order of cost (on the assumption that the main corporation tax rate is reduced to 50%):

a. As a minimum, the profits limits for the small companies' rate ought to be revalorised. And there is a case for increasing the limits by rather more than the rate of inflation so that, in round figures, the lower profits limit could rise from £90,000 to £100,000 and the upper profits limits from £225,000 to £250,000 (an increase of about 11%). The marginal rate would come down from 60% to $56\frac{2}{3}$%/ The cost of this change would be £m6 in 1983-84 and £m10 in a full year.

/(as a result of the 2% cut in the main corporation tax rate).

b. Raising the lower limit to £100,000 but the upper limit to £300,000 would bring down the marginal rate even further from 60% to 55%. It would, of course, <u>increase</u> the number of companies within the marginal band (by perhaps another 3,000), but for some 20,000 others there would be a useful 5 point reduction in their marginal rate. It would cost only a little more than option a: £m10 in 1983-84 and £m15 in a full year.

c. A third option is to make an even greater increase in the lower profits limit. This would extend the full benefit of the 40% rate to a wider range of companies. For example, we estimate that raising the limit from £90,000 to £120,000 would remove some 7,000 companies from the marginal band altogether this year. To keep the marginal rate above £120,000 at 60% would mean increasing the upper limit to £240,000. Here too the cost would be £m10 in 1983-84 and £m15 in a full year.

d. Fourthly, it would be possible to combine the advantages of b. and c. by increasing the lower profits limit to (say) £120,000 <u>and</u> reducing the marginal rate to 55%. This would require the upper profits limit to go up to £360,000. We estimate that, with these measures, some 15,000 to 20,000 companies would fall within the marginal band. The cost would be rather more substantial: £m15 in 1983-84 and £m25 in a full year.

The slice system

11. Finally, there is the possibility of moving to a "slice" system under which <u>all</u> companies would be charged at the small companies' rate on the first slice of their profits and at the full 52% rate on the rest. They would keep this benefit even when their profits rose above the small companies' limit, even though larger profits would be taxed at 52%. This would replace the present small companies' regime and has received a certain amount of support in the representations on the Green Paper including from the CBI, the ABCC and the Institute of Directors.

A simple slice system

12. One possibility would be to convert to a slice system on the basis of the present 40% rate and the first £90,000 of profits.

13. However it would probably be desirable, at very modest additional cost, to raise the limit from £90,000 to a round £100,000. With a £100,000 slice the benefit would vary according to the size of a company's profits running from nil at £90,000 of profits to a maximum of £12,000 at £225,000 of profits (the upper profits limit under the present system). As compared with a possible cut in the corporation tax rate from 52% to 50%, companies with profits up to £600,000 would do better under the slice system; those with profits above £600,000 would do less well. The cost would be of the order of £m50 in 1983-84 and £m90 in a full year, (on the assumption the 52% rate were left unchanged).

The Secretary of State for Trade's idea

14. Lord Cockfield has suggested another variant: reducing the rate on the first slice from 40% to 35%, while leaving the main corporation tax rate at 52%. This would help <u>all</u> companies paying corporation tax in some degree. It would increase the maximum benefit for any one company from £12,000 to £17,000, reached at profits of £225,000 or above. As compared with a cut in the main corporation tax rate from 52% to 50%, his scheme would:

a. give more help to companies with profits up to £850,000;

b. do something for companies with profits below £90,000: for them it is simply equivalent to a cut in the small companies' rate (at profits of £90,000, the benefit is £4,500).

The cost of this would be some £m110 in 1983-84 and up to £m200 in a full year.

15. The main argument in favour of moving over to a slice system is that it would get rid of the awkward marginal provisions. It would give some help to all companies with taxable profits of more than £90,000, and if combined with a cut in the small companies' rate, to those with profits below £90,000 as well. It would give proportionately most benefit to small and medium-sized companies, and least to the largest companies (or, strictly speaking, to those making the largest taxable profits). For companies measuring their profits in millions of pounds the benefit would be relatively small, and much less attractive than cutting the 52% rate to 50%. Because they cost about the same, Lord Cockfield's more ambitious scheme ought to be regarded as an alternative to cutting the main rate.

16. There are obvious presentational advantages in simplifying the small companies' regime, and doing away with the marginal rate altogether. But there would be a price. It would no longer be possible in future to concentrate relief particularly on companies making small profits; further reductions in the small companies' rate or increases in the profits limit would then be somewhat more expensive because they would run for all companies and not just the smaller ones. There would also be a small staff cost in tax offices. This is because even the largest companies would have their lowest slice of profits taxed at a different rate from the rest of their profits. This would interact with the other

rporation tax rules eg for allowances and reliefs; and there would be rather more work arising in particular on groups of companies. We tentatively put this at 10 to 15 staff, mainly at Inspector level.

Other matters

17. There are also structural questions to be considered in the light of responses to the Green Paper and the Government's future strategy on corporation tax generally. These have been considered in a separate submission to the Minister of State (R), and you

/a will wish to consider whether/balanced package of measures can be put together at an acceptable cost.

Oil industry

/a 18. The oil industry would be/significant beneficiary from a reduction in the main corporation tax rate (as a capital intensive industry it would get little benefit from an NIS reduction). A reduction of 2 points to 50% would, on the latest forecast, benefit oil companies as follows:

1983-84	1984-85	1985-86	1986-87
25	60	90	110

The total tax reductions for the industry would then be £m65 in 1983-84 if the APRT phasing out is not accelerated, or up to £m115 if it is. The 1984-85 reductions would be £m220, or rather less if APRT phasing out had been accelerated.

AB

A M W BATTISHILL

CABINET OFFICE
Central Policy Review Staff
70 Whitehall, London SW1A 2AS Telephone 01-233 7765

From: John Sparrow
CONFIDENTIAL

EXCHEQUER
26 JAN 1983
ACTION Mr Kemp 27.1
COPIES TO CST, FST, EST, MST C, MST R, Sir D Wass, Sir A Rawlinson, Mr Burns, Mr Bailey, Mr Middleton, Mr Moore, Mr Monger, PS/IR, Mr Traynor

Qa 06231

26 January 1983

The Rt Hon Sir Geoffrey Howe QC MP
HM Treasury
SW1

Dear Geoffrey,

1983 BUDGET

I may be helpful if I mention now three major points which emerged in our study of unemployment, and which are very relevant to your decisions on the Budget.

Our present tax system subsidises capital and taxes labour in a way which is difficult to defend in present circumstances. I therefore very much agree with Patrick Jenkin that abolition or at least further reduction of NIS should have the first call on whatever headroom you have.

If you also have scope for lower direct taxes, it would be desirable to use it to ease the problems of the unemployment trap. This means, in the first instance, that raising tax thresholds is preferable to cuts in tax rates. But an across the board increase in tax thresholds is a blunt instrument for tackling the unemployment trap. The great majority of families affected by the trap are single-earner couples, mostly with children, yet only a small part of the benefit of raising tax thresholds across the board would go to such families. Pending reform of taxation of husband and wife (which cannot under any circumstances happen for some time) one of the most effective ways of concentrating tax help on these families would be to create a new allowance for people with at least one child under 5. If it would be administratively impractical to introduce a new tax allowance for the coming Budget, a useful second-best would be to use the child benefit system to achieve a similar result.

I would also urge that, as in previous Budgets, some part of any fiscal headroom should be used for public works which meet important social and economic needs and which are also labour intensive. Such programmes have a low import content and will promote employment. They can be targetted to geographical areas of maximum difficulty. Projects which increase the supply of jobs circulating in the normal labour market are likely to have a greater effect on confidence and morale than schemes designed to occupy the unemployed. Moreover they help sustain the private construction industry.

Yours sincerely,

John.

John Sparrow

CH/EX. REF. NO B (83)3

COPY NO 3 OF 4 COPIES

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

THE 1983 BUDGET

We spoke on 20 January about the 3 February Cabinet, and I now enclose the paper which I plan to circulate. It is very similar to the one I circulated last year - C(82)1 - which produced a rather successful discussion on 28 January.

2. I am sure that we should again resist any pressure for changes in the monetary and fiscal framework which we have established. Sustaining present policy is right, both economically and politically.

3. My present thinking therefore is that:-

a. for the monetary aggregates we should, as envisaged in last year's Red Book, reduce the target range from this year's 8-12 per cent to 7-11 per cent for 1983-84. Our policy in respect of the exchange rate should remain unchanged (though in periods of weakness due to political factors, we should not allow interest rates to rise.)

b. the 1983-84 PSBR should certainly not be much higher than the estimated 1982-83 outturn, now put at £8 billion: indeed we have spoken of the case for showing a lower figure next year. We published a figure of £8 billion (2¾ per cent of GDP) for 1983-84 in the Autumn Statement. Our latest forecast (before any changes beyond revalorisation) is some £6 billion.

4. This would give us room for tax cuts of some £1.5 to £2 billion, depending on whether we in the end go for a PSBR of £7.5 or £8 billion. It is far too soon to settle this; indeed it is important to stress that we are still at an early stage: the picture, and the figures, may change a lot before 15 March. In order to retain freedom of manoeuvre, my Cabinet paper does not mention the £6 billion and £2 billion figures.

5. I should prefer that colleagues concentrate their advice on how best we should target our fiscal measures. As the draft Cabinet paper says, the fall in the exchange rate has to some extent changed the balance of claims for relief as between persons and companies. Given the fall in interest rates over the last year, and the reductions in NIS which we announced in the autumn, it could be argued that the bulk of tax reductions in March should go to raising income tax thresholds. Within a total fiscal adjustment of £2 billion, there may be scope for raising them some 8 percentage points over the Rooker-Wise revalorisation, giving around 13½ percentage points in all. This would restore allowances to roughly the same percentage of average earnings as in 1978-79.

6. But there are also strong pressures for further help for companies; and it is of course true that substantial problems of profitability and competitiveness remain. And we do want to encourage output, as well as demand. Moreover, a Budget that contained major tax reductions, but none for companies, would be out of line with what we have tried to do in recent years, and could be misconstrued as electorally-motivated.

7. I am at present inclined to helping both individuals <u>and</u> companies. Action on industrial rates is ruled out for the present largely on grounds of practicality. A further reduction in NIS, or indeed its abolition, is widely sought; and if there is room some small move - say a further half per cent reduction -

would certainly be desirable. Conceivably there may be a stronger case for a reduction in the Corporation Tax rate, from 52 per cent to, say, 50 per cent.

8. The indirect taxes ought I believe to be revalorised in line with inflation in most cases. However I shall want to look carefully at the individual components; and, as you have asked, will look in particular at the petrol and derv duties. But the real price of petrol at the pumps has in fact dropped since the last Budget, and a failure to revalorise these duties would cost some £0.25 billion.

9. I am also working on a range of possible measures to promote enterprise and small firms, to encourage wider share ownership, and to stimulate technology and innovation. I envisage further concessions on oil taxation as an encouragement to North Sea development. And I am looking again at the ceiling on mortgage interest relief.

10. The questions posed in my Cabinet paper are designed to give colleagues an opportunity to express their views on the broad strategic issues, and on the right blend of fiscal change. What we must of course avoid on 3 February is any attempt to reach precise quantified decisions: the whole picture could change sharply as a result of major oil price, or exchange rate, movements. I shall wish to keep you in the picture throughout; but I would not want to have to go back to Cabinet to seek the reversal of decisions reached too soon, too precisely, and too collectively.

11. We might perhaps discuss this, and the draft paper, at our meeting on 27 January.

(G.H.)
26 January 1983

CONFIDENTIAL

ANNEX 1

SELECTED ECONOMIC INDICATORS, 1979 TO 1983

	1979	1980	1981	1982	1983[1]
World GDP, volume (per cent change)	+3½	+1½	+1½	-1	+1 to +2
UK GDP, volume (per cent change)	+2	-2½	-2½	+½	+1½ to +2½
Domestic demand, volume (including stockbuilding) (per cent change)	+4	-3	-1½	+2½	+3 to +4
Retail prices Q4 (per cent change)	+17½	+15½	+12	+6	about 6½
Interest rates (average 3-month interbank)	14	16½	14	12½	11½ [5]
Current balance (£ billion)	-1	+3	+6	+4½	+1 to +3
Unemployment (UK, per cent, narrow, new definition)	5	6½	10	12	13 [2]

TAX AND PUBLIC EXPENDITURE 1979-80 TO 1983-84

	1979-80	1980-81	1981-82	1982-83	1983-84
Tax and NIC as percentage of GDP	36	37½	40½	40	-[4]
Public expenditure as percentage of GDP[3]	41	43	44½	44	43½
PSBR as percentage of GDP	5	6	4	3	-[4]

Notes:

(1) Provisional pre-Budget figures.
(2) Not a forecast. Figures based on assumptions in PEWP
(3) Including debt interest. PEWP figures.
(4) Depending on decisions to be made.
(5) On 25 January.

ANNEX 2

TAXATION: Effects of Indexation

DIRECT TAXES

The Retail Price Index increased in the year to December 1982 by 5.4 per cent. With indexation by this amount and statutory rounding, the figures for the main allowances and other thresholds would be:

Personal Allowances	1982-83	1983-84
	£	£
Single and wife's earned income allowance	1,565	1,655
Married allowance	2,445	2,585
Bands eg		
30% rate	1-12,800	1-13,500
60% rate	over 31,500	over 33,500
Investment Income Surcharge threshold	6,250	6,600

The total revenue costs of indexation (reflected in the forecast) are £845m in 1983-84, £1,080 m in a full year at forecast 1983-84 prices and incomes.

INDIRECT TAXES

Excise duties: increases based on 5.4% revalorisation with rounded price changes including VAT effects

	Typical price change	Revenue (a) £m	RPI impact effect %
Beer	1 pence/pint	90	0.1
Wine	5½ pence/75 cl light wine	25	neg
Spirits	25 pence/bottle	25	0.05
Tobacco	3½ pence/20 KS	115	0.15
Petrol	4½ pence/gallon	210	0.1
Derv	3½ pence/gallon	45	nil
VED	£5 car licence	90	0.05
Increased revenue (reflected in the forecast)		600	0.5 (b)

(a) First and full year revenue effects are largely identical

(b) RPI effects do not sum because of rounding.

TAX: BACKGROUND FACTS

Total taxation

1. Since the Government came to power total taxation as a proportion of GDP has risen by over 5 percentage points. The figures are as follows:-

Table 1:

Total taxation* as a % of GDP (market prices)

1978-79	34.4
1979-80	36.0
1980-81	37.3
1981-82	40.3
1982-83 (forecast)	40.2
1983-84 (assuming indexation)	about 40

(*Including National Insurance Contributions and local authority rates)

Personal taxation

2. To restore personal taxes (direct and indirect) to the same proportion of personal income as in 1978-79 would require reductions of some £9 billion. For income tax and national insurance the following table gives an idea of how the proportion of gross pay they represent has risen, particularly for the low paid:-

Table 2

Income tax and National Insurance Contributions as a percentage of gross earnings

	Married*		
	½ average earnings	Average earnings	2 average earnings
1978-79	16.4	28.0	31.6
1979-80	16.4	26.4	28.9
1980-81	18.2	27.5	29.9
1981-82	21.1	29.4	32.4
1982-83 (forecast)	21.3	30.0	32.5
1983-84 (assuming indexation)	21.7	30.3	32.8

(*Wife not working: the couple are assumed to have no children, to avoid distortion of the figures from the abolition of child tax allowances.)

In 1983-84 the employees' National Insurance Contribution will be 2½ percentage points higher than in 1978-79. Even with the indexation of allowances assumed in the forecast, in 1983-84 income tax and National Insurance Contributions as a percentage of gross earnings would increase for all family types over 1982-83 levels because of the rise in NIC announced in the Autumn Statement.

3. Because we were unable to make any change in personal allowances in 1981 tax thresholds have not risen as fast as prices since we came to office, and more slowly still than earnings:

Table 3

Personal allowances as a percentage of average earnings

	Single	Married
1978-79	20.1	31.3
1979-80	20.1	31.4
1980-81	19.8	30.9
1981-82	17.8	27.8
1982-83 (forecast)	18.6	29.1

Real net incomes are, however, higher than in 1978-79. The increase in the proportion of gross earnings taken in tax partly reflects the fact that earnings have risen faster than prices.

Company sector

4. Real rates of return have been falling since the early 1960s:

Table 4:

Net pre-tax real rates of returns

	Industrial and commercial companies excluding North Sea	Manufacturing companies
1960	13.2	13.2
1965	11.2	10.6
1970	8.7	7.5
1975	4.9	3.5
1979	5.3	4.3
1980	4.0	3.4
1981	3.2	2.1
1982 (estimated)	3.8	n.a.

Real interest rates are now above real rates of return.

5. But the tax burden on companies has not fallen:-

Table 5

Tax paid by industrial and commercial companies (excluding North Sea)

£ billion

	Taxes on companies' income(3)	Employers NIC and NIS (1)	Rates (2)	Total	Total in constant prices(4)
1978	2.8	4.3	2.3	9.4	9.4
1979	2.8	5.4	2.5	10.7	9.4
1980	3.2	6.5	3.2	12.9	9.7
1981	3.6	7.0	4.0	14.6	10.0
1982 (estimated)	4.4	7.1	4.7	16.2	10.2

(1) Estimates of proportion paid by industrial and commercial companies

(2) Includes North Sea and unincorporated business.

(3) Includes mainstream corporation tax, ACT, and tax on company investment income.

(4) Deflated by total final expenditure deflator (1978 = 100).

6. Comparing Tables 4 and 5 shows that companies' ability to pay is falling, but that the demands made on them are rising.

ANNEX 4

READY RECKONER: Illustrative Tax Changes

£ million at forecast 1983-84 income levels

	Direct Revenue Effect	
	1983-84	Full Year
INCOME TAX		
Allowances and Thresholds		
1% above indexation on allowances and Thresholds	140	180
1% above indexation on allowances only	130	160
Rates		
Change basic rate by 1p	850	965
Investment Income Surcharge		
Change threshold by 10% points	1	18
CORPORATION TAX		
Change main rate by 1 percentage point	65	115
Change small companies' rate by 1 percentage point	10	15

OTHER TAXES

	First year cost/yield	Full Year	RPI
Car tax: reduce from 10 to 5 per cent from 1 April 1983	240	325	-0.2
VAT: 1 per cent change	500	690	1.5
NIS: ½ per cent off from August 1983	200	400	
abolition of 1½ per cent rate from August 1983	650	1200	
(Assuming recovery from public sector)			

EXCISE DUTIES

The costs and effects of specimen changes in alcohol, tobacco and petrol etc can be seen from Annex 2.

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

THE 1983 BUDGET

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But can we predict it

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Empty property still possible

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11. We might perhaps discuss this, and the draft paper, at our meeting on 27 January.

(G.H.)
26 January 1983

14/3

Donna

We mustn't forget!

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

Robert Fellowes, Esq
Buckingham Palace

26 January 1983

Dear Mr Fellowes,

Thank you for your letter of 24 January addressed to my colleague, John Kerr. The Chancellor will, of course, be pleased to attend the audience at 6pm on 14 March, as you suggest.

Yours sincerely,

Margaret O'Mara

MISS M O'MARA
Private Secretary

14/3

SANDRINGHAM, NORFOLK

24th January, 1983

Dear Mr. Kerr,

The Queen would like to receive the Chancellor of the Exchequer for his pre-Budget audience at 6 p.m. on 14th March at Buckingham Palace. I should be grateful if you would confirm that he can attend at this time.

Yours sincerely

Robert Fellowes

J.O. Kerr, Esq.

DEPARTMENT OF TRADE
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J0778
Secretary of State for Industry

PS/IR
CST, FST, EST,
DST(C), DST(R)
Sir P Wass
Mr Robinson
Mr Martin
Mr Kemp
Mr Murphy
Mr Moore
Mr French
Mr Beighton (IR)

27 January 1983

The Rt Hon Sir Geoffrey Howe MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1

(RA)

Dear Geoffrey,

Michael Edwardes wrote to you on 24 January about the possible consequences for Mercury Communications Limited of their potential liability for Development Land Tax. He has sought my support in his request that Mercury be granted some form of relief pending the passage of the Telecommunications Bill which will extend the benefits of a General Development Order to all public telecommunication operators.

I understand that your officials are already well siezed of the problem and are proving most helpful in processing the assessment of Mercury's liability. For our part we have stressed to Mercury the need to provide the additional information requested from them as soon as possible. But whether or not Mercury's proposals would produce a Development Land Tax charge I am seriously concerned at the implications of the present situation for our telecommunications policy. We may only be talking of a 6-8 month period but it could prove crucial to Mercury's future. If they fail to establish their network within the timescale announced the business communities' confidence in their ability to provide an effective and reliable alternative to British Telecom will be diminished and with it public credibility in our policy. Of equal concern is the point of principle raised by the inequitable tax liability on the two public telecommunication operators. As you know, the introduction of competition into telecommunications is the basis of our current policy. Mercury faces a formidable task in seeking to enter a market where their only rival is already firmly established. To ask them to do so without the major tax concessions enjoyed by that rival is imposing upon them an unfair burden at variance with our policy.

My concern at this stage, therefore, is not so much the size of the potential charge but whether Mercury should, in the context of our overall telecommunications policy, be subject to the Development Land Tax. Ideally what I would like to see is all public telecommunication operators put on an equal footing. This is one of the objectives of the Telecommunications Bill but until

it becomes law present practice is working against our policy.

I recognise that it is important first to determine Mercury's position. If it were to be decided that Mercury's proposals did not give rise to a Development Land Tax charge, while the objection of principle would remain, we may be able to avoid taking any further action. But in this and in any future action that may prove necessary timing is of the essence. We cannot afford to wait upon the Bill to resolve the difficulty. I should be most grateful, therefore, if you would give this matter your urgent attention and to learn of any solution you are able to offer.

Yours ever

Peter

CH/EX REF. NO B(83)4

COPY NO 1 OF 22 COPIES

NOTE OF A MEETING ON FRIDAY 28 JANUARY 1983 AT 11.AM IN THE CHANCELLOR'S ROOM, HM TREASURY

Present: Chancellor of the Exchequer - in the Chair
Financial Secretary
Economic Secretary
Sir Douglas Wass
Mr Burns
Mr Middleton
Mr Cassell
Mr Kemp
Mr Moore
Mr Griffiths
Mr Kerr
Mr Ridley
Mr French
Mr Freedman - C&E
Mr Howard - C&E
Mr Walters - No 10

---

1 BUDGET 1983 EXCISE DUTY OPTIONS

Papers: Sir Douglas Lovelock's minute of 24 January
Economic Secretary's Private Secretary's minute of 25 January
Chief Secretary's Private Secretary's minute of 25 January
Mr Freedman's minute of 27 January to the Economic Secretary

The following decisions were taken:

i. the duty on a pint of beer would rise by 1p (5.9 per cent).

ii. the duty on wine would increase by 5.9 per cent. It would be described in the Budget speech as an increase of about 5p.

iii. the duty on a bottle of spirits would rise by 25p (5.0 per cent

iv. the duty on a packet of 20 king-size cigarettes would rise by 3p (4.8 per cent)

v. the duty on a pint of cider would rise by the same amount as the duty on beer ie 1p. That was equivalent to an increase of 19 per cent.

vi. the Vehicle Excise Duty would rise by £5 (6.25 per cent).

2. It was agreed to defer decision on the increases in duty on petrol and derv. The Chancellor asked that in advance of consideration of these at an overview meeting a table be produced showing not only the RPI impact of the alternatives proposed, but also the effect of the variants in changing the RPI from its forecast path. It would be helpful to have this by 11 February.

2. "TECHNICAL" INCREASE IN AMOUNT OF DUTY ON SPIRITS

Papers: Mr Freedman to the Economic Secretary of 17 January
Economic Secretary to the Private Secretary's minute of 21 January

3. After a brief discussion it was concluded that no further action need be taken on the question raised in Mr Freedman's minute.

3 VAT ANNUAL ACCOUNTING FOR SMALL BUSINESSES

Papers: Mr Fraser's minute to the Economic Secretary of 20 January
Economic Secretary's Private Secretary's minute of 24 January
Financial Secretary's Private Secretary's minute of 24 January

4. In a brief discussion it was pointed out that the poor state of compliance at the moment and the substantial cost in 1984-85 suggested that this might not be the right year to introduce this measure. The Financial Secretary pointed to the cash flow benefit for small firms, and the help it would give in simplification of their dealings with the tax man. Summing up the Chancellor said that there had to be a presumptic against action in this year's Budget, although he did not wish to reject the idea outright at this stage.

4 BETTING

1. Racing

Papers: Mr Friedman's minute of 11 January to the Economic Secretary
Economic Secretary's Private Secretary's minute of 18 January.

5. It was agreed there was no case for change on this front.

2. Casinos

Papers: Mr Friedman's minute of 21 January
Economic Secretary's Private Secretary's minute of 25 January

6. There was a brief discussion of the merits of shifting the duty scale to alleviate some of the burden on smaller casinos and recouping from the larger casinos. It was decided not to proceed with any changes.

5 TOURISM

Papers: Secretary of State for Trade's letter of 29 October and subsequent comments.

7. Discussion focussed only on the possibility of some VAT relief for tourist-related activities. It was agreed that this was not a runner and should be dropped.

8. It was agreed that the Economic Secretary would take decisions on minor duties and VED on lorries.

9, The meeting closed at 12.15pm.

JKR

JILL RUTTER
28 January 1983

Distribution: Those Present
PS/CST
MST(C)
MST(R)

C.

FROM: D J L MOORE
DATE: 27 January 1983

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State (R)
Minister of State (C)
Sir Douglas Wass
Mr Burns
Mr Middleton
Mr Bailey
Mr Kemp
Mr Cassell
Mr Evans
Mr G Smith
Mr Robson
Mr Reed
Mr Gleed
Mr Ridley
Mr French
Mr Harris

PS/Inland Revenue
Mr Green)
Mr Battishill) IR
Mr Painter)

C.

for next Tuesday's overview, I think (as the main subject)

JG.

I should want [illegible] of all [illegible] of [illegible] 3 papers (incl the [illegible] on UKCS), [illegible] please

NATIONAL INSURANCE SURCHARGE
(including comparison with Corporation Tax)

... The attached paper summarises the main options and considerations for a further reduction in NIS.

2. The second half, from paragraph 11, looks at the industrial and economic impact of cuts in NIS by comparison with corporation tax. Paragraphs 13-15 and the annex are the work of Mr Cassell's group.

3. You may wish to consider this alongside Mr Battishill's paper of 26 January on Corporation Tax rates. (below)

DJLM.

D J L MOORE

N'TIONAL INSURANCE SURCHARGE

1. The rate of NIS will be 1½% from April 1983. Options for further reductions from 1 August are:-

(£m 1983-84 prices and income levels)	Revenue costs 1983-84	full year	PSBR costs 1983-84	1984-85 (fixed interest rates)
½% cut	220	400	200	300
abolition	670	1200	600	900

These costings assume full recovery from the public sector.

2. It would be possible to repeat the 1982 Budget procedure and provide an additional, temporary, reduction between August 1983 and March 1984 so that employers had the full year benefit of a ½% reduction. But this would, of course, add to the 1983-84 costs and it would create a firm presumption that the temporary reduction would be consolidated in April 1984.

Legislation

3. The clause in the Finance Bill would be short. It would provide for the cut, or abolition, and for local authorities to continue to pay in 1983-84 at a rate of 2½% - as assumed in the RSG for that year.

4. Some Members would no doubt dispute whether it was right to give priority to further NIS changes in this Budget. There would again be criticism of charging local authority direct labour organisations 2½% NIS in 1983-84 when their private sector competitors were paying less, and possibly some criticism of reducing the EFLs of "productive" nationalised industries. But debate over the provision would be likely to be relatively straightforward.

/ ninistrative changes

5. DHSS would have to prepare revised NIS/NIC deduction tables to replace those being issued shortly to take effect from April. This task should not cause any difficulties. But, if changes were to be made, the Chancellor might wish to warn the Secretary of State for Social Services.

6. Employers would have to change their records and computer programmes again. But they are unlikely to complain of a further cut and still less of abolition.

7. 1983-84 cash limits and external financing limits would have to be amended. This would be highly unwelcome to those managing the programmes. They find ita messy and time-consuming operation damaging to the cash limits philosophy. For cash limits a November decision to make a change from the following April is much better; the new NIS rate can then be taken on board before the limits are set. But this is not an overriding objection to making a cut in the Budget. If necessary, limits could be amended mid-year, as they have been with previous changes.

Main representations

8. The Industry Secretary, in his letter of 12 January to the Chancellor said:

> "In my view abolition of the NIS is far and away the best of the taxation possibilities. It would be generally welcomed by industry, as have been the successive reductions you have already been able to make. Equivalent concessions through reductions in Corporation Tax would be less well received. and they would be of less help to many of the manufacturing sectors in greatest difficulty." *

9. The Governor, in his letter of 13 January, also suggested abolition of NIS. The Energy Secretary (10 January) advised against further NIS reductions now. The Trade Secretary (12 January) did not mention NIS but favours a cut in corporation tax.

* CPRS (26 January) agree that NIS should have priority.

10. The CBI, in their 1983 representations, put abolition of NIS from April at the top of their list. Other outside bodies wanting NIS cuts or abolition include the Association of British Chambers of Commerce, the National Federation of Self Employed, the Retail Consortium, the Union of Independent Companies and the BIM.

Industrial and economic impact: NIS and corporation tax compared

11. The following table (based on yields in 1981-82) compares the way in which the immediate benefit of a reduction in NIS and in corporation tax would be distributed between sectors of industry and commerce:

	NIS (limited to private sector)	Corporation Tax (mainstream and ACT)
	%	%
Manufacturing	43	27
Distribution	15	12
Financial	11	12
North Sea	-	8
Public Corporations	-	4
Central and Local Government	-	-
Other private sector*	31	37
	100	100

* Includes construction, mining, agriculture, transport services and property.

12. As the table shows a considerably higher proportion of the money from a cut in NIS accrues to the manufacturing sector than from a cut in corporation tax. But a cut in NIS, unlike CT, would not help with the North Sea oil industry.

13. A cut in NIS reduces employers' labour costs, and boosts their cash flow. Simulations on the model suggest that, in the short run, companies would use this to repay bank borrowing and rebuild liquidity. But, over time, competitive pressures are likely to lead companies to pass on part of the fall in costs in the form of lower prices, and pass part back into wages (though when the effect of lower prices is also taken into account, there is little net change in nominal earnings; employees' real earnings, of course, are higher). This reduction in labour costs improves the UK's international competiiveness, raising export volumes and checking imports, while the increase in real wages boosts consumption. Companies' expenditure on stockbuilding and employment is likely to rise in response to their improved financial position.

14. The effects of a cut in CT would be more uncertain, since the tax base is different and companies tend to move in and out of liability to CT. But broadly speaking, our ready reckoners assume that the companies concerned - which would tend to be the more profitable ones - would retain more of the benefits over the medium term, with less passing on into prices than with a NIS cut. As a result, the effect on company sector expenditure might be greater, particularly on investment and dividends, although the benefit to persons and the increase in consumption would be smaller.

15. The annex summarises the likely effects of the two measures, where for illustrative purposes a cut of 1% in NIS and 5-6% in CT (which would have an equivalent PSBR cost in 1983-84) are compared. None of the effects would be large (particularly for a ½% reduction in NIS or 2 points off CT). The main difference stems from their effects on inflation and competitiveness, where the benefits of a NIS cut are more sustained. This means that its medium term impact on GDP and employment are likely to be greater than an equivalent cut in CT.

COMPARISON OF EFFECTS OF 1% REDUCTION IN NIS FROM AUGUST WITH EQUIVALENT CUT IN CORPORATION TAX(1)
(Assuming no change in interest rates)

Change to		NIS	Corporation tax
GDP	1983-84	0.05	0.05
(%)	1984-85	0.2	0.1
	1985-86	0.3	0.15
Employment	1983-84	5	5
(000s)	1984-85	20	15
	1985-86	40	20
Inflation	1983-84	-0.1	0
(%)	1984-85	-0.2	0.1
	1985-86	0	0.2
Real Personal Disposable income	1983-84	0.1	0
(%)	1984-85	0.3	0.1
	1985-86	0.5	0.2
Non-North Sea ICCs Real Disposable Income (%)	1983-84	1.6	1.3
	1984-85	2.1	2.2
	1985-86	1.1	1.9
Competitiveness (% - minus indicates better performance)	1983-84	-0.8	-0.65
	1984-85	-0.9	-0.3
	1985-86	-0.8	-0.1
PSBR	1983-84	400	400
(£m)	1984-85	600	550
	1985-86	450	600

(1) i.e. one with same cost to the PSBR in 1983-84, equivalent to a reduction of some 5-6% in the CT rate. (Including that for small firms).

MP1
25.1.83

Covering Secret.

CHANCELLOR OF THE EXCHEQUER

Richard.

I attach the Chancellor's Paper for Cabinet on Thursday. I understand that the PM instructed that it was not to issue before 1 Feb; and then only under ministerial instructions to ensure that it did not go beyond Private Offices.

Please let me know how many – presumably less than 95 – copies of the Annexes you'll want from us.

John Kerr
28/1.

John

40 copies of Annexes only sent to R. Hatfield Cab. Off. 1.2.83

Ken

Good, many thanks

1/2

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ANNEX 1

SELECTED ECONOMIC INDICATORS, 1979 TO 1983

	1979	1980	1981	1982	1983(1)
World GDP, volume (per cent change)	+3½	+1½	+1½	-1	+1 to +2
UK GDP, volume (per cent change)	+2	-2½	-2½	+½	+1½ to +2½
Domestic demand, volume (including stockbuilding) (per cent change)	+4	-3	-1½	+2½	+3 to +4
Retail prices Q4 (per cent change)	+17½	+15½	+12	+6	about 6½
Interest rates (average 3-month interbank)	14	16½	14	12½	11½ (5)
Current balance (£ billion)	-1	+3	+6	+4½	+1 to +3
Unemployment (UK, per cent, narrow, new definition)	5	6½	10	12	13 (2)

TAX AND PUBLIC EXPENDITURE 1979-80 TO 1983-84

	1979-80	1980-81	1981-82	1982-83	1983-84
Tax and NIC as percentage of GDP	36	37½	40½	40	- (4)
Public expenditure as percentage of GDP(3)	41	43	44½	44	43½
PSBR as percentage of GDP	5	6	4	3	- (4)

Notes:

(1) Provisional pre-Budget figures.
(2) Not a forecast. Figures based on assumptions in PEWP
(3) Including debt interest. PEWP figures.
(4) Depending on decisions to be made.
(5) On 25 January.

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ANNEX 2

TAXATION: Effects of Indexation

DIRECT TAXES

The Retail Price Index increased in the year to December 1982 by 5.4 per cent. With indexation by this amount and statutory rounding, the figures for the main allowances and other thresholds would be:

Personal Allowances	1982-83	1983-84
	£	£
Single and wife's earned income allowance	1,565	1,655
Married allowance	2,445	2,585
Bands eg		
30% rate	1-12,800	1-13,500
60% rate	over 31,500	over 33,500
Investment Income Surcharge threshold	6,250	6,600

The total revenue costs of indexation (reflected in the forecast) are £845m in 1983-84, £1,080 m in a full year at forecast 1983-84 prices and incomes.

INDIRECT TAXES

Excise duties: increases based on 5.4% revalorisation with rounded price changes including VAT effects

	Typical price change	Revenue (a) £m	RPI impact effect %
Beer	1 pence/pint	90	0.1
Wine	5½ pence/75 cl light wine	25	neg
Spirits	25 pence/bottle	25	0.05
Tobacco	3½ pence/20 KS	115	0.15
Petrol	4½ pence/gallon	210	0.1
Derv	3½ pence/gallon	45	nil
VED	£5 car licence	90	0.05
Increased revenue (reflected in the forecast)		600	0.5 (b)

(a) First and full year revenue effects are largely identical

(b) RPI effects do not sum because of rounding.

ANNEX 3

TAX: BACKGROUND FACTS

Total taxation

1. Since the Government came to power total taxation as a proportion of GDP has risen by over 5 percentage points. The figures are as follows:-

Table 1:

Total taxation* as a % of GDP (market prices)

1978-79	34.4
1979-80	36.0
1980-81	37.3
1981-82	40.3
1982-83 (forecast)	40.2
1983-84 (assuming indexation)	about 40

(*Including National Insurance Contributions and local authority rates)

Personal taxation

2. To restore personal taxes (direct and indirect) to the same proportion of personal income as in 1978-79 would require reductions of some £9 billion. For income tax and national insurance the following table gives an idea of how the proportion of gross pay they represent has risen, particularly for the low paid:-

Table 2

Income tax and National Insurance Contributions as a percentage of gross earnings

	Married*		
	½ average earnings	Average earnings	2 average earnings
1978-79	16.4	28.0	31.6
1979-80	16.4	26.4	28.9
1980-81	18.2	27.5	29.9
1981-82	21.1	29.4	32.4
1982-83 (forecast)	21.3	30.0	32.5
1983-84 (assuming indexation)	21.7	30.3	32.8

(*Wife not working: the couple are assumed to have no children, to avoid distortion of the figures from the abolition of child tax allowances.)

In 1983-84 the employees' National Insurance Contribution will be 2½ percentage points higher than in 1978-79. Even with the indexation of allowances assumed in the forecast, in 1983-84 income tax and National Insurance Contributions as a percentage of gross earnings would increase for all family types over 1982-83 levels because of the rise in NIC announced in the Autumn Statement.

3. Because we were unable to make any change in personal allowances in 1981 tax thresholds have not risen as fast as prices since we came to office, and more slowly still than earnings:

Table 3

Personal allowances as a percentage of average earnings

	Single	Married
1978-79	20.1	31.3
1979-80	20.1	31.4
1980-81	19.8	30.9
1981-82	17.8	27.8
1982-83 (forecast)	18.6	29.1

Real net incomes are, however, higher than in 1978-79. The increase in the proportion of gross earnings taken in tax partly reflects the fact that earnings have risen faster than prices.

Company sector

4. Real rates of return have been falling since the early 1960s:

Table 4:

Net pre-tax real rates of returns

	Industrial and commercial companies excluding North Sea	Manufacturing companies
1960	13.2	13.2
1965	11.2	10.6
1970	8.7	7.5
1975	4.9	3.5
1979	5.3	4.3
1980	4.0	3.4
1981	3.2	2.1
1982 (estimated)	3.8	n.a.

Real interest rates are now above real rates of return.

5. (3ut the tax burden on companies has not fallen:-

Table 5

Tax paid by industrial and commercial companies (excluding North Sea)

£ billion

	Taxes on companies' income(3)	Employers[1] NIC and NIS	Rates[2]	Total	Total in constant prices(4)
1978	2.8	4.3	2.3	9.4	9.4
1979	2.8	5.4	2.5	10.7	9.4
1980	3.2	6.5	3.2	12.9	9.7
1981	3.6	7.0	4.0	14.6	10.0
1982 (estimated)	4.4	7.1	4.7	16.2	10.2

(1) Estimates of proportion paid by industrial and commercial companies

(2) Includes North Sea and unincorporated business.

(3) Includes mainstream corporation tax, ACT, and tax on company investment income.

(4) Deflated by total final expenditure deflator (1978 = 100).

6. Comparing Tables 4 and 5 shows that companies' ability to pay is falling, but that the demands made on them are rising.

ANNEX 4

REA[illegible] RECKONER: Illustrative Tax Changes

£ million at forecast 1983-84 income levels

	Direct Revenue Effect	
	1983-84	Full Year
INCOME TAX		
Allowances and Thresholds		
1% above indexation on allowances and Thresholds	140	180
1% above indexation on allowances only	130	160
Rates		
Change basic rate by 1p	850	965
Investment Income Surcharge		
Change threshold by 10% points	1	18
CORPORATION TAX		
Change main rate by 1 percentage point	65	115
Change small companies' rate by 1 percentage point	10	15

OTHER TAXES

	First year cost/yield	Full Year	RPI
Car tax: reduce from 10 to 5 per cent from 1 April 1983	240	325	-0.2
VAT: 1 per cent change	500	690	1.5
NIS: ½ per cent off from August 1983	200	400	
abolition of 1½ per cent rate from August 1983 (Assuming recovery from public sector)	650	1200	

EXCISE DUTIES

The costs and effects of specimen changes in alcohol, tobacco and petrol etc can be seen from Annex 2.

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FINANCIAL SECRETARY TO THE TREASURY

FROM: E KWIECINSKI
DATE: 28 January 1983

PS/CHANCELLOR

cc Chief Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir D Wass
Mr Burns
Mr Middleton
Mr Bailey
Mr Kemp
Mr Cassell
Mr Evans
Mr G Smith
Mr Robson
Mr Moore
Mr Reed
Mr Gleed
Mr Ridley
Mr French
Mr Harris
Mr Green)
Mr Battishill) IR
Mr Painter)
PS/IR

NATIONAL INSURANCE SURCHARGE AND CORPORATION TAX

The Financial Secretary has seen Mr Moore's minute of 27 January.

He has commented that the analysis in the paper attached to Mr Moore's minute seems to show that a cut in CT would not be nearly as good a bet as a cut in NIS.

The line-up at the last overview was :-

NIS	CT
CST	EST
MST(C)	MST(R)
	FST

If FST is changing camps, this is significant!

E KWIECINSKI
28 January 1983

CONFIDENTIAL

FROM: C D HARRISON
DATE: 28 JANUARY 1983

PS/CHANCELLOR

cc Chief Secretary
Financial Secretary
Minister of State (C)
Minister of State (R)
Sir Douglas Wass
Mr Burns
Mr Middleton
Mr Bailey
Mr Kemp
Mr Cassell
Mr Evans
Mr Moore
Mr G Smith
Mr Robson
Mr Reed
Mr Gleed
Mr Ridley
Mr French
Mr Harris

NATIONAL INSURANCE SURCHARGE AND CORPORATION TAX RATES

The Economic Secretary has seen Mr Moore's submission of 27 January on the NIS, and Mr Battishill's submission of 26 January on corporation tax rates.

2. If the choice is between a ½% reduction in NIS or 2 points off the corporation tax rate, the Economic Secretary would go for the latter. This is primarily on the grounds of the evidence quoted by Mr Byatt (paper on taxation in the longer term, 21 December 1982), on the way in which corporation tax hits equity finance considerably harder than debt finance, as well as from the point of view of enhancing profitability.

3. He would go for increases in the profits limits for the small companies' rate of corporation tax of £100,000 and £250,000.

CDH

C D HARRISON

CONFIDENTIAL

FROM: MISS J M SWIFT

DATE: 28 JANUARY 1983

~~PRINCIPAL PRIVATE SECRETARY~~

cc. Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir Douglas Wass
Mr Middleton
Mr Kemp
Mr Moore
Mr Robson
Mr French
Mr Ridley
Mr Battishill) I/R
Mr Green)

CORPORATION TAX RATES

The Chief Secretary has seen Mr Battishill's minute of 26 January to the Chancellor.

2. The Chief Secretary does not find the case for a change in the rates of Corporation Tax very convincing, at least as a priority, when the scope for tax reductions is necessarily limited.

A change for "small" cos is, in any case, necessary: in that context, are [illegible] A.B §10(d)

Then two 3 CT options?

(a) 10(d) alone ✓
(b) 10(d) + 2% off CT rate ✓
(c) [illegible] scheme ✓

Spoke to S Robson

MISS J M SWIFT
28 January 1983

Not a v. strong case for (b) or (c) ∴ not so good for economy, not widely requested: but has a lower [illegible] cost than NIS? and may be a necessary intermediate [illegible] for oil package — between oil package B + oil package C.

∴ We need a collated table bringing together options for NIS, CT + oil

(tho' we may date distinctly than difficulty for presentation e.g. include small cos changes in [illegible] package; + (part of) CT rate cut in oil package

CONFIDENTIAL

From The Assistant Private Secretary
Date 28 January 1983

PS/CHANCELLOR

cc PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
PS/Minister of State (C)
Sir Douglas Wass
Mr Burns
Mr Middleton
Mr Bailey
Mr Kemp
Mr Cassell
Mr H P Evans
Mr Moore
Mr Robson
Mr G Smith
Mr Reed
Mr Gleed
Mr Ridley
Mr French
Mr Harris

PS/Inland Revenue

NATIONAL INSURANCE SURCHARGE (NIS) AND CORPORATION TAX (CT) RATES

The Minister of State (Revenue) has seen Mr Moore's minute of 27 January and Mr Battishill's minute of 26 January.

2. He recognizes that it is desirable to phase out NIS as soon as possible but at the moment he would rank a further cut in NIS below a reduction in CT - he favours a cut in the main CT rate to 50% and an increase in the lower and upper limits on the small companies' rate to £100,000 and £300,000 respectively (paragraph 10b of Mr Battishill's minute) - and below a fairly substantial increase in the personal tax allowance thresholds.

Tim Milner
J C MILNER

CONFIDENTIAL

FROM: MISS J M SWIFT
DATE: 31 January 1983

CHIEF SECRETARY TO THE TREASURY

PS/CHANCELLOR

cc Financial Secretary
Economic Secretary
Minister of State (C)
Minister of State (R)
Sir D Wass
Mr Burns
Mr Middleton
Mr Bailey
Mr Kemp
Mr Cassell
Mr Evans
Mr G Smith
Mr Robson
Mr Moore
Mr Reed
Mr Gleed
Mr Ridley
Mr French
Mr Harris
Mr Green)
Mr Battishill) IR
Mr Painter)
PS/IR

NATIONAL INSURANCE SURCHARGE AND CORPORATION TAX

The Chief Secretary agrees with the Financial Secretary's comment recorded in Eric Kwiecinski's minute of 28 January.

MISS J M SWIFT

MR R C MITCHELL

4. <u>What is the size of the VAT burden on charities?</u>

I can give no reliable figure. The overwhelming majority of charities are not registered for VAT and those who are make returns relating only to their business purchases.

5. <u>In 1972 the then Chancellor of the Exchequer promised to give charities relief if VAT caused them serious disadvantages. Will the Chancellor honour this commitment?</u>

There was no open-ended commitment to VAT relief. The Chancellor promised to consider some means of additional help if any charities could show that they were seriously disadvantaged after all the tax changes made in the 1972 Finance Bill. In fact, taking account of further direct tax concessions made in the following year, charities in general benefited from the tax changes.

6. <u>What has the Government done to mitigate the burden on charities of the increased rate of VAT?</u>

Each of my last three Budgets has contained measures to benefit charities and their beneficiaries, particularly the disabled. I would remind the hon Member of the increased tax relief available to covenanted donations, on capital transfer tax, development land tax and the mobility allowance, and the extensions of specific VAT reliefs for medical equipment, ambulances and aids for the disabled. We have also increased the amount of direct grants to charities in real terms.

7. <u>The public resents VAT being paid on their donations</u>

VAT is not paid on donations. Much of charities' income from donations is spent on items that are not subject to VAT (eg staff costs, rents, heating, food) and only a small percentage is spent on VAT - it is far less than the 15% sometimes suggested.

MR R C MITCHELL

NOTES FOR POSSIBLE SUPPLEMENTARY QUESTIONS

1. Will the Chancellor provide VAT relief for charities in his Budget?

The hon Member will not expect me to anticipate my Budget Statement.

2. What are the objections to providing VAT relief?

We have looked carefully at this possibility time and time again, but have been forced to conclude that it is not possible to provide such a relief fairly and economically. There would be an indiscriminate tax subsidy based on the pattern of spending rather than on merit, need or public support. Administration and control would require many extra civil servants to deal with a very large number of charities, the vast majority of whom are not registered for VAT.

3. The administrative costs have been exaggerated. Research shows only 10,000 potential claimants

I am aware of the claims made by the Charities VAT Reform Group following a survey made at the Charity Commission. I have to say that, having studied their research findings closely, I think their estimate is far too low. For example, it assumes that charities who do not submit accounts regularly to the Charity Commission are inactive, whereas in fact not all registered charities are required to submit accounts. It assumes that charities would not seek to claim VAT refunds below £150, which seems a very doubtful proposition. And, very importantly, it takes no account of charities in Scotland and Northern Ireland, and the tens of thousands of charitable bodies, including churches, who do not have to register with the Charity Commission.

MR R C MITCHELL

8. Local authorities can recover VAT. Why not charities?

The refund of VAT to local authorities under Section 15 of the Finance Act 1972 is one of the ways in which local authority spending is financed by central government. The alternative would be an increase in the rates or rate support grant. It would be wrong to use Section 15 to provide government finance to bodies outside the public sector.

9. Commercial companies can recover VAT on their purchases as input tax. Why not charities?

Commercial companies can recover input tax on purchases related to taxable supplies made in the course of business. Charities who carry on businesses are treated in exactly the same way as commercial companies.

10. Many charities provide services which supplement National Health Service provisions. Why cannot they be allowed a VAT refund in line with the arrangement announced last week for refund of VAT on services contracted-out by NHS hospitals?

A. The arrangement to which the hon member refers is a method of providing an incentive to improve the efficiency of public bodies which, unlike charities, are already paid for out of taxation. It will lead to real savings. If they incurred VAT on contracted-out services it would simply add to the total size of the tax bill. There would be no sense in that. In any case, a VAT relief could not be limited to selected charities, such as those operating in the health field. Everyone has passionately held views about which charities are most deserving, and selective relief would be widely regarded as indefensible by non-beneficiaries.

MR R C MITCHELL

NOTE

1. The Chancellor last answered oral questions on 27 January. Written representations on VAT relief for charities are reaching Customs and Excise at a rate of about 12 a week. A final total, necessarily excluding those in the pipeline, will be provided on 23 February.

2. Mr Mitchell recently forwarded a letter on the Southampton Spastics Association. A copy of the letter and draft reply
... are attached. Mr Mitchell has also added his name to the
... Early Day Motion on VAT and charities (copy attached).

3. The current campaign for VAT relief for charities is being orchestrated by the Charities VAT Reform Group, an ad hoc committee of some 120 charities who claim to pay irrecoverable VAT of some £7 million a year. A major plank of their argument is that the administrative cost of providing relief has been exaggerated since research carried out for them at the Charity Commission indicates that no more than 10,000 charities would be likely to seek benefit under any realistic scheme for refund of VAT on charities' purchases. In replying to these claims, which have been presented by Mr John Hannam MP and Mr Tim Yeo of the Spastics Society, the Chancellor replied to the effect that, based on Inland Revenue experience, a refund scheme would be an undertaking involving at least 100,000 charities. He pointed out that the Charities VAT Reform Group's estimate was based on false assumptions (eg that registered charities who do not submit regular accounts to the Charity Commission are inactive and that charities would not seek to reclaim VAT refunds under £150 per annum), and that it also took no account of tens of thousands of charitable bodies, including churches and congregations, who are exempt from registration with the Charity Commission, as well as all charities in Scotland and Northern Ireland.

MR R C MITCHELL

4. Customs and Excise have recently had discussions with representatives of the Spastics Society about the Charities VAT Reform Group's claims. As a result they have concluded that the findings of the research have been misinterpreted by the Charities VAT Reform Group, in ways which seriously underestimate the number of registered charities whose income (and not potential expenditure) is over £1,000 per annum. We do not think it is appropriate at this stage to use this point in answering Parliamentary Questions, since the Spastics Society representatives have said they will clarify the matter in writing.

SOUTHAMPTON AND DISTRICT
SP[illegible]STICS
[illegible]SSOCIATION

9-19 ROSE ROAD
SOUTHAMPTON
SO2 1AE

TEL. (0703) 290

1st February 1983

Mr R G Mitchell M.P.
Southampton Itchen
House of Commons
London W1

Dear Mr Mitchell,

Value Added Tax

Once again I approach you on the matter of Value Added Tax and the continuing refusal of the Chancellor of the Exchequer to grant relief to Charities.

This year the VAT reform group headed by the Spastics Society has done research at the Charity Commission and contends that the number of Charities eligible to claim relief would be no more than 10,000. This would not seem to support the fears of the Chancellor that the grant of relief to Charities would be a "massive undertaking".

Our own situation is that so far this financial year we have lost nearly £2,000 in unrecoverable VAT, and this is likely to be £2,500 by the 5th April 1983. This is a large sum to lose and could have bought 2 electric wheelchairs and a computer communication system for our children.

I do hope that you will feel able to help in this matter by signing the Early Day Motion 182 entitled "Relief for Charities" which is currently tabled in the House of Commons.

May I take this opportunity of thanking you for your assistance with this matter in the past. We were most grateful for your help.

Yours sincerely,

Ann Rich

Mrs M.A. Rich
Secretary and
Administrator

R C Mitchell Esq MP

You wrote to Geoffrey Howe on 6 February enclosing this letter from Mrs M A Rich, Secretary and Administrator of the Southampton and District Spastics Association, about VAT and charities.

I do understand charities' concern about the burden of irrecoverable VAT on their purchases and we are continually looking for ways in which to help them. We have looked very closely on several occasions at the possibility of introducing a scheme of VAT refunds to charities, but we have reluctantly had to conclude that the difficulties, which in part include those of administration, are insurmountable.

The number of charities in the UK is very large indeed, possibly approaching a quarter of a million. I know that recently the Charities' VAT Reform Group claimed that no more than 10,000 charities would be eligible to claim VAT refunds. Tim Yeo, Chairman of the Group, has since written to Geoffrey Howe explaining the basis of this estimate which Customs and Excise have studied very closely with the help of the Charity Commission and the Inland Revenue. I have to say that, having studied Customs and Excise' report, I think the estimate is far too low. It seems to exclude, for example, the many tens of thousands of bodies with charitable status which are not required to register with the Charity Commission, and all the charities in Scotland and Northern Ireland. We believe that at least 100,000 charities would seek to benefit from a general VAT relief. Refunding VAT to them would not be simply a matter of processing claim forms. Customs and Excise would require many extra staff to operate certain minimum checks and controls to guard against errors and abuse, making this a most wasteful and inefficient way of helping charities.

The administrative difficulties therefore remain very great but, of course, they are not the only problem. The cost in revenue terms, though hard to estimate, would be significant. In addition, charities would benefit unequally, with controversial charities benefiting as much as, or in some cases even more than, those with wide public support; for the amounts refunded would depend mainly on their pattern of spending not on their sources of income. There would also be problems in areas where charities provide VAT-exempt services in competition with commercial institutions, where the charities would gain considerable advantage.

For all these reasons, we have had to rule out general VAT relief for charities, but they have been helped in other ways. As well as the tax concessions introduced at the same time as VAT in 1973, each of the last three Budgets contained a package of direct tax measures or specific VAT reliefs designed to help charities and the disabled. Cash grants to charities have also been increased - they now amount to over £140 million a year. I believe that these measures are a far more effective way of using the resources available to help charities than spending all or part of the sum on indiscriminate VAT refunds.

JOCK BRUCE-GARDYNE

182 *RELIEF FOR CHARITIES*

Mr John Hannam
Mr Jack Ashley
Mr Dafydd Wigley
Sir David Price
Mr Clement Freud
Mr David Ennals

★ 149

Mr Ron Lewis
Mr Geraint Morgan
Mr Alan Williams
Mr Tom Ellis
Mr William Wilson
Mr David Ginsburg
Mr Michael Brotherton
Mr John Parker
Mr Bryan Magee
Mr Eldon Griffiths
Mr John Corrie
Mr Jim Spicer
Mrs Angela Rumbold

That this House notes that in 1972 the then Chancellor of the Exchequer gave a commitment that if value-added tax caused 'serious disadvantage' to charities he would consider granting them relief; that the increase from 8 per cent. to 15 per cent. in the rate of value-added tax in June 1979 greatly increased the financial hardship caused by this tax to charities; recognises that many charities provide vital services which are often similar to those provided by local authorities which, like commercial companies, are able to recover value-added tax; and urges the Government to take steps to end this anomalous burden on the voluntary sector in the forthcoming Budget.

★ *The figure following this symbol gives the total number of names of Members appended, including those names added in this edition of the Notices of Questions and Motions.*

141 *PENSIONS CLAWBACK*

Ms Harriet Harman
Mr Frank Haynes
Mr Dennis Skinner
Mr A. W. Stallard
Mr Alfred Dubs
~~Mr Jim Marshall~~

★ 86

Mr John Cartwright

That this House condemns the Government's determination to implement the clawback arrangements on pensions and other benefits announced in the Chancellor's autumn finance statement, whilst the basic pension is still woefully inadequate, and as Christmas approaches, pensioners are once again offered the meagre charity of a £10 Christmas hand-out, long since overtaken by inflation.

151 *PENSIONERS' CLAWBACK*

Mr Charles Irving
Mr Albert McQuarrie
Miss Betty Boothroyd
Mr Lawrence Cunliffe
Mr David Knox
~~Mr A. W. Stallard~~

★ 97

Mr Gavin Strang — Mr John Corrie — Mr Robin F. Cook
Mr William Wilson

That this House urges Mr Chancellor of the Exchequer not to take any steps to implement clawback arrangements on pensions and other benefits announced in his autumn financial statement; and hopes that the Budget in April 1983 will give greater help, not less.

★ *The figure following this symbol gives the total number of names of Members appended, including those names added in this edition of the Notices of Questions and Motions.*

Mr R C Mitchell
Social Democrat
Southampton, Itchen

Thursday
24 February
ORAL

To ask Mr Chancellor of the Exchequer, how many representations he has received requesting value-added tax relief for charities since he last answered oral questions.

---- since 27th January.

My Treasury colleagues and I have received /_ _ _7* written representations on this subject since ~~I last answered oral questions~~ 27 January

MS

B H KNOX

HM Customs and Excise
King's Beam House
Mark Lane EC3

16 February 1983

* See NOTES

NOTE OF A MEETING ON FRIDAY 28 JANUARY 1983 AT 11.AM IN THE CHANCELLOR'S ROOM, HM TREASURY

Present: Chancellor of the Exchequer - in the Chair
Financial Secretary
Economic Secretary
Sir Douglas Wass
Mr Burns
Mr Middleton
Mr Cassell
Mr Kemp
Mr Moore
Mr Griffiths
Mr Kerr
Mr Ridley
Mr French
Mr Walters - No. 10.
Mr Friedman - C&E
Mr Howard - C&E

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1 BUDGET 1983 EXCISE DUTY OPTIONS

Papers: Sir Douglas Lovelock's minute of 24 January
Economic Seccretary's Private Secretary's minute of 25 January
Chief Secretary's Private Secretary's minute of 25 January
Mr Friedman's minute of 27 January to the Economic Secretary

The following decisions were taken:

i. the duty on a pint of beer would rise by 1p (5.9 per cent).

ii. the duty on wine would increase by 5.9 per cent. It would be described in the Budget speech as an increase of about 5p.

iii. the duty on a bottle of spirits would rise by 25p (5.0 per cent)

iv. the duty on a packet of 20 king-size cigarettes would rise by 3p (4.8 per cent)

v. the duty on a pint of cider would rise by the same amount as the duty on beer ie 1p. That was equivalent to an increase of 19 per cent.

vi. the Vehicle Excise Duty would rise by £5 (6.25 per cent).

2. It was agreed to defer decision on the increases in duty on petrol and derv. The Chancellor asked that in advance of consideration of these at an overview meeting a table be produced showing not only the RPI impact of the alternatives proposed, but also the effect of the variants in changing the RPI from its forecast path ~~of the variants~~. It would be helpful to have this by 11 February.

2. "TECHNICAL" INCREASE IN AMOUNT OF DUTY ON SPIRITS

Papers: Mr Fr~~i~~eedman to the Economic Secretary of 17 January
Economic Secretary to the Private Secretary's minute of 21 January

3 ~~2~~ After a brief discussion it was concluded that no further action need be taken on the question raised in Mr Fr~~i~~eedman's minute.

3 VAT ANNUAL ACCOUNTING FOR SMALL BUSINESSES

Papers: Mr Fraser's minute to the Economic Secretary of 20 January
Economic Secretary's Private Secretary's minute of 24 January
Financial Secretary's Private Secretary's minute of 24 January

4. In a brief discussion it was pointed out that the poor state of compliance at the moment and the substantial cost in 1984-85 suggested that this might not be the right year to introduce this measure. The Financial Secretary pointed to the cash flow benefit for small firms, and the help it would give in simplification of their dealings with the tax man. Summing up the Chancellor said that there had to be a presumption against action in this year's Budget, although he did not wish to reject the idea outright at this stage.

4 <u>BETTING</u>

<u>1. Racing</u>

<u>Papers</u>: Mr Fr~~i~~eedman's minute of 11 January to the Economic Secretary
Economic Secretary's Private Secretary's minute of 18 January.

5. It was agreed there was no case for change on this front.

<u>2. Casinos</u>

<u>Papers</u>: Mr Friedman's minute of 21 January ~~1983~~
Economic Secretary's Private Secretary's minute of 25 January

6. There was a brief discussion of the merits of shifting the duty scale to alleviate some of the burden on smaller casinos and recouping from the larger casinos. It was decided not to proceed with any changes.

5 <u>TOURISM</u>

<u>Papers</u>: Secretary of State for Trade's letter of 29 October and subsequent comments.

7. Discussion focussed only on the possibility of some VAT relief for tourist-related activities. It was agreed that this was not a runner and should be dropped.

8. It was agreed that the Economic Secretary would ~~m~~take ~~a~~ decision~~s~~ on minor duties and VED on lorries.

9, The meeting closed at 12.15pm.

JILL RUTTER
28 January 1983

<u>Distribution</u>: Those Present
PS/CST
MST(C)
MST(R)

Budget Secret

EXCISE DUTIES (C&E OF 24/1 and Ministerial comments)

Customs Package				Min Comments			
	Price	Revenue	RPI	EST (Price)	MST(R) CST		SoS T
Beer	✓ 1p (5.9%)	90m	0.1	✓	✓	✓	
Wine	✓ 5½p (5.9) - abt 5	25m	-	6p	✓	✓	
Spirits	✓ 25p (5.0)	25m	0.05	✓	✓	✓	
Tobacco	3p 3½p (5.~~6~~ 4.8)	100m. 115m	0.13. 0.15	3p	✓	✓	
Petrol	Delay 4½p (5.5)	210m	0.1	6p	✓	✓	6p
Derv	3½p (5.0)	45m	0	✓	✓	✓	3½ or 4
VED	✓ £5 (6.25)	90m	0.05	No Change	✓		No change
Cider	✓ 1p (19.0)	4m	-	Large			

+ duty increase on cider

(✓ = support C&E)

Table showing RPI impact of agreed package + alternative option downward RPI effect.

15th

~~13th~~

Defer dec'n prob. wt.

VAT ANNUAL ACCOUNTING FOR SMALL BUSINESSES

(C&E of 20/1 and Min comments)

C&E: improve small business cash flows; once-and-for-all cost in yr introduced, ongoing interest cost; but staff savings. But won't press in 1983 ∴ state of trader compliance

EST: Not until compliance better

FST: Attractive part of small business package

BETTING

No

1. Racing (C&E to EST of 11/1; EST of 18/1)

Industry demand - 2 percentage points off on-course and off-course duties (cost £65-70m)

removal of tax-on-tax (cost £15-20m)

C&E - no case for change

EST - agrees; but if backbench pressure for concession would favour removal of tax-on-tax

No

2. Casinos (C&E to EST of 21/1; EST of 25/1)

Gaming Board - concern about impact of gaming licence duty on smaller casinos

C+E - no change though recognise "social" case for relief for smaller casinos

E ST - wants shift from larger to smaller casinos with restructured scale :

CURRENT SCALE		NEW SCALE	
Yield £mpa)	Duty	Yield	Duty
0-1	5	0-0.2	Nil
1-4½	12½	0.2-1	6¼
> 4½	25	1-4½	12½
		4½-9	25
		> 9	33⅓

but note possible objections to duty being charged on bad debts

NO

TOURISM PACKAGE

You are only looking at VAT relief; S/S Trade asked you to consider, if you were making general VAT concessions.

Specific support on VAT from S/S Scotland who wants concession on food element in restaurant meals

but opposed by officials (S Robson of 13/1) } severe complication
EST } on VAT front
FST - no case for tourism package at all

General conclusion that other elements (p/ex or perhaps Cap allowances) might be preferable

"TECHNICAL" INCREASE IN AMOUNT OF DUTY ON SPIRITS

Q of whether 2.4p increase should be publicly acknowledged in Budget - requested by some of spirits lobby.

C&E doubts that spirits traders really want to have revealed that duty has so far been "underpaid" make allowance if necessary by adjusting change in legal rate of duty.

EST prepared to accept if really view of spirits lobby - but has doubts.

CST to consider, in search of a suggestion or two

Royal Institute of British Architects 66 Portland Place London W1N 4AD ☎ 01-580 5533

From the President's Office

1 February 1983

HM TREASURY – MCU
RECD. - 2 FEB 1983
ACTION: FST (B. Lee)
REF No. 0000230

OL/CAN

The Rt Hon. Sir Geoffrey Howe QC MP,
Chancellor of the Exchequer,
H.M. Treasury,
Parliament Street,
London SW1P 3AG.

Dear Chancellor

I attach on behalf of the Royal Institute a memorandum of proposals to which I hope you will give consideration in the preparation of the Budget for 1983.

We believe these to be reasonable and practicable proposals which would enable the profession and the construction industry to make a positive contribution to national objectives with regard to the economy and employment.

Yours sincerely

Owen Luder

OWEN LUDER
President

FINANCIAL SECRETARY
REC. - 3 FEB 1983
PS | IR PS | CTE
PPS EST MST C
CST MST R
SIR D WASS
Mr MIDDLETON
Mr MOORE
Mr HODSON
Mr GRIFFITHS
Mr MARTIN
Mr MURPHY
Mr FRENCH
Mr KEMP

Enc.

RIBA BUDGET PROPOSALS TO THE CHANCELLOR OF THE EXCHEQUER

INTRODUCTION

1.1 The Budget Statement last year recognised that the construction industry is one 'which can make a particularly significant contribution to the creation of new jobs', but the potential of the industry to stem the surge in unemployment has not been utilised. In the first nine months of 1982 the growth in construction output in the private sector was largely offset by a decline in public sector output exceeding 4%, in real terms, below the level of 1981.

1.2 Current forecasts for 1983 and 1984 project increases in output of 4% and 2% respectively. Even if realised this growth would go only a little way towards compensating for the fall in output of over 16% in real terms which the industry suffered during 1980 and 1981. It should not be forgotten that the industry had already seen output decline by 15% between 1973 and 1979, the year the present Government entered office. Any upturn which now occurs will be from a very low base indeed.

1.3 The effects of Government policy towards the construction industry on the architectural profession have been severe. Architects in private practice have in the past received a significant proportion of their work from public sector clients. The reduction in their public sector work has not been compensated by a corresponding increase in work from private sector clients and an RIBA survey last year found that 30% of architects in private practice were underemployed.

1.4 The Prime Minister's announcement in November last year encouraging local authorities to fully spend their capital allocations was welcome. However the exhortation came so late that there will be significant underspending in 1982-83, even though the Government had ample warning (e.g. through the RIBA Survey of Local Authority Offices, published in June) that the problem would arise. The RIBA is not convinced that the underspend problem, which the construction industry has faced for many years, will not recur in the future.

1.5 The problem does not merely consist of underspend and the comparisons which have been made of 1982-83 'expected output' and 1983-84 'provision' are spurious. For housing in 1983-84 the Government plans to increase the gross capital provision by only 1.7% on a cash basis, a drop in year-on-year provision. The Institute is thus continuing to seek a sustained and significant real increase in annual provision. The announcement that local authority spending allocations will not drop by more than 20% over a two year period was a step in the right direction, but many projects demand planning over a longer period and further guarantees would offer greater stability to the industry and provide a more efficient use of resources.

1.6 A sustained increase in construction activity is essential. No one can justifiably deny that the nation has adequate resources to provide basic housing for all, yet the state of much of our stock is a disgrace. Nor can it be doubted that there is scope for improving our industrial buildings, schools and hospitals to meet modern needs and increasing the level of preventative maintenance.

1.7 Fiscal changes may remove obstructions to a revival in the fortunes of the industry. However these alone will not create a sufficient level of construction output in the coming years. The Institute must urge, once again, that the Government's spending programme gives construction work a higher priority.

BUDGET RECOMMENDATIONS

V.A.T

2.1 Higher registration threshold for small traders: The depth of the recession in the construction sector has resulted in many architects leaving their employment in local authorities or in medium or large sized private practices. Many of these have started up small practices of their own and evidence suggests that they are suffering from underemployment.

2.2 As for many small entrepreneurs, VAT is often a burden which threatens their very existence at a time when work is scarce. Only by raising the threshold for registration to around £25,000, an increase considerably exceeding the inflation element, would the Government be sufficiently encouraging the smaller businesses it claims to favour.

2.3 Whatever level the Government chooses it is imperative that traders below the threshold should maintain the option whether or not to register.

2.4 Zero rating on the repair and maintenance of buildings: The English House Condition Survey confirmed the growing problem of disrepair in the housing sector. Almost a quarter of the nation's housing stock (amounting to 4.3m dwellings) requires repairs which will cost over £2,500. This work alone represents potential construction work worth considerably in excess of £20,000m in value.

2.5 An increasing number of houses - and other buildings - have been falling into disrepair in recent years. Many of these are historic buildings of significant architectural importance. Preventative maintenance work has not been carried out and minor repairs have developed into serious defects. Much of this work is not eligible for grants.

2.6 Despite the welcome encouragement which the Government is now offering through the home improvement grant programme, grants alone cannot be expected to effectively stimulate the level of repair work which is required, not least because of the administration involved. Constraints on current spending have already led to an enormous backlog of improvement grant claimants in many areas.

2.7 The RIBA proposes that as an incentive to encourage the vast amount of work necessary to improve the nation's building stock which is ineligible for grants, building repair and maintenance work by registered traders should be zero-rated for VAT purposes. There should be a concerted effort to amend the relevant EEC regulations.

2.8 This recommendation is in the long term economic interest of the nation:

i) It may preclude a further recurrence of mass dereliction and the subsequent need for slum clearance schemes.

ii) The work would be highly labour-intensive and reduce the level of unemployment, not least because consumer expenditure would be stimulated in the domestic economy due to the very low import content of building repair work.

iii) There would be an important counterbalancing effect on fiscal revenue. The current incentive to clients of a discount equivalent to the value of VAT for cash payments, which has facilitated the growth of the black economy, would be lost.

iv) There may be significant side effects, such as improved energy performance through conservation work.

2.9 Energy conservation: One of the ways by which energy conservation is discriminated against is through fuel and power being zero rated for VAT purposes whilst conservation work is liable to VAT.

2.10 The Government should zero rate energy conservation services and, where appropriate, extend the range of products covered. The alternative way of curing the anomaly, ending zero rating on fuel and power services, whilst being in line with the Government's stated objective of encouraging conservation through 'economic pricing', could have unacceptable social consequences.

SCHEDULE A INCOME : ABORTIVE EXPENDITURE

3.1 At present when a company is taxed under Schedule A the cost of employing a consultant architect is not an allowable business expense except in connection with maintenance work. Property developers frequently incur abortive expenditure, for example when an entry is prepared for an architectural/developer competition (eg Hampton) where only one competitor can win.

3.2 The Institute believes that not to treat architects' fees as an allowable expense when no income is actually realised to the company is, effectively, a tax on creative design and innovation. The Government should therefore take steps to remedy this anomaly.

CAPITAL ALLOWANCES FOR INDUSTRIAL BUILDINGS

4.1 Office content: Preliminary research by NEDO has indicated that the typical proportion of industrial buildings accounted for by office space requirements exceeds 20%. However, industrial buildings qualify for tax allowances in full only where the cost of the office content does not exceed 10%.

4.2 The existing office threshold does not take into account the needs of modern industrial buildings where new technology may well demand a 30-40% office content. The tax threshold should be raised to 20% immediately and the situation kept under review.

4.3 Value of allowances: The private industrial building sector is continuing to be particularly hard hit by the recession. Output for the first nine months of 1982 was over 5% down on the low level of the prevous year and, ominously, the value of orders over the same period dropped by more than 10%.

4.4 Restructuring is proving necessary, to meet the needs of Britain's changing economy. It is the right time to raise the capital allowance in this sector, at least for conversion and improvement work, to 100%, in order that the industrial stock is made suitable for such change.

4.5 Small Workshops Scheme: This has met with considerable success and last year it was extended to March 1985, but only for workshops of up to 1,250 sq ft. The Institute believes that this extension should apply for all small workshops covered by the scheme.

STAMP DUTY

5.1 The threshold for liability to Stamp Duty is currently much lower in relation to house prices than it has been in the past. Consequently the proportion of house purchasers liable to this tax has more than doubled, from 16% in 1974 to 38% of current purchasers. The threshold in 1974 was equivalent to £38,500 at today's house prices; the present threshold, despite a welcome increase in 1982, is only £25,000.

5.2 The average house price is now £26,000 (according to the Nationwide Building Society) and although first time buyers tend to buy relatively cheaper property, prices vary regionally to the extent that many first time buyers, particularly in the South, pay Stamp Duty.

5.3 The Institute recommends that Stamp Duty be abolished for first time purchasers. At the very least the threshold should be raised to a level which would exclude the vast majority of such purchasers. In order to enable most first time buyers in high cost regions to avoid liability this would involve raising the threshold to around £35,000.

NATIONAL INSURANCE CONTRIBUTIONS

6.1 With the present high level of unemployment there has been much support for a reduction in employers' National Insurance contributions. It is widely recognised that by directly increasing the costs of employing staff they act as a tax on employment and the reductions in the surcharge last year were welcome. The larger private architectural practices in particular find that salary related expenditure forms a large proportion of their costs.

6.2 The RIBA believes that as a step towards scaling down employers' contributions the Government should abolish the National Insurance Surcharge. This would be of major importance in fulfilling the Government's aim of 'pricing people back into jobs' and improving company liquidity. There would be greater certainty that benefits which might accrue from a reduced tax burden will not be lost to the domestic economy through import leakage.

CORPORATION TAX

7.1 The development of thriving small businesses is essential to the health of our economy. However corporation tax, even at the small companies rate, often creates a burden which hinders their progress by acting as a disincentive to building up profits for future investment.

7.2 The Institute believes that corporation tax for companies with profits of less than £50,000 should be at the lower rate of 20%. This new level would have the effect of reducing the tax liability of very small companies and creating a more gradual incidence.

NEW TECHNOLOGY

8.1 The RIBA wishes to encourage the appropriate development of new patterns of technology. To date the purchase of micro-computers within the architectural profession, for example, has on the whole been confined to a relatively few large practices.

8.2 Whilst such purchases are allowable against income for tax purposes this does not provide an incentive to companies with low profit levels. If the Government wishes to speed up the growth in use of new technology it should offer grants for purchases of micro-computer equipment and related software.

8.3 These grants would enable many small businesses to use new technology where they would not otherwise consider purchasing the necessary equipment. If the grants were taxable this would prevent a tax free bonus reaching companies which would have bought the equipment regardless of the grant being offered.

February 1983

MR HAYDON
MR JOHNSON
MRS WILKINS

(mp)

FROM: J PAGE
DATE: 2 February 1983

cc Mr Kemp
Miss O'Mara
Mr R I G Allen
Mr Hall
Mr Monaghan

Mr Chambers
Mr Batchelor

IDT ALL

BUDGET ASSIGNMENT : DOCUMENTATION

The head of Support Unit has the responsibility for the provision of budget documents to:

a. The Gallery

b. The Lobby

c. Other Press, TV and Radio

d. Non-press

The consolidated IDT document indent has been sent to Miss O'Mara in Mr Haydon's minute of 26 January titled Budget Aid Memoire. This minute proposed amendments to Miss O'Mara's minute of 13 January.

The non-press arrangements are now in operation and written requests are coming in to Mr Haydon from those firms and organisations contacted in the 1982 list.

Although Mr Haydon will be departing from IDT before the Budget he has kindly agreed to supervise the handling of Budget documents in the Press Gallery and in the Lobby on Budget Day.

When Mr Haydon hands Support Unit to Mr Johnston the latter will take responsibility for all press and non-press documentation, liaising with Mr Chambers, Mr Batchelor and with the Chancellor's Office.

Mrs Wilkins, Miss Brown and Mrs Sturton in Support Unit have a key role in Budget documentation and are adept in the existing procedures.

Problems arising on documentation should be referred to myself in the first instance. The cardinal rule is not to accept bids for documents outside the terms set out in my circular letter dated 20 January and in the Treasury Press Notice to be sent out on 7 February.

J. Page

JOHN PAGE