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PART E

BUDGET SPEECH 1984

DDS 25 years N. A3L3 28/08/94

PO -CH /NL/0004
PART E

CLOSED

CONTINUED ON:-

PART F

Budget Speech
1984

PO/CH/NC

Part E

B(84) 792

FROM: R G LAVELLE
DATE: 7 March 1984

MISS O'MARA

cc: Sir T Burns
Mr Littler
Mr Evans
Mr Folger

BUDGET SPEECH: THE ECONOMIC BACKGROUND

I attach a marked-up text indicating the comments Mr Evans and I have to offer on the draft you circulated yesterday. It also incorporates a redraft suggested by Mr Littler of the final two sentences of paragraph 11.

2. The comments consist either of largely self-explanatory drafting changes, or factual points (in the latter case notably to reflect the further revision in the current account surplus - Mr Bartlett's minute of yesterday refers). The small drafting change to the third sentence of paragraph 5 is suggested because this sort of sentiment usually - at least in the case of the weather - refers to much older records. The deletions suggested in paragraph 10 are to avoid repetition.

3. In paragraph 11, third sentence, the case for deleting the word 'abnormally' before the reference to high US interest rates is that real rates are only marginally higher than in the 1950s so that the word is a bit strong. But we would not press this: the yield curve is pretty abnormal. If retained, it would be more accurate to say 'have been abnormally high ' ...

4. Mr Littler's suggestion on the final sentences of paragraph 11 is/intended in particular to acknowledge that a substantial shift in the value of the dollar has been taking place. We had been going to offer a redraft reflecting the same point, but his was neater.

R G LAVELLE

THE ECONOMIC BACKGROUND

There is now convincing evidence of low inflation and a recovery of output based upon the pursuit of prudent monetary and fiscal policies.

2. Since 1980, inflation has fallen steadily from a peak of over 20 per cent. Last year it was down to 4.6 per cent, the lowest figure since the sixties. And lower inflation has brought lower interest rates.

3. At the same time the underlying strength of the recovery has become widely recognised. Unlike previous cycles this recovery has not come from any self-defeating stimulus to monetary demand but from re-establishing sound finance and honest money. Lower inflation and lower interest rates have produced a better environment for industry and for business and consumer confidence. Recovery has emerged as a result of falling inflation making room for real growth, as we always said it would.

4. Across the economy, total money incomes grew in 1983 by about 8 per cent, of which 3 per cent represented real growth in output. Although there is still room for improvement, this is a very much healthier division between inflation and real growth than we experienced in the 1970s. Output in the second half of 1983 is now reckoned to have exceeded the previous peak in 1979, before the world recession, and is still rising strongly.

5. Productivity has continued to improve at a rapid pace. Just as many have erroneously and prematurely predicted an end to the recovery, so it has been suggested that the sharp rise in productivity remarked on by my predecessor last year was a flash in the pan. Yet during 1983 manufacturing productivity grew by 6 per cent with no sign of slowing down. We saw the smallest annual increase in unit labour costs in manufacturing since these records were first collected fourteen years ago ~~in 1970.~~ It has allowed a welcome and necessary recovery in real levels of profitability. But further progress is needed: although our increase in unit wage labour costs in 1983 was under 3 ~~probably no more than (3)~~ per cent, our three biggest competitors - the US, Japan and Germany - all secured a fall in unit wage ~~labour~~ costs over the latest 12 month period. I welcome the growth in productivity and its contribution to lower unit labour costs, but the employment prospect would be significantly improved if a bigger contribution were to be made by lower pay rises.

6. Demand, output, profits and employment all rose last year. Home demand has played the ~~a~~ major part in the recovery so far. Lower inflation reduced people's need to save and real incomes rose. Personal consumption increased by over 3½ ~~nearly 4~~ per cent compared with 1982. Fixed investment rose rather faster than consumption, with investment in housing and services particularly strong.

7. Imports rose a little faster than home demand last year, as the UK emerged from recession ahead of our main trading partners - our rate of economic growth last year was the

For much of 1983 exports

highest in the European Community. ~~Exports grew less rapidly~~ reflected the weakness in many of our markets ~~than home demand for the same reason~~. However, by the end of last year world trade was clearly moving ahead again and in the three months to January manufacturing exports increased substantially compared with the previous three months. The balance of payments on current account last year is estimated to have been in surplus by about £2½ billion, enabling us to secure a further increase in our income-earning assets overseas.

8. The sharp ~~increase~~ recovery in profitability ~~during the present recovery~~ is particularly welcome, not least because higher profits lead to more jobs. The number of people in employment increased by an estimated 8~~7~~5,000 between March and September last year. The loss of jobs in manufacturing has slowed down sharply, while jobs in services increased by nearly 200,000 in the first nine months of last year. This is encouraging news for the unemployed and those who will be leaving school this summer.

9. Our critics have been confounded by this combination of recovery and low inflation. Even the pessimists have been forced to acknowledge the strength of the recovery and that it is set to continue throughout this year. Inflation is expected to remain low, edging down to 4½ per cent by the end of this year. With rising incomes and low inflation, personal consumption will continue to grow, but the recovery is already becoming more broadly based. Encouraged by higher profitability and better long-term growth prospects, investment is expected to rise by 6 per cent this year.

10. ~~And as world trade expands, there will be increasing opportunities for our exports.~~ World economic prospects are more favourable now than for some time. Output in the United States should continue to grow strongly. And the recovery is spreading to the rest of the world with activity rising in Japan and signs that the long-awaited upturn is at last getting under way in continental Europe. ~~The benefits are beginning to spread to other countries and~~ the pace of world trade is accelerating. British exporters stand to benefit from this recovery.

del

del

11. Of course, there are inevitable uncertainties, and some real risks. The size and continued growth of the United States budget deficit is causing widespread concern, not least within the United States itself. As a direct consequence of its deficit, US interest rates, and thus international interest rates, are [abnormally] high in real terms, impeding the progress of world recovery and exacerbating the problem of the debtor countries. ~~[To finance its massive budget deficit the US has to attract foreign capital on a vast scale, thus producing an artificially strong dollar and a growing balance of payments deficit on current account. But this adds to the pressures for protectionism within the United States now and increases the risks of more volatile exchange rates later.]~~ countries.

? del - or say 'have been' instead of 'are'

Littler redraft

12. A second potential risk is disruption in the oil market. The immediate prospects are less obviously volatile than they were a year ago. But uncertainties remain, and the United Kingdom and the world economy inevitably remains vulnerable to any major disturbances in these markets.

13. But despite these risks there is a growing sense throughout the industrialised world that the recovery this time is not merely cyclical, but one which can be sustained. The essential requirement is the pursuit of prudent monetary and fiscal policies.

14. Certainly, that is the way forward for the UK and the path we intend to take. Inflation has fallen, and is set to fall further. Output has been recovering steadily, and there are sound reasons for expecting this to continue. It can no longer be doubted that steady growth can be combined with falling inflation if the appropriate policies are followed. And with output continuing to rise at an annual rate of 3 per cent in 1984 the outlook for employment should improve still further.

B (84) 797

FROM: T P LANKESTER
7 March 1984

MISS O'MARA

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
PS/C&E

BUDGET SPEECH BLOCK F, PUBLIC SECTOR BORROWING: AND BUDGET SPEECH BLOCK D, THE MTFS

You asked for comments on the drafts circulated under your minute of 6 March.

Block F

2. I would like to suggest a redraft of paragraph 4 (changes underlined):

> "Further progress has been made in reducing interest rates. The latest fall brings base rates to their lowest level for 6 years. It is now necessary to secure a further marked fall in borrowing, so that interest rates can continue their decline as monetary growth slows down. Sterling interest rates are, of course, also influenced by dollar interest rates; but this makes it more, not less, important that domestic pressures are curbed and the extent of the dollar's influence thus minimised. In contrast to virtually the whole of the post-war period, UK longer-term rates are now lower than American rates. As long as American rates remain near their current level, it is highly desirable that this advantage be maintained."

3. Gilt yields fell temporarily below US Treasury bond yields in the third quarter of 1982; they have been below US yields again since the third quarter of 1983. Hence the phrase - "in contrast to virtually the whole of the post-war period...."

4. I have discussed the Chancellor's redraft with Mr Odling-Smee; he has no comments.

Block D

5. Neither Mr Odling-Smee nor I have any comments on this redraft either.

TL

T P LANKESTER

BUDGET SECRET

B (84) 794.

COPY NO. 1 of 23

FINANCIAL SECRETARY TO THE TREASURY

FROM: MISS F P BOGAN
DATE: 7 March 1984

PS/CHANCELLOR
MISS O'MARA

cc Chief Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Lankester
Mr Monger
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
PS/C&E

BUDGET SPEECH BLOCK I: SAVINGS AND INVESTMENT

Your minute of 6 March requested comments by mid-morning.

2. The Financial Secretary has suggested the addition of the words 'or a state index linked pension' after the word scheme on line 7 of paragraph 10: the sentence would then read as follows:

> 'It hits the small businessman who reaches retirement without the cushion of a company pension scheme or a state index linked pension and impedes the creation of farm tenancies.'

FPBogan

MISS F P BOGAN

B(84) 790

BUDGET: SECRET

E 3

FROM: ADAM RIDLEY
7 March 1984

MISS O'MARA

cc PS/CST
PS/FST
PS/MST
PS/EST
Sir P Middleton
Mr Cassell
Mr Monger
Mr R I G Allen
Mr Battishill
Mr Folger
Mr Norgrove
Mr Lord
Mr Portillo

PS/IR
PS/C&E

BUDGET SPEECH

... Your various minutes of March 6 ask for comments. I attach specific drafting proposals. In addition there are two larger issues.

2. First, style. I have long believed that the typical Budget Speech - particularly those of Mr Healey - has tended to sound rather arrogant and egocentric if it is plastered with 'I' everywhere. This draft seems to do so needlessly often, perhaps particularly in the detailed description of measures at the end. So I would urge a major effort to excise as many as is possible.

3. Second, the VAT extension in Block K and income tax allowance changes in Block L. The extension can, I believe, be presented more positively as not regressive, without going as far as denying that the less well-off buy papers, repair homes or eat take-away food. This could be a useful extra theme in K. By the same token one might want to make it clearer in L how far the higher allowances will more than offset the VAT effects, and leave most low and middle income people with higher after-tax earnings. A final point which could be worth making is that social security beneficiaries will get full compensation for the VAT changes as the May RPI up-rating should largely reflect their impact, and the historic system ensures that all their impact will be taken into account as a matter of principle.

AM

A N RIDLEY

BLOCK A

§ 3. One could describe the effects of the MTFS in more favourable terms, for example by an expression like "the fruits of the MTFS....".
And does not the second half of the sentence not imply the recovery has only just started? This could be strengthened on the lines of
"..accompanied for some time by a steady recovery of output and rising living standards and, more recently, by rising employment."

THE ECONOMIC BACKGROUND

§ 2. For the unsophisticated would it not be better to replace 4.6% by "about 4½%"?

§ 3. The last sentence would read better
"Recovery has emerged because falling inflation has made room for real growth..."

§ 7. The point at the end about income earning assets could be reinforced, if one so wished, by referring to the substantial income they generate. As the very recent report on the 1983 Balance of Payments revisions suggest, they are generating a flow of IPD of something like £¾ billion a quarter - or some £3 billions a year.

§ 9. It might help reinforce the good prospects for investment if one added at the end of the last sentence something on the lines of

"...total investment is expected to rise by 6% this year, and by more still in manufacturing".

Provided, of course, we are content with this forecast!

BLOCK D: MTFS

§ 4. The last sentence might read better
"It is therefore assumed, for the purpose of presentation, that the level of real public spending in 1987-8 and 1988-89 is the same as that currently planned for 1986-7."

BLOCK F: PUBLIC SECTOR BORROWING

§ 5. The last phrase reads awkwardly. Should one talk of "any other reduction in net public expenditure"? I would suggest something on the lines of "asset sales reduce the Government's need to borrow just as do reductions in other kinds of public spending. But as a rule they do not help lower interest rates to the same extent."

BLOCK G: PUBLIC SPENDING

§ 2. The reference in the third line to a"steady increase" in the tax burden is not technically correct, as the LTPE paper shows. It may not matter much, but "substantial increase" would be more accurate. Once again, the unsophisticated listener may be bemused by the percentages in the later part of the paragraph, and it would be better to say "with a taxable income of nearly half of average earnings" for 45%; and "under a third of average earnings" for 30%.

§ 4. Is comprehensible to us, but it may be a bit too terse for the ordinary listener. The principal of "finance must determine expenditure" is lurking at the end, but a bit obscurely. And there really seem to be three points struggling to get out. The first that marginal changes are not enough; second that fundamental reviews are needed; and third that these must be constrained by the total that can be afforded. I would be tempted to redraft on the (very rough) following lines.

First, at the beginning of para. 3 write "...what we have seen is a steady and unplanned enlargement of the role of the State...."

Then begin para. 4 "Clearly this dangerous process has to be halted and reversed. That cannot be done sensibly simply by making ad hoc marginal changes in public spending from year to year. Some issues need more fundamental reviews over a longer time scale. Nor can it be done simply by considering the purposes of our various public spending programmes. The programmes which have created this malign result have for the most part been directed to eminently desirable ends. What is clearly essential is that the total impact of the decisions we take about individual programmes should fit in with the best view we can make of what we are likely to be able to afford over the longer term."

BLOCK J: BUSINESS TAXATION

§ 15. The third line does not make it clear that it is deduction against tax which is at issue. Perhaps somethink like the following would be better:

"- allows a company to offset interest paid against that tax in full, but dividends only partially so."

§ 17. The date at the end of the first sentence gets lost. Better would be

"..and £600 million in 1985-6 - made up of...."

§ 18. This gets a bit jargonish. Is one not really saying something like

"I expect these changes to have a somewhat different impact in the short and longer term".? (First sentence)

§ 22. The phrase "a special measure" is over doing it a bit in reference to the VAT registration threshold. Perhaps delete "special"?

§ 40. The reference to the extra £1.2 billion from bringing forward VAT receipts will hit people pretty hard, coming as quickly as it does. Does one not need to say something to indicate that part of this burden will fall on foreign importers; and that much of the rest of it can be met by extension of credit, at a relatively modest cost in terms of extra interest paid? Quite apart from anything else, people would immediately set this very large figure alongside the rather smaller estimates of the costs of the CT measures set out in para. 17.

BLOCK K: PERSONAL AND INDIRECT TAXATION

§ 9. The fourth line from the end reads oddly. Clearly better would be

"higher duty on competing imports".

BLOCK L: INCOME TAX

~~§5. The reference to "every penny I have in hand" is not strictly fair at this stage in the exposition, given that IIS and stamp duty are still to come.~~

§ 6. This seems to underplay the considerable presentational importance of only indexing the upper threshold. The point will be lost on people by the time the first sentence 6 has been spoken, and the listener is deluged with meaningless figures in thousands of pounds.

BLOCK I: SAVINGS AND INVESTMENT

§ 9. The treatment of life assurance relief is very bald. The justification for abolishing it in the second sentence does not carry any conviction. The fact that there may now be other forms of savings open to ordinary people will not appear sufficient reason for eliminating the relief - people will still think it worth giving some encouragement to life assurance. And does one not need to emphasise that with the multiplicity of savings outlets now open to people, what will happen as a result of the change proposed is a reallocation rather than reduction of personal savings, with the money being distributed more sensibly and evenly between the various opportunities open to people?

§ 10. The first sentence may have to stay as it is; but I wonder whether it will not lead to anxiety about pension funds? A minimal change that might help would be to write

"..the abolition of these outdated privileges for institutional investment..."

§ 14. The term composite rate needs to be introduced into the first sentence - e.g. in line 4 - if it is to be referred to crudely at the end of the first sentence.

§ 15. The first sentence is a little obscure. Is one not trying to say

"...the advantage of the present arrangements for taxing Building Societies outweighs the disadvantage"?

§ 17. One needs to make more explicit the assumption relevant to the last sentence that the Revenue would have faced these impossible difficulties if the present tax system were continued. This could be done either by breaking up the sentence; or by a redraft, such as

"...impossible task the Revenue would otherwise have been faced with under the present system were the recent trend..."

B (84) 791

FROM: R A L LORD

DATE: 7 MARCH 1984

cc. PS/Chief Secretary
PS/Financial Secretary
PS/Minister of State
PS/Economic Secretary
Sir P Middleton
Mr Cassell
Mr Monger
Mr R I G Allen
Mr Battishill
Mr Folger
Mr Norgrove
Mr Ridley
Mr Portillo
PS/IR
PS/C&E

MISS O'MARA

BUDGET SPEECH

One or two comments.

BLOCK I

Paragraph 7: Omit 'an exemption I now propose to extend to certain convertible loan stocks'. I believe the Revenue have now withdrawn this proposal since they believe these convertibles are already exempt from stamp duty under the existing law.

BLOCK J

Paragraph 12: Substitute 'most other capital allowances' for 'all'. Enterprise zones will continue to attract 100% capital allowances.

Paragraphs 40 & 41: Now presumably 1st November.

BLOCK K

Paragraph 19: Add 'Taking into account the reductions in income tax which these changes will enable me to make, the effect of personal tax changes as a whole will be to reduce the tax and price index slightly.'

THE ECONOMIC BACKGROUND

Paragraph 1: Substitute 'coupled with' recovery of output.....

Paragraph 5: Omit 'erroneously and'

R A L LORD

BUDGET-SECRET

B(84) 787

FROM: A M W BATTISHILL
DATE: 7 March 1984

MISS O'MARA

cc Mr Norgrove

BUDGET SPEECH

I attach some comments by Mr Norgrove. There are a few more.

2. Section B, paragraph 9, line 6. There is always a problem with Budget speeches about references to "this year" or "next year": cometimes we are talking about calendar years and sometimes about financial years. It is more than usually important to watch out for pitfalls when the Budget comes at the end of the financial year (that then ends in fiscal terms a week or two later). For clarity I would replace "this year" with "1984". We will try to keep an eye open in CU for other problem references of this kind.

3. Block F, paragraph 7, line 7. The phrase "a rather larger tax increase" is perhaps a shade ambiguous. Would it be better to say "to put up taxes even more".

4. Block F, paragraph 8, lines 2 and 3. The piece in the brackets might be though a little disingenuous: indexing income taxes is beneficent whereas indexing specific duties is not, from the taxpayers point of view. Perhaps this is captured better by saying:

> "after allowing for the overall net beneficent effects of indexation"

5. Block G. I notice three omissions from the considerable shortening of this Section. Have the references to public sector manpower, the European Budget and Calke Abbey dropped out intentionally or inadvertently? At an earlier stage the Chancellor was particularly keen on mentioning the third: and there was an alternative suggestion for introducing this alongside the references to capital taxes.

BUDGET-SECRET

6. Block H, paragraph 4, line 3. Those who follow the expenditure versus income argument about taxation might quarrel with the phrase "our entire income-based tax system". The IFS have argued, quite fairly, that our income tax system already contains expenditure-based elements. I suggest removing "entire".

7. Block I, paragraph 9. Once the detailed arrangements for friendly societies are sorted out, there may be a strong case for some mention, however brief, that they are affected too.

8. Block I, paragraph 14, line 13-15. The Revenue will no doubt comment: but it is too much to claim that taxpayers need not return building society interest to the Inland Revenue. It has to go on tax returns: but they are spared (unless they are higher rate payers) the task of accounting for tax on it. I will not second guess likely amendment here from Somerset House. There is much the same flavour about the second half of the first sentence of paragraph 17. There, the formula might be to say:

> "... they will be able to forget about the tax due altogether, since it will have effectively been paid at source".

9. Block J. As drafted, paragraph 4 and 5 may leave the impression that the Chancellor intends to remove many more corporation tax reliefs. The main difficulty is the interaction of "too many special reliefs" (third line of paragraph 4) and "these reliefs" (first line of paragraph 5). My solution would be in the latter reference to say "some unnecessary reliefs".

10. Block J, paragraph 14. The Revenue may hesitate over the references to 1984-85, 1985-86 and 1986-87. Strictly, the references should be to "the financial year 1984" (for the 45 per cent rate), "financial year 1985", and "financial year 1986".

11. Block J, paragraph 28. There is no mention of the indexed increase in the CTT threshold. After "60 per cent" insert "and to raise the threshold to £64,000 in line with indexation."

12. Block J, paragraph 36. I think the last sentence needs to be looked at very carefully by Customs. It goes to the root of the question whether our present arrangements give importers a cash flow advantage over those buying from domestic suppliers. The latter effectively bear VAT at the point when they settle their bills from their suppliers. With trade credit arrangements that may be sooner than some importers, or it may not. Again, I prefer not to second guess the Customs; but the point does need to be expressed very carefully. Similarly, the last sentence of paragraph 38, and the last 5 words in particular, are open to challenge. I would add "straightaway" after "VAT".

13. Block K, paragraph 18. Delete "almost" and substitute "a little over".

14. Block L, paragraph 4, 2 lines from the end. Delete "in December" and substitute "to December".

15. Block L, paragraph 6. The reference to "allowances and thresholds" in the second line is a bit difficult. Only two "allowances" (those for the aged) are going up in line with indexation; numerically, the majority (single allowance, married allowance, single parents' allowance and wife's earnings allowance) are going up by more. I would simply delete the words "allowances and", leaving "thresholds" to cover the aged and higher rate payers.

16. Block L, paragraph 7, penultimate line. For "£2,000" read "£2,005".

17. Block L, paragraph 8. Two points. In the third line delete as unnecessary the words "as a whole". The last sentence is not strictly true. There will be some "tax-paying married couples" whose income lies between the present and the proposed tax thresholds. Some of them will get less than £2 a week. Better to say "practically every" (though again the Revenue may comment too).

AMB

A M W BATTISHILL

... PS I also enclose some comments on Block A from Mr Littler.

B(84) 788

FROM: J.G.LITTLER
DATE: 7 MARCH, 1984

MR. BATTISHILL

BUDGET SPEECH BLOCK A

I imagine you are collating any comments. I have two.

2. As drafted, the last two sentences of paragraph 2 suggest that defeating inflation and achieving stable prices are higher objectives than improving performance, future prosperity, etc. Would it not be better to reverse the two sentences and delete "above all". As a minimum, delete "above all".

3. In the first line of paragraph 5, not just "to reduce" but "to continue reducing" or "to reduce still further".

JGL

(J. G. LITTLER)

632.

BUDGET SECRET

B(84)789

FROM: D R NORGROVE
DATE: 7 MARCH 1984

1. MR BATTISHILL DB

2. MISS O'MARA

BUDGET SPEECH

I offer the following comments on the sections so far circulated.

2. In the Economic Background section, paragraph 2, lower interest rates are attributed to lower inflation. In Block F, paragraph 4 lower borrowing is seen as the requirement for lower interest rates ("... so that interest rates can resume ..."). The two statements can be reconciled, but I suggest amending the last sentence of paragraph 2 of the Economic Background to read: "and lower inflation has contributed to lower interest rates" and the first sentence of Block F to read "... fall in borrowing, in order to help towards a further decline in interest rates as monetary growth slows down".

3. In paragraph 5 of the Economic Background section the phrase "... since records were first collected in 1970" has a touch of bathos about it. (1970 is not very long ago.) This might be helped by substituting the word "figures" for "records".

4. In paragraph 11 of the same section, last line, the reference to "risks of more volatile exchange rates later" is already beginning to be overtaken by events, with the DM ~~down~~ up by well over 10 per cent against the dollar over the past month. I suggest adding "... more volatile exchange rates later, which have indeed started to become reality".

5. In paragraph 4 of Block F the reference to "the dollar's influence" may not be wholly understood. When people talk about the dollar they tend to mean the dollar exchange rate rather than dollar interest rates. It might be worth changing "dollar's" to "overseas".

6. In Block G, paragraph 11, you will be aware of the concern about the possible effect on the sale of BT of references to further sales of other shares in 1984-85. Mr Burgner has offered a redraft.

7. In Block I, paragraph 9, I suggest omitting the reference to advertisements in daily newspapers for tax management schemes, bearing in mind the adverts now appearing headed Budget leak and urging people to take advantage of LAPR before the Budget. The reference in the draft would particularly risk shouts about the Guardian article.

8. The penultimate sentence of the same paragraph says that "existing policy holders will not be affected at all". I do not think this is correct, and have asked the Inland Revenue to consider the point. (People may for example have options under their existing policies to increase the size of their existing policy without a medical examination or to change from a without profits to a with profits policy. Some at least may be caught.) Paragraph 14 in the same block says with the composite rate system the taxpayer is spared the bother of making any return of building society interest he has earned. Paragraph 17 states the main qualification to this, which is that higher rate taxpayers particularly do have to declare their building society interest for tax and of course building society interest has to be declared by those people not in the higher rate bands who happen to have to make a return in any particular year. I suggest amending the sentence to read: "Most taxpayers are spared the bother of making any return of the building society interest they have around ...".

N: See my amendment and comment. AB/

9. Paragraph 16, also in Block I, says that the purpose of the change is not to attract savings into Government hands. I wonder whether that risks an Opposition jeer. It might help to take the phrase "The purpose of the move ... Government hands" to the end of the paragraph.

10. In block J paragraph 22 the increase from £18,000 to £18,700 in the VAT registration threshold is only 3.9 per cent, less than indexation. It is perhaps too strong to claim this as a "special" measure to help small firms.

11. In Block J, paragraph 24, is there a risk that the reference to a second-generation immigrant might sound racist? The point could be put less bluntly (though more long windedly) by referring to the children of immigrants who say they intend to return to their parents' country of origin.

12. The last sentence of paragraph 38 in the same section is a little misleading. We do already charge VAT on imports of course. The sense would not be lost if the phrase "and charge VAT on imports" were dropped.

This is the argument when the Chancellor accepted over taken [illegible] the Red Book.

13. Paragraph 42, also in Block J, says that abolition of NIS will save private sector employers "getting on for £1 billion in 1985-86". This might be compared with the full year figure shown in the FSBR of £865 million and the more astute could realise that the difference between the full year figure and the 1985-86 figure is attributable to the forecast increase in the wage bill between 1984-85 and 1985-86. The difference between £1 billion and £865 million is over 15 per cent and the difference between the accurate figure of £925 million for 1985-86 and £865 million for the full year is 6.9 per cent. Neither would be a welcome deduction for people to make about our forecasts. It would be much safer, even though less dramatic to give a figure of "some £900 million" for 1985-86.

D R Norgrove

D R NORGROVE

PMG

FST proposes redraft of the new Mauger sentence in para 4:

Transactions from today will be able to benefit from the new rate, unless documents have to be stamped before 20 March, which is the date when legal effect can be given to the change.

BUDGET SECRET

B(84) 786

FROM: G W MONGER
DATE: 7 March 1984

MISS O'MARA

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo
Mr Lankester
Mr Allen
Mr Griffiths
Mr Kucyzs IR
Mr Wilmott C&E
PS/IR
PS/C&E

BUDGET SPEECH BLOCK I: SAVINGS AND INVESTMENT

I attach a photocopy of Block I with suggested amendments shown.

2. Most of them explain themselves, but I would add the following points.

a. The Inland Revenue would like to delete paragraph 7. Mr Lankester will propose this in his comments, and I have not included it in mine.

b. The change at the beginning of paragraph 9 is suggested because it is not safe to say that when LAPR was introduced (in the nineteenth century) life assurance was the principal or only savings medium for ordinary people. Other saving through friendly societies was at least as important.

c. The Inland Revenue feel strongly that it would be criticised as misleading not to give, in paragraph 11, the figure for the full year cost of abolishing IIS. I think this is right.

3. The last sentence of paragraph 14 should be amended as follows:
"Most taxpayers are spared the bother of paying tax on interest through PAYE or individual assessment, while the Revenue are spared the need to recruit up to 2,000 extra civil servants in order to collect the tax due on interest paid without deduction."

G W MONGER

4.93.

BUDGET SECRET

CH/EX REF. NO. B(84) 478

FROM: MISS M O'MARA

DATE: 6 March 1984

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
PS/C&E

MR LANKESTER

MR MONGER

BUDGET SPEECH BLOCK I: SAVINGS AND INVESTMENT

I attach Block I of the Budget speech on which the Chancellor worked over the weekend. I should be grateful if comments could reach this office by mid-morning tomorrow.

Mom

MISS M O'MARA

BLOCK I: SAVINGS AND INVESTMENT

First, the taxation of savings and investment.

2. The proposals I am about to make should improve both the direction and quality of savings and investment. And they will contribute further to the creation of a property-owning and share-owning democracy, in which more decisions are made by individuals rather than by intermediary institutions.

3. First, stamp duty. This was doubled from its long-standing 1 per cent by the post-war Labour Government in 1947, reduced by the Macmillan Government in 1963, and once again doubled to 2 per cent in the first Budget presented by the Rt Hon member for Leeds East in 1974. At its present level it is an impediment to mobility and incompatible with the forces of competition which have been unleashed in the City following the withdrawal of the Stock Exchange case from the Restrictive Practices Court.

The change cannot be given legal effect until 20 March but from today most transactions will benefit from the new rate.

4. I therefore propose to halve the rate of stamp duty to 1 per cent [~~on all transactions taking place after today~~].

5. For the home buyer, the new flat rate 1 per cent stamp duty will start at £30,000. Below this level no duty will be payable at all. As a result of this increased threshold, 90 per cent of first time home buyers will not be liable for stamp duty.

6. The reduction in the rate of duty on share transfers will remove an important disincentive to direct investment in equities and increase the international competitiveness of the UK stock market. It should also help British companies to raise equity finance. In addition, I have three proposals to encourage the issue of corporate bonds. I shall go ahead with the new arrangements for deep discount stock and the reliefs for companies issuing Eurobonds in this country which were announced by my Rt Hon and Learned Friend in last year's Budget, but not enacted. And I propose to exempt from Capital Gains Tax
Certain ~~new~~ corporate fixed interest securities that have been held for more than a year.

7. Since such securities are already exempt from stamp duty, an exemption I now propose to extend to certain convertible loan stocks, this means that the tax concessions for Government borrowing in the gilt-edged market will now apply equally to private sector borrowing in the corporate bond market.

8. The reductions in stamp duty will cost £450 million in 1984-85, of which £160 million is the cost of the relief on share transfers and £290 million the cost of the relief on transfers of houses and other real estate.

9. Next, life assurance. I have concluded that there is no longer any justification for ~~life assurance~~ premium relief~~,~~ ~~which was introduced at a time when this provided the principal or only savings medium for ordinary people~~. ~~Its~~ The main effect

of the relief

on life assurance, which is now only one of a number of savings channels for ordinary people.

today is to encourage institutional rather than direct investment, and to spawn a multiplicity of tax management schemes - as anyone reading the advertisements in their daily newspapers can see for themselves. So I propose to withdraw the relief on all new ~~policies with effect from today [13 March]~~ insurances made after today. I stress that this change will apply to new (or newly enhanced) policies only, taken out or increased after today. Existing ~~policyholders~~ policies will not be affected ~~at all~~. The change is estimated to yield £90 million in 1984-85.

X

10. Alongside the abolition of outdated privileges for institutional investment, it is necessary to consider unjustified penalties on direct personal investment. The investment income surcharge is an unfair and anomalous tax on savings and on the rewards of successful enterprise. It hits the small businessman who reaches retirement without the cushion of a company pension scheme and impedes the creation of farm tenancies. In the vast majority of cases it is a tax on savings which have been made out of hard-earned and fully-taxed income in the first place. More than half of those who pay the investment income surcharge are over 65, and of these more than half would otherwise be liable to tax at only the basic rate.

11. I have therefore decided that the investment income surcharge should also be abolished. The cost in 1984-85 will be some £25 million and in a full year around £350m.

12. Finally, I propose to draw more closely together the tax treatment of depositors in banks and building societies. These institutions, which are coming to resemble each other more and more closely, compete in the same market for personal deposits. They should be able to do so on more equal terms.

13. One source of unequal treatment has already been removed, with the recent ruling by the Inland Revenue, on legal advice accepted by Ministers, that under existing law the building societies' profits from gilt-edged securities are liable to tax in ~~exactly~~ the same way as the banks' gilt-edged profits are.

14. But the major source of unequal treatment, against which the banks in particular have consistently complained, lies with the special arrangement for interest paid by building societies under which the societies pay tax at a special rate to the Inland Revenue and the depositor receives credit for income tax paid at the full basic rate. This system, which has worked well for the past 90 years, has both an advantage and a disadvantage. The disadvantage is that a ~~small~~ minority of depositors, who are below the income tax threshold, still suffer the deduction of tax at the composite rate. However, it is always open to such depositors to put their savings elsewhere, such as National Savings. The advantage of the scheme is its extreme simplicity, both for the taxpayer and the Inland Revenue. [The taxpayer is spared the bother of making any return of the building society interest he has earned during the year, and being assessed individually on it; while the Revenue are spared the need to recruit an extra /2,000/ civil servants in order to deal with such assessments].

See minute

15. In common with my predecessors of all Parties over the past 90 years, I am satisfied that the advantage outweighs the disadvantage. It follows that equal treatment between building societies and banks should be achieved, not by removing the composite rate from the societies, but by extending it to the banks and other licensed deposit takers.

16. Non-taxpayers will continue to be able to receive interest gross, should they wish to, by putting their money into appropriate National Savings facilities. But the purpose of the move is not, of course, to attract savings into Government hands: as I have already announced, next year's target for National Savings is the same as this year's and the total Government appetite for savings, which is measured by the size of the Public Sector Borrowing Requirement, has been significantly reduced. Moreover I have decided to reduce substantially the permitted maximum size of future holdings in the National Savings Investment Account and in Income Bonds.

17. The new composite rate arrangements will provide a welcome simplification of the tax treatment of bank interest for individual bank customers: in effect, unless they are higher rate taxpayers, they will be able to forget about it altogether, since all the tax due has effectively been deducted at source. And it will enable the Inland Revenue to make staff savings of up to 1,000 civil servants. Moreover, this figure takes no account of the impossible task the Revenue would otherwise have been faced with were the recent trend towards the payment of interest on current accounts to develop, as it seems highly likely to do.

18. Accordingly, I propose to extend the composite rate arrangements to interest received by UK resident individuals from banks and other licensed deposit takers with effect from 1985-86. The composite rate will not apply either to non-residents or to the corporate sector. Arrangements will also be made to exclude from the scheme Certificates of Deposit of £50,000 or more.

19. Taken together, the major proposals I have just announced on stamp duty, life assurance relief, the investment income surcharge and the composite rate, coupled with other minor proposals, will go a fair way towards providing a simpler and more straightforward tax system for savings and investment, while removing biases which have discouraged the individual saver from investing directly in industry. They also reinforce the Government's policy of encouraging competition in the financial sector, as part of our policy of promoting competition in the economy as a whole.

FROM: M C SCHOLAR

7 March 1984

PS/CHANCELLOR OF THE EXCHEQUER

cc: Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Anson
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo

BUDGET SPEECH BLOCK G: PUBLIC EXPENDITURE

1. You asked for my comments on Block G of the Budget Speech.

2. Paragraph 2 might be strengthened by the addition of a sentence which we considered at the Chancellor's meeting last night, but rejected in this form as being more suitable for a speech than for a Green Paper. "Over the years more and more people on lower and lower incomes have been brought into income tax." It could be added at the end of the existing paragraph 2.

3. In paragraph 4, line 5, I suggest the deletion of "ad hoc". I suggest that the succeeding sentence might be redrafted as follows:

"This choice needs more fundamental consideration; and it needs to be set within a longer time horizon."

I suggest, too, deleting the last sentence, and making its point, in more specific terms, in paragraph 7.

4. For paragraph 7 I suggest the following:-

"The Green Paper concludes that, without firm control over public spending, there can be no prospect of bringing the burden of tax back to tolerable levels. On the assumptions made in the Green Paper, the tax burden will be reduced to the levels of the early 1970s only if public expenditure is held at its present level in real terms right up to 1993-94. If, on the other hand, what by historical standards is a very modest rate of public expenditure growth is assumed - 1 per cent a year in real terms after 1988-89 - the tax burden would be scarcely back to the 1978-79 level even after ten years of growth in the economy at about 2 per cent a year: still less to its level in the 1960s and early 1970s."

5. At the end of paragraph 8 it seems a little Irish to say first of all that price protection is measured by reference to the RPI in May, then to say that accordingly Mr Fowler will be announcing these rates in June. Should we substitute for "in June" the following: "when the May RPI is available, in mid June"?

6. On paragraphs 10 and 11 of the draft you will have seen Mr Burgner's minute of 6 March, with its suggested redraft of this material.

MCS

M C SCHOLAR

B(84)799

FROM: G W MONGER

DATE: 7 March 1984

MISS O'MARA

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
PS/C&E
Mr Allen
Mr Griffiths
Mr Kucyzs IR
Mr Wilmott C&E

BUDGET SPEECH BLOCK H: TAX REFORM

I have only one comment on the redraft of Block H. I think myself that it is a pity not to give more space to the positive general arguments for tax reform. Would it not at least be worth adding a third point in paragraph 2: "Third, the need to reduce the disortions in the tax system, and leave the taxpayer to take more decisions for himself."

G W MONGER

4.93

BUDGET SECRET

CH/EX REF. NO. B(84)476

FROM: MISS M O'MARA

DATE: 6 March 1984

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
PS/C&E

cc Mr Allen

MR MONGER

BUDGET SPEECH BLOCK H: TAX REFORM

I attach Block H of the Budget speech on which the Chancellor worked over the weekend. I should be grateful if comments could reach this office by mid-morning tomorrow.

Mom

MISS M O'MARA

788

BLOCK H: TAX REFORM

As I have already indicated to the House, this will be a radical, tax-reforming, Budget. It will also significantly reduce the overall burden of tax over the next two years taken together - and indeed over the whole MTFS period - although I would hope to have scope for further reductions in tax in subsequent Budgets.

2. My proposals for tax reform are guided by two basic principles. First, the need to make changes that will improve our economic performance over the longer term. Second, the desire to make life a little simpler for the taxpayer.

3. But I am well aware that the tax reformer's path is a stony one. Any change in the system is bound, at least in the short term, to bring benefits to some and disadvantages to others. And, if I may borrow from the vocabulary of the Rt Hon member for Leeds East, the howls of anguish from the latter group tend to be rather more audible than the murmurings of satisfaction from the former.

4. Partly for this reason, I have rejected the extreme suggestion popular in some quarters that I should scrap our entire income-based tax system and replace it with a brand new expenditure-based system. A reform of this kind would produce, in the real world, an upheaval of mind-boggling dimensions.

5. Nor, on the other hand, do I believe we can afford to opt for the quiet life and do nothing. I have therefore chosen the middle course of proposing a number of major tax reforms, but within the framework of our existing income-based system. I shall also be proposing transitional arrangements where I believe it only fair and appropriate to do so.

6. The changes I shall be proposing today fall into three broad categories. These are the taxation of savings and investment, business taxation, and the taxation of personal income and spending.

B(84) 797.

FROM: T P LANKESTER
7 March 1984

MISS O'MARA

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
PS/C&E

BUDGET SPEECH BLOCK I: SAVINGS AND INVESTMENT

Your minute of 6 March.

2. I would like to suggest a redraft of paragraph 6 starting with the third sentence as follows:

> "In addition, I have four proposals to encourage the issue of corporate bonds. I shall go ahead with the new arrangements for deep discount stock and the reliefs for companies issuing eurobonds and convertible loan stock which were announced by my Rt Hon and Learned Friend last year, but not enacted. And I propose to exempt from Capital Gains Tax new [quoted] corporate fixed interest securities that have been held for more than a year."

This redraft includes the reference to the proposal to allow the issuing costs of convertible loan stock against tax. No decision has yet been taken on whether the CGT exemption should cover unquoted as well as quoted securities, hence the square brackets in the last sentence. The Financial Secretary is taking a meeting on this tomorrow morning.

3. I suggest paragraph 7 should be redrafted as follows (changes

underlined):

> "Since such securities are already exempt from stamp duty, an exemption I can confirm also extends to certain convertible stocks, this means that the tax concessions for Government borrowing in the gilt edge market will now be virtually the same as for private sector borrowing in the corporate bond market."

4. The exemption from stamp duty of loan stock convertible into equities is a clarification by the Revenue of the 1976 Finance Act, although it will be announced in a press release on Budget day. So I think it would be wrong to suggest that this is a "Budget measure". Hence the phrase "I can confirm also....."

5. The tax treatment of gilt edged borrowing and borrowing in the corporate bond market will not be precisely the same, even after the new concessions, because deep discount bonds will be taxed on an income accrual basis whereas low coupon gilts, at least for individuals, are subject to a capital gains regime. But this is a minor point, and the Chancellor may prefer to stick to his earlier draft.

6. There is no mention in this section, or as far as I know in any other part of the speech, of the proposal to extend the allowance of ~~allow~~ the discount on acceptance credits against corporation tax. But this was announced last year, it is a pretty small item, and it does not fit easily in this section; so it may be best not to mention it in the speech.

7. I would prefer to delete the last part of the penultimate sentence of para 16. The sentence could then finish as follows: "... as I have already announced, next year's target for national savings is the same as this year's and the year before."

8. Without the deletion, we will be explicitly admitting that the £3 billion target will be a higher proportion of the borrowing requirement.

9. Mr Monger will be letting you have comments on other paragraphs in this block.

T P LANKESTER

BUDGET SECRET

B(84)798

FROM: G W MONGER

DATE: 7 March 1984

MISS O'MARA

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgove
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
PS/C&E
Mr Allen
Mr Griffiths
Mr Kucyzs IR
Mr Wilmott C&E

BUDGE SPEECH BLOCK L: PERSONAL TAXATION/INCOME TAX

We have only the small amendments to this Block shown on the attached photocopy.

2. I have square bracketted "greatly" in paragraph 5 because the poverty trap can reach 60-70% even where no tax is paid. But if the Chancellor wanted to leave in "greatly" I think it could be defended.

3. There are three points on the important last sentence of paragraph 8:

i. Unfortunately, it has to be amended as shown to exclude pensioners.

ii. Arguably, there should also be an exclusion for those only just above the present threshold, who already pay less than £2 a week in tax. But the absence of a reference to them could be justified on the ground that they clearly cannot get a cut of £2.

iii. Mr Folger has pointed out that those losing the foreign earnings or emoluments reliefs could suffer substantial losses. This is true, but I think myself that paragraph 8 is fairly clearly referring to the effect of the allowance changes.

G W MONGER

CH/EX REF. NO. B(84) 480

FROM: MISS M O'MARA

DATE: 6 March 1984

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
PS/C&E

MR MONGER

BUDGET SPEECH BLOCK L: PERSONAL TAXATION/INCOME TAX

I attach Block L of the Budget speech on which the Chancellor worked over the weekend. I should be grateful if comments could reach this office by mid-morning tomorrow.

MOM

MISS M O'MARA

BLOCK L: PERSONAL TAXATION/INCOME TAX

Finally, I come to income tax.

2. Since we took office in 1979, we have cut the basic rate of income tax from 33 per cent to 30 per cent and sharply reduced the punitive higher rates inherited from the last Labour Government. We have increased the main tax allowances not

around) simply in line with prices but by almost 8 per cent in real

X

terms. It is a good record. But it is not enough. The burden of income tax is still too heavy.

3. During the lifetime of this Parliament, I intend to carry further the progress we have already made. For the most part, this will have to wait for future Budgets, particularly since I have thought it right this year to concentrate on setting a new regime of business taxation for the lifetime of a Parliament - and beyond. But as a result of the measures I have just announced on indirect taxes I can make a start.

4. I propose to make no change this year in the rates of income tax. So far as the allowances and thresholds are concerned, I must clearly increase these by the amounts set out in the statutory indexation formula, based on the 5.3 per cent

to) increase in the Retail Price Index ~~in~~ December. The question is how much more ~~than this~~ I can do.

X

5. I have decided that, this year, the right course is to use every penny I have in hand, within the framework of a revenue neutral Budget, to lift the level of the basic tax thresholds, for the married and single alike. It is fundamentally wrong that people should pay income tax on incomes so low that they are entitled to social security benefits on grounds of need. Moreover low tax thresholds greatly exacerbate the poverty and unemployment traps, so that the incentive to find a better job or even any job at all may virtually cease~~s~~ to exist. There is, alas, no quick or cheap solution to these problems, but that i~~t~~s all the more reason to make a start on solving them now.

6. Accordingly, I propose to increase the bulk of the allowances and thresholds strictly in line with the statutory requirement. The first higher rate of 40 per cent will apply when taxable income reaches £15,400 a year and the top rate of 60 per cent to taxable income of £38,100 or more. The single age allowance will rise from £2,360 to £2,490 and the married age allowance from £3,755 to £3,955.

7. For the basic thresholds statutory indexation would mean putting the single and married allowances up by £100 and £150 respectively. I am glad to say that, as a result of the measures I have already announced, I can do considerably better than that. In short, I propose to increase the basic thresholds by well over double what is required by indexation. The single person's threshold will be increased by £220, from £1,785 to £2,00~~0~~5; and the married threshold by £360, from £2,795 to £3,155.

(some) 8. This is an increase of around 12½ per cent, or ~~more than~~ 7 per cent in real terms. It brings the married man's tax threshold, for 1984-85 X ~~as a whole~~, to its highest level in real terms since the war. It means that every tax-paying married couple in the land (of working age) will enjoy an income tax cut of at least £2 a week.

9. The changes I have announced will also take a large number of people, those with the smallest incomes of all, out of income tax altogether. Some 850,000 fewer people will pay tax in 1984-85 than if thresholds had not been increased at all, and 400,000 fewer than if the allowances had merely been indexed.

10. All these changes will take effect under PAYE on the first pay day after 10 May. Their cost is considerable: some £1.8 billion in 1984-85, of which roughly half represents the cost of indexation.

11. This is as far as I can go on income tax this year, and still produce a broadly revenue-neutral Budget for 1984-85. But as I have already said, so long as we hold to our published planned levels of public spending, there is an excellent prospect of further income tax cuts in next year's Budget. This is in addition to the fact that, as I told the House earlier, the measures I have announced in this Budget will reduce taxation in 1985-86 by some £1¾ billion.

B(84) 503.

BUDGET SECRET

FROM: N MONCK
DATE: 7 March 1984

PS/CHANCELLOR

cc Sir P Middleton
Sir T Burns
Mr Battishill
Mr Monger
Mr Folger
Mr Portillo

BLOCK J: BUSINESS TAXATION

Paragraphs 2 and 3 substitute "business" for "industry". "Industry" is too close to manufacturing which, on our present figures which we are checking, is likely to lose in cash terms even on a 2 year basis.

2. Paragraph 11. Following last night's meeting between the Chancellor and Mr Tebbit I suggest the following sentences, which I will need to check later with DTI and the Revenue:

X "After consulting my rt hon Friend the Secretary of State for Trade and Industry, I have decided to make transitional tax arrangements for certain investment projects in the regions. Existing capital allowances will continue to apply to expenditure on projects in Development Areas and special Development Areas for which regional development grants are available and offers of selective assistance have already been made between 1 April 1980, and today. Similar arrangements were announced for regional development grants in my rt hon Friend's White Paper on Regional Industrial Development last December." X

3. Paragraph 13 third line from end: I suggest extending the sentence to read

> "............. inflation has fallen sharply and will be falling further during this Parliament."

I think the last sentence should go but the Revenue will comment on that.

4. Paragraph 18. If the short-term acceleration of investment is to be made explicit and not held in reserve for defence against questions about the quantity of investment, I think it ought to be made more clearly

subordinate to the longer term quality effects. In the sixth line from the end the sentence might begin:

"But the more important and durable effect will be to encourage ....".

5. Paragraph 19 might be a place for a short reference for the reasons why higher net profitability are a good thing. Viz the greater willingness of business to spend and take risks in an enterprising way. I suggest something on the lines of:

"Higher net profits should encourage and reward enterprise and stimulate higher current expenditure and innovation in all its forms - research and development and work on new products, processes and markets."

6. Paragraph 38 line two insert after "competitive disadvantage" "in the home market". The opponents of earlier payment of VAT on imports will argue that their competitiveness has been reduced in export markets. The answer to that is that they will be in the same position as their opposite numbers in EEC countries. But we do not want to look as though we have missed the point.

PP. S. Lelauber
N MONCK

BUDGET SECRET

B(84) 796

FROM: G W MONGER
DATE: 7 March 1984

MISS O'MARA

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
PS/C&E
Mr Allen
Mr Griffiths
Mr Kuczys -IR
Mr Wilmott -C&E

BUDGET SPEECH BLOCK K: PERSONAL TAXATION/INDIRECT TAXES

I have not yet had Customs & Excise comments on this block but in view of your deadline I am sending it forward now. Customs and Excise may wish to comment later. Answers to the detailed question in paragraphs 12, 15 and 16 will need to come from them.

2. Some small amendments are shown on the attached photocopy.

<u>1979 Manifesto (para 2)</u>

3. The full reference in the 1979 Manifesto was as follows:

> ["Growing North Sea oil revenues and reductions in Labour's public spending plans will not be enough to pay for the income tax cuts to country needs.] We must therefore be prepared to switch to some extent from taxes on earnings to taxes on spending."
> (1979 Manifesto, page 14)

I suggest after "elected in 1979" adding the words "...and which emphasised the need for some switch from taxes on earnings to taxes on spending."

Lollipops

4. Paragraph 8 already mentions one lollipop. It might be worth referring to the two others agreed in this area. Add after paragraph 8:

> "I also propose to extend the concessionary duty rate of £60 paid on small horsepower cars registered before 1947 to all cars registered before that date."

5. Then perhaps as a new paragraph after 17 there could be inserted the following:

> "I have one further measure to propose to assist disabled people. I propose to relieve from VAT and car tax cars designed or adapted to take a wheelchair or stretcher for disable persons."

This also could be inserted in paragraph 8. But the other two lollipops in paragraph 8 deal with VED, whereas this does not, and it would make more of it to give it a separate paragraph.

Beer/wine judgement (paras 9-10)

6. I am not certain about the tactic of emphasising that we are taking the action on beer/wine because we have to obey the judgement of the Curopean Court. This is however a matter of political judgement. I wonder however whether the Chancellor might consider replacing "I am now obliged to implement" by "I am now implementing". The word "obliged" seems to convey expecially strongly the impression that the Europeans are telling us what to do.

Future VAT changes

7. Mr Knox suggested with his minute of 2 March an additional paragraph designed to leave open the possibility of further extensions of the VAT base. The Chancellor has now however reduced the length of this block of the speech and I take it that he would not now want to make additions to cover this point. If he does not, I think that paragraph 2 and 14 are in fact sufficient to safeguard the position, although a briefing line will need to be developed to answer the explicit question whether more VAT changes are contemplated.

G W MONGER

4.95

BUDGET SECRET

CH/EX REF. NO. B(84) 479

FROM: MISS M O'MARA
DATE: 6 March 1984

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
PS/C&E

MR MONGER

BUDGET SPEECH BLOCK K: PERSONAL TAXATION/INDIRECT TAXES

I attach Block K of the Budget speech on which the Chancellor worked over the weekend. I should be grateful if comments could reach this office by mid-morning tomorrow.

Moira

MISS M O'MARA

BLOCK K: PERSONAL TAXATION/INDIRECT TAXES

I have announced major reforms of both the taxation of savings and investment and the taxation of businesses. The third and final area in which I propose to make progress on tax reform is the taxation of personal income and spending.

2. The broad principle was clearly set out in the Manifesto on which we were first elected in 1979. /Quote from 1979 Manifesto/ My predecessor made an important move in this direction in his first budget, and the time has come to make a further move today. A change of this kind is important in two ways. It improves incentives and makes it more worthwhile to work, and it increases the freedom of choice of the individual.

See covering minute

3. I do not however see the excise duties as an area for major change this year. I shall of course need to raise the duties broadly in line with inflation, so as to maintain their real value: not to do so would run counter to the philosophy I outlined a moment ago. But broadly speaking I do not intend to do any more than revalorise the excise duties, and with inflation now as low as it is, the necessary increases are mercifully modest.

4. I propose an increase in the tobacco duty which, including VAT, will put 4p on the price of a packet of

cigarettes, with corresponding increases for hand-rolling tobacco and cigars. But I do not propose to increase the duty on pipe tobacco, which is important for a great many pensioners. These changes will take effect from midnight on Thursday.

5. I propose increases in the duties on petrol and derv which, again including VAT, will increase the price at the pumps by 4½p and 3½p a gallon respectively. I do not propose to increase the duty on heavy fuel oil, which is of particular importance to industrial costs. These changes will take effect for oil delivered from refineries and warehouses from six o'clock this evening.

6. There is one excise duty which I propose to do away with altogether. Many of those who find it hardest to make ends meet, including in particular many old age pensioners, use paraffin stoves to heat their homes. Accordingly, I propose to abolish the duty on kerosene from six o'clock this evening. I am sure that this will be welcomed on all sides of the House.

7. The various rates of Vehicle Excise Duty will, once again, go up roughly in line with prices. Thus the duty for cars and light vans will be increased by £5, from £85 to £90 a year. However, given the further evidence my Rt Hon Friend the Secretary of State has now received on the

contribution that various types of vehicle make to the wear and tear caused to the roads, there will be reductions in duty for the lightest lorries, offset by higher increases for some heavier lorries. All these changes in Vehicle Excise Duty will take effect from tomorrow.

8. In addition, however, I propose to exempt from Vehicle Excise Duty all recipients of the War Pensioners' Mobility Supplement.

9. I now come to the most difficult decision I have to take in the excise duty field. As the House will be aware, the rules of the European Community, so far as alcoholic drink is concerned, are designed to prevent a Member state from protecting its own domestic product by imposing a significantly higher duty on imported competitors, the comparison being made broadly on the basis of relative alcoholic content. In pursuit of this, the Commission has taken a number of countries to the European Court of Justice.

10. In our case, the Commission contended that we were protecting beer by under-taxing it in relation to wine. We fought the case, but lost; and I am now obliged to implement the judgement handed down by the Court last year. Accordingly, I propose to increase the duty on beer, not by the 7p a pint which has been widely rumoured in the press, but by the minimum amount ~~needed~~ to comply with the judgement: 2p on

required, taking account of the need for revenue, a typical pint of beer, including VAT. At the same time, the duty on table wine will be reduced by the equivalent of about 18p a bottle, again including VAT.

11. I cannot, however, ignore the fact that while we comply with the judgement of the European Court, one of our partners appears determined not to do so. I refer to Italy, which has been clearly ordered by the Court to remove its discrimination against Scotch whisky forthwith, and shows no sign whatever of complying. I have therefore decided to introduce a temporary duty surcharge on vermouth of some 20p a bottle on top of the regular revalorisation increase. This surcharge will come into operation on 1 September unless the Italian Government has - as I very much hope - implemented the Court's judgement by that date, and it will lapse as soon as I am satisfied that it has complied.

12. As for the rest of the alcoholic drinks, cider, which increasingly competes with beer but attracts a lower duty, will go up by 3p a pint. The duties on made-wine will be aligned with those on other wine. And I propose to increase the duty on sparkling wine, fortified wine and spirits by about 10p a bottle, including VAT. [When to come into force?]

13. These changes in excise duties will, all told, bring

broadly in some £650 million in 1984-85. But that is of course ~~merely~~ what is needed to keep pace with inflation.

14. The extra revenue I need to make the switch this year from taxes on earnings to taxes on spending must therefore come from VAT. I propose no change in the rate of VAT. Instead, I intend to broaden the base of the tax by extending the 15 per cent rate to three areas of expenditure that have hitherto been zero-rated.

15. First, alternations to buildings. At present repairs and maintenance are taxed, but alternations are not. The borderline between these two categories is the most confused in the whole field of VAT. [An example?] I propose to end this confusion, not to mention the illogicality of the difference, by bring all alterations into tax. However, to allow a reasonable time for existing commitments to be completed or adjusted, the change will be deferred until 1 June.

16. Second, I propose to bring into tax newspapers (including newspaper advertisements) and all other pirnted matter, with the sole exception of books, which will remain zero-rated. Other news media, of course, are already subject to tax. [Check] This change will apply from 1 April.

17. Third, food. Most food is zero-rated. But food served in restaurants, and a miscellaneous range of items including ice-cream, confectionery, soft drinks and crisps were brought

into tax by the Rt Hon Member for Leeds East. Take-away food clearly competes with these forms of catering, and I therefore intend to bring into tax hot take-away food and drinks, with effect from 1 May.

18. The total effect of the extensions of the VAT coverage which I have proposed will be to increase the yield of the tax by £600 million in 1984-85 and by almost £1 billion in 1985-86.

19. The total impact effect on the Retail Price Index of the VAT changes and excise duty changes taken together will be three-quarters of one per cent. This has already been taken into account in the forecast I gave to the House earlier of a decline in inflation to 4½ per cent by the end of the year.

/̄20. The revenue raised by the broadening of the VAT base will enable me to lighten the burden of income tax, within the overall framework of a neutral Budget./

5-12

Mr Kerr

You will see that the shortest speech is considered to be Benjamin Disraeli's in 1867, lasting 45 mins. P.J. Edwards 12/3

FROM N G FRAY
DATE: 7 MARCH 1983

PMP

PS/CHANCELLOR (MISS RUTTER)

C.

We shall not beat him.

JOL.

cc Minister of State (C) (for paragraph 1
Sir Douglas Wass
Mr Burns
Mr Middleton
Mr Kemp
Mr Norgrove

LENGTH AND DURATION OF BUDGET SPEECHES

As you asked I have carried out some more research into the length and duration of Budget Speeches given by Mr Lloyd George, Mr Churchill and Mr Butler. The results are attached immediately below.

2. With regard to the contents of the various speeches and general points of interest, I also attach a note consolidating all the research that I have carried over the past few months There is some repetition from minutes previously circulated, but the idea is to collect all the information together.

N G FRAY

	LENGTH	DURATION
LLOYD GEORGE		
29 April 1909	MISSING	
30 June 1910	7500	1 hr 10
16 May 1911	MISSING	
2 April 1212	7750	1 hr

Both speeches above include many interruptions

Average:130.w.p.m. (approx)

	LENGTH	DURATION
CHURCHILL		
28 April 1925	16200	2 hrs
26 April 1926	13700	1 hr 40
11 April 1927	16000	2 hr
24 April 1928	20250	2 hr 15
15 April 1929	15500	1 hr 45

Average:140 w.p.m. (approx)

	LENGTH	DURATION
BUTLER		
11 March 1952	13850	1 hr 25
14 April 1953	11350	1 hr 10
6 April 1954	12200	1 hr 15
19 April 1955	11250	1 hr 10

Average:162 w.p.m.

THE GENERAL DEVELOPMENT OF THE BUDGET SPEECH

The Budget speech has progressed from being mainly a very detailed and technical discussion of taxation and borrowing, to the Budget Speech we know today.

Length of the Speech

2. The length of Budget speeches varies enormously. An analysis is shown in Annex A. The longest Budget speech was given by Sir William Gladstone on 18 April 1853 - it lasted approximately 4¾ hrs. The then Leader of the Opposition said of the speech: "... it was so extensive that it is impossible, without consideration, to weigh its disadvantages and advantages."

3. However many of the speeches given at the end of the last century and into this were very often on the short side. The main reason for this was because the Budget was directed only at expenditure and revenue. They also seem to have been spoken more slowly.

4. There are several contenders for the shortest speech: Benjamin Disraeli delivered a speech in 1867 lasting approximately 45 minutes. A speech of similar length was given by Mr R Lowe on 7 April 1873. However the shortest Budget speech ever may have been the one delivered by Sir Mark Hicks Beach on 5 March 1900 at 35 minutes.

5. The Budget speech given by Mr C Ritchie on 23 April 1903 appears to be the first speech which has defined sections and can I think be justified as being the first truly 'modern' Budget speech because it dealt with a greater variety of subjects rather than being confined purely to expenditure and revenue. The structure of this speech is given with a selection of others at Annex B.

The Speech itself

6. The speech as we know it today has only been termed the 'Budget Statement' for just over 20 years. Previously it was called 'Budget Proposals' and from the turn of the century back into history was called the 'Financial Statement'.

7. Up until 1968, the Budget was presented before a Committee of the House. At Roy Jenkins' Budget Speech on 19 March 1968, the Speaker was present for the first time at an annual Budget Statement. It was also the first time that taxation proposals had been initiated in the whole House since 7 May 1641.

8. The 7 May 1908 speech was a rare occasion, when Mr H H Asquith presented the Budget as Prime Minister, to which office he had succeeded on the 8 April on the retirement of Sir Henry Campbell-Bannerman. It was the first time in living memory that the annual financial statement had been submitted by any other Minister than the Chancellor of the Exchequer (though the Financial Statement had been presented in this way in the times of Sir Robert Peel). The reason for this unusual occurrence was that the Ministerial changes had only taken place on 8 April and the new Chancellor of the Exchequer (Mr Lloyd George) felt that it would be a matter "not merely of personal, but also of public convenience" that Asquith should present the Financial Statement as he had previously held the post of Chancellor.

9. The arrangement worked well because the Financial Statement of 1908 was a natural progression from the Statement delivered by Asquith the previous year. The Budget of 1908 was to announce the establishment of a scheme of old age pensions and was therefore the first stage of Asquith's "social reform" which he had set in hand a year earlier.

Civil Service Numbers

10. A final point to note is that in 1928, when Winston Churchill was Chancellor of the Exchequer, the Conservative Party, like today, wanted to reduce the numbers employed in the Civil Service. From the time the Conservatives took office in 1924 up to 1 April 1927, the total number of officials in the Civil Departments had been reduced by over 7,000 (a reduction of perhaps 10 per cent by my calculation). The scheme mentioned by Churchill in his Budget in 1928, contemplated a 5 year programme beginning from 1 April 1927 to reduce the number of officials by a further 11,000 (18 per cent of those in post in the Civil Departments at that time). The reductions were needed to save money to finance the ever increasing cost of housing grants and pensions.

5-16

ANNEX A

LENGTH AND DURATION OF BUDGET SPEECHES

Listed below are some of the longest and shortest Budget speeches made since 1853

CHANCELLOR	APPROX NO OF WORDS	DURATION	AVERAGE W.P.M.
Sir Geoffrey Howe			
9 March 1982	18,200	1 hr 45	
10 March 1981	14,500	1 hr 30	164
26 March 1980	19,000	2 hr	
12 June 1979	11,500	1 hr 10	
Denis Healey			
11 April 1978	9,500	1 hr	152
26 March 1974	20,500	2 hr 20	
Anthony Barber			
6 March 1973	18,00	2 hr	146
30 March 1971	15,500	1 hr 50	
Roy Jenkins			
14 April 1970	17,000	1 hr 55	151
19 March 1968	20,000	2 hr 10	
James Callaghan			
3 May 1966	13,000	1 hr 20	160
6 April 1865	22,000	2 hr 20	
Reginald Maudling			
14 April 1964	13,000	1 hr 30	149
3 April 1963	17,000	1 hr 50	
Selwyn Lloyd			
9 April 1962	14,000	1 hr 30	160
17 April 1961	13,000	1 hr 20	
Derick Heathcoat Amory			
4 April 1960	13,000	1 hr 20	163
Harold Macmillan			
17 April 1956	15,000	1 hr 45	143
R A Butler			
19 April 1955	11,250	1 hr 10	162
11 March 1952	13,850	1 hr 25	
Sir Stafford Cripps			
18 April 1950	18,000	2 hr	150
W S Churchill			
15 April 1929	15,500	1 hr 45	140
28 April 1925	16,200	2 hr	
D Lloyd George			
2 April 1912	7,750	1 hr	130
30 June 1910	7,500	1 hr 10	
Benjamin Disraeli			
4 April 1867	6,500	45 mins	144
Sir William Gladstone			
18 April 1853	35,000	4 hr 45	123

ANNEX B

STRUCTURE OF SPEECHES

SIR GEOFFREY HOWE: 9 MARCH 1982

I INTRODUCTION
II MONETARY POLICY
- MONETARY CONTROL AND DEBT SALES
III PUBLIC SECTOR BORROWING
IV PUBLIC EXPENDITURE
V SOCIAL SECURITY AND CHARITIES
VI MANAGING THE PUBLIC SECTOR
- CIVIL SERVICE
- THE NATIONALISED INDUSTRIES
VII NATIONAL INSURANCE SURCHARGE
VIII INDIRECT TAXES
IX OIL TAXATION
X INDUSTRIAL ENERGY COSTS
XI INDUSTRIAL INNOVATION
XII FISCAL JUSTICE
- TAX HAVENS AND COMPANY RESIDENCE
XIII THE CONSTRUCTION INDUSTRY
XIV BUSINESS, ENTERPRISE AND SMALL FIRMS
XV CAPITAL TAXES
XVI INCOME TAX
XVII CONCLUSION

ROY JENKINS: 19 MARCH 1968

I INTRODUCTION
II EXTERNAL POSITION
- PROSPECTS FOR 1968-69: CURRENT ACCOUNT
- PROSPECTS FOR 1968-69: THE CAPITAL ACCOUNT
III THE BUDGET JUDGEMENT
IV GOVERNMENT FINANCE: OUTTURN AND PROSPECTS
- THE FINANCIAL STATEMENT
- 1967-68 PROVISIONAL OUTTURN
- 1968-69 PROSPECTS
- CENTRAL GOVERNMENT NET BALANCE
V MONETARY POLICY
VI TAX CHANGES
VII TAX CHANGES: CUSTOMS AND EXCISE
VIII TAX CHANGES: OTHER INDIRECT TAX CHANGES
IX TAX CHANGES: DIRECT TAXATION
X TAXATION OF BENEFITS FROM OWNERSHIP
XI CONCLUSIONS

SELWYN LLOYD: 17 APRIL 1961

I EXCHEQUER OUTTURN
II PUBLIC EXPENDITURE
III THE UK ECONOMY 1960-61
IV ECONOMIC PROSPECTS FOR 1961-62
V DOMESTIC DEMAND
VI LONGER TERM ISSUES
VII SIMPLIFICATION OF THE TAX SYSTEM
VIII ECONOMIC REGULATORS
IX EXCHEQUER PROSPECTS FOR 1961-62
X ALLOWANCES FOR NI CONTRIBUTIONS
XI TAX CHANGES
XII CONCLUSIONS

HARDOLD MACMILLAN: 17 APRIL 1956

I BALANCE OF PAYMENTS
II INTERNATIONAL SITUATION
III MONETARY POLICY
IV EXCHEQUER OUTTURN 1955-56
V NATIONAL DEBT
VI EXCHEQUER PROSPECTS
VII FINANCE FOR THE NATIONALISED INDUSTRIES
VIII ECONOMIC PROSPECTS 1956-57
IX SAVINGS
X SAVINGS CERTIFICATES AND DEFENCE BOND
XI SAVINGS BANK DEPOSITS
XII RETIREMENT PROVISIONS FOR THE SELF EMPLOYED
XIII STAMP DUTY ON CONVEYANCES
XIV PREMIUM BONDS
XV GOVERNMENT EXPENDITURE
XVI CHANGES IN THE TAX CODE
XVII MAJOR TAX CHANGES

R A BUTLER: 19 APRIL 1955

I INTRODUCTION
II BALANCE OF PAYMENTS
III THE MEASURES OF 24 FEBRUARY*
IV OUTTURN FOR 1954-55
V REVENUE IN 1954-55
VI EXPENDITURE IN 1954-55
VII OUTTURN IN 1954-55
VIII NATIONAL DEBT
IX NATIONAL SAVINGS
X REVENUE FOR 1955-56
XI EXPENDITURE FOR 1955-56
XII SUPPLY EXPENDITURE
XIII CIVIL EXPENDITURE
XIV EXCHEQUER PROSPECTS ON EXISTING BASIS OF TAXATION
XV EXTERNAL PROSPECTS
XVI HOME PROSPECTS
XVII BUDGET JUDGEMENT
XVIII BUDGET PROPOSALS

*Action taken to moderate the growth of imports and to encourage exports, including an increase in the Bank Rate by 4½ per cent.

SIR STAFFORD CRIPPS: 15 APRIL 1950

I DEMOCRATIC PLANNING
II EXTERNAL ECONOMIC SURVEY
III GOLD AND DOLLAR POSITION
IV EUROPEAN ECONOMIC CO-OPERATION
V OUTTURN FOR 1949-50
VI PROSPECTS ON BASIS OF EXISTING TAXATION
VII BASIS OF BUDGET POLICY
VIII TAX: MINOR PROPOSALS
IX TAX: MAJOR PROPOSALS

W S CHURCHILL: 11 APRIL 1927

I INTRODUCTION
II EFFECTS OF THE GENERAL STRIKE AND COAL TRADES DISPUTE
III REVENUE 1926-27
IV EXPENDITURE 1927-28
V GENERAL REVIEW OF EXPENDITURE
VI POST-WAR GOVERNMENT DEPARTMENTS
VII REVENUE 1972
VIII DEBT POSITION
IX SINKING FUND POLICY
X SIMPLIFICATION OF INCOME TAX
XI TAX ADVOIDANCE
XII MINOR PROPOSALS
XIII TRANSLUCENT POTTERY (CUSTOMS DUTY)
XIV IMPORTED MOTOR TYRES (CUSTOMS DUTY)
XV IMPORTED SENSITISED CELLULOID FILM
XVI MATCHES (REVISED DUTIES)
XVII WINES (CUSTOMS DUTIES)
XVIII BRITISH WINES (EXCISE DUTIES)
XIX TOBACCO (INCREASED DUTIES)
XX RAOD FUND RESERVE
XXI BREWERS CREDIT
XXII FINAL BALANCE SHEET

D LLOYD GEORGE: 30 JUNE 1910

I INTRODUCTION
II GROWTH OF EXPENDITURE
III REVENUE - ARREARS OF REVENUE FOR 1909-10
IV REVENUE FOR 1910-11 - TRADE OUTLOOK
V CUSTOMS DUTY - SPIRIT DUTY
VI MORAL EFFECTS OF THE DUTY
VII OTHER CUSTOMS DUTIES
VIII EXCISE DUTIES
IX DEATH DUTIES
X STAMP DUTIES
XI INCOMES TAX AND SUPER TAX
XII LAND VALUE DUTIES
XIII NON-TAX REVENUE
XIV TOTAL REVENUE AND SURPLUS
XV RELIEF TO LOCAL AUTHORITIES
XVI OLD AGE PENSION PAUPER DISQUALIFICATION
XVII FUTURE LIABILITIES
XVIII UNEMPLOYMENT AND INVALIDITY INSURANCE
XIX FINANCIAL PROSPERITY

BROADCASTING OF PARLIAMENT (ANNUAL REVIEW)

Dr. Edmund Marshall accordingly presented a Bill to provide for the annual review of arrangements for the broadcasting of parliamentary proceedings: And the same was read the First time; and ordered to be read a Second time upon Friday 15 April and to be printed. [Bill 100.]

BUDGET 1983

WAYS AND MEANS

Budget Statement

Mr. Deputy Speaker (Mr. Bernard Weatherill): Before I call the Chancellor of the Exchequer, it may be for the convenience of hon. Members if I remind them that, at the end of the Chancellor's speech, as in past years, copies of the Budget resolutions will not be handed around in the Chamber but will be available to hon. Members in the Vote Office.

3.38 pm

INTRODUCTION

The Chancellor of the Exchequer (Sir Geoffrey Howe): The longest Budget speech that I have been able to trace was given by Mr. Gladstone on 18 April 1953—*[Interruption.]*

Mr. Deputy Speaker: Order. Perhaps the Chancellor would like to start again.

Sir Geoffrey Howe: I am content, Mr. Deputy Speaker, to recognise that, although Liberals have long lives, they do not live that long. The date to which I refer, of course, was 1853. The speech lasted for about 4¾ hours. The then Leader of the Opposition said of the speech:

"... it was so extensive that it is impossible, without consideration, to weigh its disadvantages and advantages".

That could have its merits in certain circumstances. But I can assure the House that I shall not try to rival Mr. Gladstone. Instead, I shall try to follow Disraeli, who delivered a Budget speech in 1867 lasting only 45 minutes. I am afraid that I cannot quite match that; but at least this will be one of the shortest—perhaps the shortest—of my Budget speeches, or at any rate the shortest so far. And that will not be its only attractive feature.

I begin, as last year, by making it clear that I shall today be proposing further significant cuts in the taxes paid both by businesses and by individuals. These proposals will be consistent with our medium term strategy for effective control of the money supply, for lower public borrowing, and for further progress on inflation.

The requirement we saw, and the country accepted, in 1979, was for resolve, for purpose and for continuity. My proposals in this Budget are rooted in that same resolve, and will maintain that purpose, and that continuity. They are designed to further the living standards and employment opportunities of all our people and to sustain and advance the recovery for which we have laid the foundations.

WORLD ECONOMY

In 1979 it was clear that the long-term decline of Britain's relative position in the world economy called for a fresh start, for a radical new beginning. And it soon became apparent, as the effects of the second oil price shock hit home, that that fresh start would have to be made in an international setting that was increasingly difficult.

Last year world output and trade were lower than generally expected. In the major industrial economies output fell; and more than 30 million of their people were unemployed.

Developing countries have faced similar difficulties. Weak markets for their products, high oil import costs and

B(84) 1021

(put)

Budget Secret

ECONOMIC SECRETARY

FROM: J.M. BRIDGEMAN

7th March, 1984

cc: Chancellor ✓
Chief Secretary
Financial Secretary
Minister of State
Sir Peter Middleton
Mr. Cassell
Mr. Battishill
Mr. Monger
Mr. Lankester
Mr. O'Leary (IR)
Mr. Munroe (IR)
PS/IR

Clearly we want to harmonise the limits: the choice is between £500 all round and £750 all round. On the balance of evidence here [illegible] (including the cost of a 'co-op' funeral) I would I think favour £750; but I am very happy to leave this to the EST to decide. The [illegible] force in para 6 of Mr B's note below: the question is → how much mayhem & aggro we would cause, compared with £750. (It is also worth) → considering, if we do go to £500 on practicalities, whether the taxable limit might not be raised to £75,000. NL

You should be aware that the EST is to discuss this with Mr B at 11.00am tomorrow.

Friendly Societies: Tax-Exempt Business

This note responds to the Chancellor's request for a note on the potential consequences of a £500 limit for all societies. It amplifies paragraph 22 of the Note which I handed to you yesterday. (Not copied to all.) At the end I deal briefly with two related matters.

Implications for the Change in Limit

2. It is inevitable that any change in the tax regime which is intended to shift patterns of investment is going to affect adversely the finances and, in the short term at least, the scale of activity of institutions which have had a significiant stake in what has hitherto been a tax-favoured business. It is also inevitable that they will object volubly. The greatest noise may not come from the worst hit: this may well be the case with friendly societies.

(a) Commercial Friendly Societies

3. The worst hit friendly societies will clearly be the dozen or so societies which have been established in the last few years to take advantage of the tax-exempt limits. These are generally referred to as 'commercial friendly societies'. The majority have been set up by some sponsoring organisation which has another interest in investment: as you will recall the Registry has required arrangements which would permit a move of the friendly society towards a truly mutual status independent of the sponsor, although I have tended to regard this as a rather poor fig leaf.

4. The majority of these commercial societies have realised that the time which they have to exploit the tax relief is probably limited. Certainly I know that in the case of one of the two largest, the Homeowners which was originally floated by the Bradford and Bingley Building Society but now has business links with a number of building societies; the management has its contingency plans against the ending of tax relief.

5. I think that two groups of these societies will adjust without great difficulty. One group consists of those societies associated with an organisation which is already selling ordinary insurance business. They will probably stop taking any new business and will become closed funds. They will be run by the original sponsoring organisation, such as the AA or the Abbey Life. This happened a decade ago when a previous Finance Act stopped a previous use of friendly society schemes for tax evasion: the M & G Unit Trust Group have carried two associated friendly societies which were closed to new entrants then. One has now come to an end and one is nearing it. It is just possible that these societies may increase their management charges slightly - so investors will get smaller bonuses on maturity than they had hoped.

6. The next group may consist of only one, the Family Assurance which is the only other ~~only~~ commercial society besides the Homeowners which has become a sizeable institution. (£40 million total assets.) It is likely that it will decide to go into taxable business, and then in due course take the necessary steps to transform itself into a mutual insurance company.

7. The main problem will arise with the smaller societies with no large organisations to back them up. A particular problem is that some have had a premium structure with deductions for management expenses heavily front loaded, so that when new business stops, the provision for the management will be inadequate to cover the costs of administering the rump. There is also some risk of a management walk away leaving the members to their own devices. There would seem to be two possibilities for them. The first is a transfer of engagements to one of the larger commercial societies which is continuing: for example it is possible, but far from certain, that the Homeowners might take in other friendly societies with building society-linked schemes. But that does depend in part on competitive rivalries between building societies. Another possibility would be for a consortium of the smaller commercial societies to be formed in order to reduce management expenses. The Registry may have to use its influence and good offices to try to ensure such mergers or groupings take place. Even if they do,it is probable that it will be necessary for the societies to amend their rules to increase the permitted

management deduction. So here too policy holders will not get as much in the way of bonuses as they might otherwise have expected. Their investment, which will still be tax free, will not prove to have been quite as attractive as they had originally thought but it should still leave them with a reasonable return.

(b) Large Non-Taxable Traditional Societies

8. The next main group who will be affected will be the minority of large traditional friendly societies who have kept to non-taxable business. (The majority of large societies do both taxable and non-taxable business.) This minority includes societies like the Teachers and the Dentists. These are relatively strong societies, which have been 'bucking the downward trend' and growing in real terms. They have a substantial part of their business in non-life type activities - sickness benefits, benevolent funds and so on. While they will have an adjustment problem, we would expect to them to adapt reasonably well, and in most cases to go in for selling bigger life policies to their client professional groups, a business which they have hitherto stayed out of in order to be able to market the tax-exempt ones up to the £2,000 limit. They will clearly not like the change. But I should be surprised if, after say five years, they are any weaker as a result of it. The problem will essentially be a transitional one.

(c) Small Non-Taxable Societies

9. There are then the great majority of small friendly societies who only do non-taxable business, including the 3,000 or so branches of the Orders. They are relatively small in terms of total assets but could be quite vocal and emotional. They will complain that the measure strikes at the heart of the movement. We do not have returns from them which show how much life business they do in the £500 to £2,000 range. I have the impression, and it is no more, that there are some which have quietly been doing a significant amount, but the majority by number probably have not been doing very much. None have been marketing it aggresively, because to do so would have risked triggering certain provisions in the Taxes Act which would have applied to them the tighter conditions which have related to post 1966 societies.

10. My own assessment of this group would be that the stronger societies amongst them, those which are going to survive anyway, will be able to adjust in just the same way as the Teachers and Dentists. What this step may do is accelerate somewhat the decline of the weaker ones: you may recall that there was a section in my last Annual Report on the

problem of the declining friendly societies. But in the case of the traditional friendly societies which are in decline, I am reasonably confident that other traditional societies will accept transfers of engagements from them, in the way in which they would not from a commercial friendly society. However the Registry will have to increase its work on identifying problem cases and in making sure that the committees of management do react in time. If they want a merger that has to be initiated whilst the financial position of the society is still sufficiently strong for them to be an acceptable partner. Equally the alternative of dissolution by instrument and a cash pay out to members, which might be welcome in many cases, has to be done before the management expenses had eaten away all the funds.

(d) Taxable Friendly Societies

11. These will be the 'silent majority'. They who will not be directly affected by the change in the limit on tax-exempt business. They account for nearly 90% of the total assets of the movement, although they are only one eigth by number.. They will, of course, be affected by LAPR. They will be relieved to see the end of the exploitation of the friendly societies name by the commercial friendly societies. They will welcome the increase in the limit to £60,000 (although some, but not all, of them would like to see it abolished) and welcome the assurance of a further increase for the larger societies linked to the Life Directive.

(e) Conclusion

12. So, as I concluded in my note yesterday, some policy holders will get less than they hope for, primarily because there will not be the new business to contribute to the management costs. Some societies may either become closed funds, merge or dissolve. But I am reasonably confident that the process can be achieved without a collapse in the sense of members getting less than they had originally put in, or even very much less than they expected.

Timing of the Change in the Limit on Taxable Business

13. The solution to the problem of friendly societies and LAPR, which was worked out between Parliamentary Counsel, the Inland Revenue and ourselves yesterday evening and then reported orally to the Financial Secretary, means that the effective date for the LAPR

change for friendly societies will be the same as for everyone else, namely from after 13th March. It is therefore no longer necessary to delay the increase in the limit, as had seemed necessary when it was thought that the effective date would be later for friendly societies. On the other hand, societies can do with a little warning of the increase, so that they can prepare their marketing and pamphlets. So I see no need, in this case, to overrule the normal convention that statutory instruments should be laid at least 21 days before they come into operation. I would suggest an effective date of 1st May.

Presentation

14. The presentation of this package is going to be critically important, so that the generality of friendly societies see what are the positiive points in it for them as well as the negative ones. I would suggest that, in the first instance, you should write a letter, to be sent on the evening of Budget Day, to the Chairman of the Friendly Societies Liason Committee. This would, I think, make the point which Sir Peter Middleton raised yesterday: the strict logic of the present Budget approach would be to have no tax exemption for life policies issued by friendly societies at all. However, because of the special character of friendly societies the Government was keeping the tax exemption for policies up to £500.

15. The Revenue have agreed to post to each individual friendly society on Budget Day evening, a package containing the Inland Revenue press notice on LAPR generally, a copy of Orders which I will be making under the 1976 Finance Act which will deal with the rules of about 75% of the friendly societies, the Revenue note on the change in the limits and a note by RFS explaining in as simple language as possible how thetwo will work for societies.

16. We will let you have drafts of the letter to the Chairman and the RFS circular as soon as we can clear the necessary text with the Inland Revenue and Parliamentary Counsel.

Conclusion

17. I hope that this gives you sufficient to decide on the choice of a £500 or £1,000 limit. I would be very happy to discuss if you wish.

J.M.B.

(J.M. Bridgeman)

Budget Secret

Friendly Societies

Possible Change in Tax-Exempt Limits

Note by the Chief Registrar

£500 on 14/3/84
What collapses?
£60,000 after Royal Assent?

1 Accept argument to £500 rather than £1k but subject to more work pursued in parliament estimate of likely ...

2 Wd. agree proposal to raise max policy from £30 to 60 ... after date of going to Royal ... Bill

1. The purpose of this note is to give you the Registry's view on:-

(i) whether the change should be made this year;

(ii) the choice between £500 and £1,000;

(iii) a possible change in the limit on taxable business;

and (iv) the prudential implications for societies which are specialised in tax-exempt business.

Timing

2. The Registry has a strong preference for legislation this year. The other changes to the taxation of insurance generally may give some boost to the more 'tax-efficient' remaining schemes, notably those of the 'commercial' friendly societies. This will lead to possible prudential strains. Moreover postponement will magnify the scale of adjustment in terms of cost of administration etc when the change eventually comes. It will run the risk of potential embarrassments over the present 'fig leaf' of respectability for the commercial friendly societies, such as that raised by the prospective share issue by Dominion International based largely on the profits it expected to make out of Family Assurance Friendly Society.

3. The other changes in the taxation of financial institutions would enable a change this year to be fitted in as part of the general approach to financial institutions in the Budget. It would not be seen so much as picking on Friendly Societies which it might if left to another year.

4. Moreover, if the taxable limits are reduced it will limit the conspicuous transitional exploitation of the transitional arrangement for Friendly Socieites on LAPR, which has been forced by the ruling that LAPR does not fall within the Provisional Collection of Taxes Act.

5. This preference is subject to one proviso only, namely that the legislation should be simple and should not compound the existing anomalies. The proposal to cut the limit to either £1,000 or £500 would seem to meet this proviso.

The Choice of the Limit

X 6. The choice of limit would seem to depend critically on whether the change is seen as an 'interim' holding operation until a more fundamental change can be made in friendly society taxation, or whether it is regarded as the only likely substantive change in the forseeable future. I favour the latter, and so £500.

7. The solution of reducing the limit was put forward by the Inland Revenue, but rejected some three years ago by Mr. Nicholas Ridley, when Financial Secretary, on the grounds that he wished there to be a more fundamental reassessment of friendly society taxation. Work since then has progressed between the Inland Revenue and the Registry, albeit not as a high priority. There is general agreement on the objectives. First, the taxation of the larger friendly societies should be brought onto an identical basis to that of mutual insurance companies. Second the tax system for the very small friendly societies should not be changed. The Inland Revenue hold this second view because of the administrative problems of collection. The Registry hold a similar view,namely that such societies should be allowed at least a very considerable period of change to adjust. It is fair to say that the Revenue and Registry approaches to achieving the two objectives have differed in emphasis. The Registry have favoured some criterion of size of the society as a trigger for tax treatment, because many of the present anomalies stem from superimposing a series of changes each of which were related to the date of registration of the society. The Revenue have none the less preferred the date related approach because it is more easily policeable. At this juncture I am not sanguine that it will be possible to develop a satisfactory scheme of either type, or a hybrid between them, which would not have significant disadvantages.

8. I would therefore favour the proposal to harmonise the limit on tax-exempt business (which is at present £2,000 gross sum assured for societies doing only tax-exempt business, £500 for others, with equivalent limits for annuities) as a means of dealing with the friendly society taxation problem simply and on a reasonably lasting basis.

9. For that purpose, I would recommend £500 as the limit rather than £1,000. The actual limit for a family would, in practice, be higher than that. Both husband and wife can take out a policy. Also the limit relates to the sum assured which can be significantly increased by bonuses on redemption after ten years. There are two reasons for £500.

10. First a reduction to £1,000 would still leave a significant amount of business for the 'commercial societies'. It would not provide a certain end to that problem, either as a route for tax avoidance or as a distortion of the concept of a friendly society. Such figures as we have suggest that some commercial societies do a significant amount of business at £1,000. Therefore, if the tax exempt limit were standardised at £1,000 most of the commercial friendly societies would continue, pushing the polcies at the lower limit. The scale of activity of the societies would clearly be significantly less, but it could still be of sufficient embarrassment to lead to the kind of difficulties which we are facing at present, particularly if, as is to be hoped, the value of that £1,000 is not much eroded by inflation over the years. So there might well still need to be legislation soon to deal with the anomalies and abuses.

11. The reduction to £500 would, however, almost certainly effectively bring to an end the new business of the commercial friendly societies. (A few might decide to market taxable policies.) So the £500 limit would deal with the commercial friendly society problem.

12. Second to raise the limit to £1,000 for the traditional societies at present doing both taxable and tax exempt business would give to those societies a mis-leading message about the future pattern of their business. It would encourage them to do tax-exempt business which they have not been doing on any scale of late. Unless it was intended to revalorise the £1,000, or possibly increase it further, it would be a misleading policy signal for the Government to give to those societies. Once again the increase to £1,000 would only really make sense if there were more general friendly society taxation provisions to follow.

13. It must be recognised that a reduction to either £500 or £1,000 in the limit for societies doing only taxable business is going to affect a significant number of societies besides the commercial societies. There are a few large successful traditional societies which do only tax-exempt business eg. the Teachers, the Dentists. But life insurance is only part of their business and they could readily switch into taxable business. There is also a significant number of small ones plus an unknown number of branches of the orders (eg. the Manchester Unity of Oddfellows, Ancient Order of Forresters: the branches are separate units for tax purposes.) But for most of these also life business is not their main rationale: that is as much, if not more, the social and benevolent work, sickness benefit etc. That said, if the limit was £500 the branches and others would find that they could offer less advantageous terms on one 'traditional' policy with a long pedigree - a whole life policy designed to cover funeral expenses. I understand that a 'Co-op' funeral now costs about £700. Most of these too would adapt, but under protest.

+ profits

14. Putting it another way, in terms of gainers and losers, the losers from either a £500 or a £1,000 limit would be:-

(i) the commercial friendly societies: who would be more damaged by the £500 limit;

(ii) the other tax-exempt friendly societies who do most of their business in other forms, and who would be less affected in total: clearly the £500 limit would hit them more than a £1,000 one.

The big taxable friendly societies who do 90% of the total business of societies, Royal Liver, Liverpool Victoria etc, would welcome action against the commercials. They would clearly not say 'no' to the £1,000 limit (the Friendly Societies Liason Committee have asked for it) but I am slightly doubtful how far they would use it. They would be more interested in other changes to which I return below..

15. The only group within which gains and losses would balance somewhat if the figure were £1,000 rather than £500 would be the Orders. The tax-exempt branches would lose, the taxable central funds of the Orders would gain.

16. So I do not think that the choice of £1,000 or £500 would affect very much the opposition to the move: there would be the inevitable howls in either event, and not much more vocal support for, or less opposition to, the package if the figure were £1,000.Within the movement, the action to curb the commercials would be welcome, and the logic of that having an effect on the traditionals accepted 'off the record', but that will not stop the protests.

Limit on Taxable Business

17. The larger friendly societies, who do almost exclusively taxable business anyway, will be looking for a different quid pro quo. At present they are subject to two disadvantages in comparison with mutual insurance companies. They are subject to a limit on taxable policies of £50,000: this is principly a prudential control and variable by an order made by me with the consent of the Treasury. They are also limited to trustee investment powers. (These general trustee powers are being reviewed and any change would be expected to carry over.)

18 I would be reluctant on prudential grounds to see either changed for the smaller societies, or indeed for some of the larger societies under the present prudential regime. While hitherto, with very few exceptions, it has been the larger societies which have done taxable business, the bringing of the two limits for taxable business together will mean that more small societies will consider doing taxable business.

19. However that regime has to be tightened for the larger societies in the next year or two in order to comply with the European Life Directive. The regulations are in draft to give effect to this by an order under the European Communities Act 1972. When that comes the limit could be removed (or lifted so that it did not bite) in respect of the 30 or so largest societies authorised under the Order. The wording of the direction is such that we have little option but to widen the investment powers at the same time.

20. In the meantime, I would recommend that I increase the limit to £60,000, or possibly £75,000, as evidence of good intent. I would not go further, because I have no power at present to differentiate between large and small societies.

21. The Friendly Socieites Liason Committee would, I am sure, welcome this, but press for legislation to abolish the limit completely. Indeed Mr. Rees, when Minister of State, wrote to the Liason Committee to say in 1981:-

> 'In the light of the [then] Chief Registrar's favourable opinion on this matter we accept in principle that there is a good case for the removal of these limits......it is our hope that the necessary provision can be made the next time suitable friendly society legislation is introduced.'

But I would advise strongly against going that far: most members of the Liason Committee would individually accept the case against giving the power to a small society. I will readily explain to them that the more discriminating approach now suggested reflects a change of view for which the change in Chief Registrar and the change in the tax regime could be held accountable.

Prudential Implications

22. The change in the limits will clearly affect the financial position of societies - some quite significantly. The likely consequences for the main groups will be:-

(i) 'commercial societies' If the limit were £500, most would stop writing new business of this type. If it were £1,000 some would continue on a reduced scale. The problems which could arise would be:-

(a) management costs outstripping the present provision in the rules for transfers to the management fund. This would be particularly true of societies which heavily front load their premiums. This could require some societies to amend their rules, thereby reducing the eventual bonuses paid on maturity;

(b) management walk away.

I would expect the majority of supervisory bodies to stand behind the administration of their societies eg. A.A, Bradford and Bingley Building Society. (The RFS might have to swallow a few words about independence in persuading them to do so.) Family Assurance might not be supported but is probably strong enough to survive, diversifying into taxable business. Some of the smallest might need to merge, in order to secure economies of management;

(ii) larger traditional societies eg. Dentists, Teachers. These are sufficiently widely based with other business to take the shock. They would probably go in for taxable business instead;

(iii) smaller traditional societies Many of these are sufficiently broadly based to suvive. But the change will accelerate the problems of those already in decline. Here it will often be desireable to secure mergers.

To sum up, some policy holders will get less than they hoped for primarily because there will not be the new business to contribute to the management costs. The Registry may have to expend a considerable amount of effort securing support and/or mergers. But the prudential problem will not be any less, and probably more, if a change in tax treatment is deferred. The necessary support of the larger societies for these rescues is likely to be better secured by action on taxable limits than the choice of £1,000 rather than £500 for the tax-exempt limit.

Conclusion

I accordingly:-

(i) support the Economic Secretary's recommendation that the present two limits for taxable business be brought together;

(ii) recommend, however, that the figure should be £500, not £1,000;

(iii) suggest instead that the limit on taxable business be raised now to £60,000 (or possibly £75,000) with an undertaking about a future increase for the larger societies authorised under the proposed regulations to give effect to the life directive.

J.M. Bridgeman
6th March, 1984

Fully not now
MCC.
To exempt profits
to other Non-profit
eg l. Mey.

B(84)1019

BUDGET SECRET

FROM: G W MONGER

DATE: 7 March 1984

MISS O'MARA

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
PS/C&E
Mr Allen
Mr Griffiths
Mr Kucyzs IR
Mr Wilmott C&E

BUDGET SPEECH BLOCK J: BUSINESS TAXATION

I attach some comments on Block J. This minute draws attention to a few points.

Paragraph 11

2. It is worth considering whether the "Nissan" arrangement should be mentioned in the speech. The argument for including it is that there could be criticism for leaving out an important and potentially awkward point. The argument against is that the point might be taken immediately, and there could be exchanges during the Speech itself which would be better avoided. The Inland Revenue prefer exclusion

Paragraph 14

3. We have suggested excluding the words "and thereafter" because they are not strictly consistent with the last sentence. There is also the point that a commitment to maintaining the CT rate at 35% after 1986-87, if intended, would seem to require more extended treatment.

Paragraph 18

4. I am a bit doubtful about giving such emphasis to the acceleration point. If the new system is a more rational one, it seems odd to make a virtue of the fact the companies can put off its effect on them. The change shown assumes however that the Chancellor still wants to make the general point, and is designed to avoid the word "higher", which is not quite right.

Paragraph 28

5. The Inland Revenue would prefer not to give a figure for the shortfall below the true benefit, partly because there are different figures for different cars, more because to do so would suggest that there was a medium-term aim of making big increases in the scales.

Paragraph 33

6. The Department of Energy are very anxious to have the reference to their Secretary of State, but we and the Inland Revenue are not convinced that it is necessary. The Department are also proposing to issue a press notice after the Budget which will emphasise its advantages for the North Sea. This is not the line taken by paragraphs 33 and 34. The Inland Revenue will minute separately about that.

Paragraph 36

7. We think that paragraph 36 is not quite accurate in its description of VAT on imports and would like to suggest the following redraft. Customs have not yet been able to comment but in view of the shortage of time I am letting you have the draft now. They may wish to comment later. The new draft is:

X 123

"~~36.~~ Ever since VAT was introduced in this country, we have treated imports differently from the way in which they are treated by our main European Community competitors. In a nutshell, they require VAT on imported goods to be paid in the same way as customs duties. We do not. Under our system an importer does not have to account for VAT on his imports until he makes his normal VAT return, on average some 11 weeks ~~[2½] month~~s later. During this time the importer enjoys free credit at the taxpayer's expense. This is an advantage not enjoyed by the home-produced equivalent of the import, since businesses buying from UK suppliers have to pay VAT when they pay their suppliers."

Y

G W MONGER

INDIRECT TAXES

131. Having announced major reforms of both the taxation of savings and investment and the taxation of business, I turn now to the third and final area in which I propose to make progress on tax reform. This is the taxation of personal income and spending.

?
check quotation

132. The broad principle was clearly set out in the Manifesto on which we were first elected in 1979 and which emphasised the need for a switch from taxes on earnings to taxes on spending. My predecessor made an important move in this direction in his first budget, and the time has come to make a further move today. To reduce direct taxation by this means is important in two ways. It improves incentives and makes it more worthwhile to work, and it increases the freedom of choice of the individual.

133. I do not however see the excise duties - with certain exceptions - as an area for major change. I shall of course need to raise most of the duties broadly in line with inflation, so as to maintain their real value: not to do so would run counter to the philosophy I outlined a moment ago. But with inflation now as low as it is, the necessary increases are on the whole mercifully modest. Only for a few particular duties do I envisage steeper rises.

134. One significant exception is tobacco, where I ~~am~~ believe it is right ~~convinced of the need~~ to raise the duty in real terms, given ~~to help cut smoking and thus reduce~~ the potential danger to health. I therefore propose an increase in the tobacco duty which, including VAT, will put 10p on the price of a packet of cigarettes, with corresponding increases for hand-rolling tobacco and cigars. This will do no more than restore the tax on tobacco to its 1965 level. I do not propose to increase the duty in pipe tobacco, which is important for a great many pensioners. These changes will take effect from midnight on Thursday.

135. For the duties on petrol and derv I propose simply broad revalorisation, which means increases which, again including VAT, will raise ~~increase~~ the price at the pumps by 4½p and 3½p a gallon respectively. I do not propose to increase the duty on heavy fuel oil, which is of particular importance to industrial costs. These changes will take effect for oil delivered from refineries and warehouses from six o'clock this evening.

136. There is one excise duty which I propose to do away with altogether. Many of those who find it hardest to make ends meet, including in particular many pensioners, use paraffin stoves to heat their homes, and it is with them in mind that I propose to abolish the duty on kerosene from six o'clock tonight. I am sure that this will be welcomed on all sides of the House.

137. The various rates of Vehicle Excise Duty will, once again, go up roughly in line with prices. Thus the duty for cars and light vans will be increased by £5, from £85 to £90 a year. However, ~~given the further evidence my Rt Hon Friend the Secretary of State has now received on~~ the wear and tear that various types of vehicle cause to the roads, there will be reductions in duty for the lightest lorries, offset by higher increases for some heavier lorries. All these changes in Vehicle Excise Duty will take effect from tomorrow.

in the light of the reassessment my RHF has made of

138. However, I propose to exempt from Vehicle Excise Duty all recipients of the War Pensioners' Mobility Supplement.

139. And I have decided to widen the specific VAT reliefs for the disabled in the important area of transport. The existing VAT relief for motor vehicles designed or adapted for use by the handicapped will be extended, and matched by a new Car Tax relief. The effect will be that neither VAT nor car tax will apply to family cars designed for disabled people or substantially adapted for their use.

140. I now come to the most difficult decision I have to take in the excise duty field. As the House will be aware, the rules of the European Community, so far as alcoholic drinks are concerned, are designed to prevent a Member state from protecting its own domestic product by imposing a significantly higher duty on competing imports. In pursuit of this, the Commission has taken a number of countries to the European Court of Justice.

141. In our case, the Commission contended that we were protecting beer by under-taxing it in relation to wine. We fought the case, but lost; and I am now implementing the judgement handed down by the Court last year. Accordingly, I propose to increase the duty on beer, not by the 7p a pint which has been widely rumoured in the press, but by the minimum amount needed to comply with the judgement and maintain revenue: 2p on a typical pint of beer, including VAT. At the same time, the duty on table wine will be reduced by the equivalent of about 18p a bottle, again including VAT.

142. I cannot, however, ignore the fact that while we comply with the judgement of the European Court, one of our partners appears determined not to do so. I refer to Italy, which has been ordered by the Court to remove forthwith its discrimination against Scotch whisky, but as yet shows no sign whatever of complying. I have therefore decided to introduce a temporary duty surcharge on vermouth of some 20p a bottle on top of the basic increase, to which I shall come in a moment. This surcharge will come into operation on 1 September unless the Italian Government has - as I very much hope it will - implemented the Court's judgement by that date, and it will lapse as soon as I am satisfied that it has complied.

143. As for the rest of the alcoholic drinks, cider, which increasingly competes with beer but attracts a lower duty, will go up by 3p a pint. The duties on made-wine will be aligned with those on other wine. And I propose to increase the duty on sparkling wine, fortified wine and spirits by about 10p a

bottle, including VAT. All these changes, except the vermouth surcharge, will take effect from midnight tonight.

144. These changes in excise duties will, all told, bring in some £840 million in 1984-85, some £200m more than is required to keep pace with inflation. The addition is of course ~~largely~~ due to the increase in tobacco duty.

145. But much of the extra revenue I need to make a substantial switch this year from taxes on earnings to taxes on spending will come from VAT. I propose no change in the rate of VAT. Instead, I intend to broaden the base of the tax by extending the 15 per cent rate to two areas of expenditure that have hitherto been zero-rated.

146. First, alterations to buildings. At present repairs and maintenance are taxed, but alterations are not. The borderline between these two categories is the most confused in the whole field of VAT. I propose to end this confusion and illogicality by bringing all alterations into tax. However, to allow a reasonable time for existing commitments to be completed or adjusted, the change will be deferred until 1 June.

147. Secondly, food. Most food is zero-rated. But food served in restaurants is taxed, together with a miscellaneous range of items including ice-cream, confectionery, soft drinks and crisps, which were brought into tax by the Rt Hon Member for Leeds East. Take-away food clearly competes with other

forms of catering, and I therefore intend to bring into tax hot take-away food and drinks, with effect from 1 May.

148. The total effect of the extensions of the VAT coverage which I have proposed will be to increase the yield of the tax by £375 million in 1984-85 and by almost £650 million in 1985-86.

149. The total impact effect on the Retail Price Index of the VAT changes and excise duty changes taken together will be less than three-quarters of one per cent. This has already been taken into account in the forecast which I have given to the House of a decline in inflation to 4½ per cent by the end of the year.

150. The extra revenue raised in this way will enable me within the overall framework of a neutral Budget to lighten the burden of income tax.

Ch/Ex Ref No B(84)549

FROM: J O KERR
DATE: 8 MARCH 1984

Sir P Middleton

cc Sir T Burns
Mr Battishill
Mr Folger
Mr Portillo

Mr Fraser: C & E

Mr Orr

Could you circulate chunks quam celerrime please, to the relevant Branch / Bankesters / who-ever (& copied to Ministers interested in that chunk specifically, incl. IR of course, and the relevant Minister), asking the addressees to co-ordinate comments for all, and submit on the same deadline.
Don't circulate indirect taxes to anyone, yet. I plan to get clearance to show it to Rangers

JOK

... I attach the latest complete draft of the Budget Speech, and would be most grateful if any suggested amendments could reach me by lunchtime on 9 March. Sections of the Speech are of course being circulated more widely.

JOK.

J O KERR

INTRODUCTION

This Budget will set the Government's course for this Parliament. It is founded on the policies which we have consistently followed since 1979.

2. Consistency of purpose is the hallmark of this Government. Those policies offer (MP) [It is] the only way to improve economic performance and they have laid (MP) [lay] the foundations for future prosperity, more jobs and lower taxation. Above all, they provide (MP) [it is] the only way to defeat inflation and achieve our ultimate objective of stable prices.

3. The results of the Medium Term Financial Strategy introduced in 1980 can be seen in three (AB) ~~four~~ years of falling inflation, down now to the lowest levels since the sixties. And that in turn has brought a steady recovery of output, rising living standards and, more recently, rising employment.

4. The facts speak for themselves. They are a tribute to the courage and foresight of the five Budgets presented from this Despatch Box by my distinguished predecessor, the present Foreign Secretary, whose duties sadly keep him in Brussels today.

5. Today's Budget has two themes: first, the further reduction of inflation, which will further improve the prospects

for jobs; and second, the reform and simplification of the tax system~~, which will make it fairer for all~~.

6. I shall begin by reviewing the economic background to the Budget. I shall then deal with the medium term financial strategy; with monetary policy and the monetary targets for next year; and with public borrowing and the appropriate PSBR for the coming year. I shall then turn to public expenditure, including the prospects for the longer term. Finally I shall deal with taxation, and the changes in the structure of taxation which will pave the way for cuts in taxes in subsequent years. Some of these cuts I shall announce today, for this is in a sense a Budget for two years. In a wider sense it is a tax reform Budget, setting out ~~a~~ much of our (MP) tax strategy for this Parliament.

Something in it for both this + next.

7. As usual, a number of press releases will be issued today, filling out the details of ~~my~~ our (MP) tax proposals.

THE ECONOMIC BACKGROUND

MP

8. But I start with the economic background, and the convincing evidence of recovery: a recovery that springs from the monetary and fiscal policies to which we shall hold.

(MF) the increase in prices over the preceding year

9. Since 1980, inflation has fallen steadily from a peak of over 20 per cent. Last year ~~it~~ was down to about 4½ per cent, the lowest figure since the sixties. And with lower inflation have come lower interest rates.

it has sprung from the

Government's (MP)

10. The underlying strength of the recovery is clear. Whereas in some previous cycles recovery has come from a self-defeating stimulus to monetary demand, this time its roots are in our commitment to sound finance and honest money. Lower inflation and lower interest rates benefit industry, business, and consumer confidence. Falling inflation has made room for real growth, as we always said it would. PEM

(MF) some

11. Across the economy, total money incomes grew in 1983 by ~~about~~ 8 per cent, of which 3 per cent represented real growth in output. Although there is still room for improvement, this ~~clearly~~ is a very much healthier division between inflation and real growth than the nation experienced in the 1970s. Output in the second half of 1983 is now reckoned to have exceeded the previous peak, before the world recession set in, and is still rising strongly.

calculated (MP)

12. Productivity too has continued to improve rapidly. Just as over the past year many have wrongly predicted an end to the recovery, so some have tried to dismiss the sharp rise in productivity as a flash in the pan. Yet during 1983 manufacturing productivity grew by 6 per cent with no sign of slowing down. Unit labour costs across the whole economy are likely to show the smallest annual increase since the 1960s. This has allowed a welcome and necessary recovery in real levels of profitability.

Revised figures in FSBR

13. Higher profits lead to more jobs. The number of people in employment increased by about ~~85,000~~ (MF) 80,000 between March and September last year. The loss of jobs in manufacturing has slowed down sharply, while jobs in services increased by [getting on for] nearly (MP) 200,000 in the first nine months of last year. This is encouraging news for the unemployed and for (MP) those who will be leaving school this summer.

Lower pay rises could increase our competitiveness; and that would help the prospects for employment (MP)

14. But further progress ~~on productivity~~ is needed: although our unit wage costs in manufacturing rose by under 3 per cent last year, such costs actually fell in the US, ~~Japan~~ and Germany, [and were unchanged in Japan (MF)] [~~our three biggest competitors.~~] [The employment prospect would be significantly improved if a bigger contribution to improved ~~productivity~~ ~~competitiveness~~ cost performance (MF) were to come from lower pay rises.] (Good sense about pay remains vital.

and a smaller one from squeezing out jobs (AR)

15. Demand, output, profits and employment all rose last year. Home demand has played the major part in the recovery so far. Lower inflation has (MP) reduced people's need to save and real

have risen last year (MP)

incomes rose. Personal consumption increased by over 3½ per cent compared with 1982. Fixed investment rose rather faster than consumption, with investment in housing and services particularly strong.

MP

MP

16. Imports rose a little faster than home demand last year, as the UK emerged from recession ahead of our main European (MF) trading partners - our rate of economic growth last year was the highest in the European Community. For much of 1983 our export performance reflected the weakness of (MP) ~~in~~ many of our overseas markets. But during ~~by the end of~~ last year world trade ~~was~~

imports rose a little faster than home demand (MP)

MP began to pick up

clearly ~~moving ahead again~~, and in the three months to January manufacturing exports increased very substantially. we estimate that the (MP) The balance of payments on current account last year is estimated (MP) to have been was in surplus by about £2 billion. last year

17. Our critics have been confounded by the combination of recovery and low inflation. Even the pessimists have been forced to acknowledge the strength of the recovery. It is set to continue (MF) ~~throughout~~ this year at an annual rate of 3 per cent. Inflation is expected to remain low, edging back down to 4½ per cent by the end of this year. But (MP) With rising incomes and low inflation, personal consumption will continue at a high level (PEM) ~~to grow~~. And the recovery is MP already becoming more broadly based. Encouraged by improved profitability and better long-term growth prospects, investment is expected to rise by a good (MF) 6 per cent this year.

[PT]

18. Looking abroad, economic prospects are also more favourable than for some time. Output in the United States should continue to grow strongly this year. And recovery is spreading to the rest of the world.

MP (MF)

19. Of course, there are [inevitable] risks ~~and uncertainties.~~ The size and continued growth of the United States budget deficit causes widespread concern, not least among Americans, and keeps American, and hence international, interest rates high. This acts as a brake on world recovery and worsens the problems of the debtor countries. Another consequence is a massive and still growing deficit in the US current balance of payments, financed by net capital inflows [of foreign capital,] and leading to mounting pressures for protectionism within the United States, and sharp exchange rate movements. [It is an The unstable] situation, is unstable and that causes anxiety (MP) [creating worrying uncertainties.] RL/AR

There is an of (MP)

20. [A second potential] risk [is] disruption in the oil market. [The immediate prospects are less obviously volatile than they were a year ago. But uncertainties remain, and] the United Kingdom, and indeed the world economy, [inevitably] remains (MP) vulnerable to any major disturbances.

PM ? // MP

21. But despite these risks there is a growing sense throughout the industrialised world that [the] this recovery [this time] is not a temporary upward blip (PEM) [merely cyclical], but [one which] can be sustained. [The essential requirement is] the continued pursuit of prudent monetary and fiscal policies. is essential to that. MP

THE MTFS

22. For the United Kingdom, the Medium Term Financial Strategy has been the cornerstone of such policies. It will continue to [play that role;] [to] provides a framework and discipline for Government and ~~to~~ sets out clearly, to industry and the financial markets, the guidelines of policy. Too often in the past Governments have abandoned financial discipline whenever the going got rough, and [been driven] to stagger from one short-term policy expedient to another. The temptation to accommodate inflationary pressures proved irresistible, and the nation's longer-term economic performance was progressively undermined.

be so (MP) It (MP) (MP) leave had (MP) / staggered / forced to stagger (TL)

23. The discipline of the MTFS was designed to ensure consistency between monetary and fiscal policies, and a proper balance in the economy. It is [so] designed to ensure that the more inflation and inflationary expectations come down, the more room [is available] for output and employment to grow.

X MP there is (MP)

24. People now know that the Government intends to stick to its medium term objectives. They understand that the faster inflation comes down, the faster output and employment can recover. Increasing realism, and flexibility in the economy, owe~~s~~ much to the pursuit of firm and consistent policies within the MTFS framework.

PM can (

25. Originally the MTFS covered four years. In this first Budget of a new Parliament MP we have thought it is appropriate to carry it forward for five years. So the MTFS published today in the Financial Statement and Budget Report -the Red Book - shows a continuing downward path for the monetary target ranges over the next five years, and a path for public borrowing consistent with that reduction. It takes full account of important influences such as the pattern of North Sea oil revenues, and the level of asset sales arising from the privatisation programme. For the last two years of the new MTFS, which lie beyond the period covered in last years Public Expenditure Survey and last month's White Paper, the Government has not yet made firm plans for public spending. But the MTFS assumption - and it is just (MP) no more than an assumption - is that the level of public spending in 1987-88 and 1988-89 will be the same in real terms as that currently planned for 1986-87.

26. The MP precise figures MP set out in the MTFS are not of course a rigid framework, lacking all flexibility. As in the past, there may have (MP) well need to be adjustments to take account of changing circumstances. But no such changes will be made only when they that (MP) will not jeopardise the consistent pursuit of the Government's objectives.

MONETARY POLICY

MP

27. [Monetary policy will continue to play a central role. For] further reductions in monetary growth are needed to achieve still lower inflation.

28. Over the twelve months to mid-February the growth of £M3 has been well within the 7-11 per cent target range, with M1 and PSL2 at or a little above the top of it. While in the early months of the target period most measures of money showed signs of accelerating, [illegible] (MP) growth in all the target aggregates has ~~since the summer~~ been comfortably within the range.

29. Other evidence confirms that monetary conditions are satisfactory. The effective exchange rate has remained fairly stable, despite the international MP [uncertainties and] instability MP [which I have described.] And nominal interest rates have continued to decline ~~in line with falling inflation.~~ TL

Page 2 AT

MP

30. [To maintain sound monetary conditions in the years ahead the monetary targets must reflect changes] in the financial system and in the significance of different measures of money. MP [There is nothing new in this.] MP Over the years we have altered the target ranges and aggregates to take account of such changes. [But the thrust of the strategy has been maintained.]

That has not changed the thrust of our strategy. To maintain sound monetary conditions, the monetary targets must continue to reflect such changes in the years ahead (MP) we have

ed (MP)

31. [One important development has been the] attempt to give a more explicit role to the narrow measures of money. Even when targets were set solely in terms of £M3, we recognised the narrow measures, (MP)

the significance of [their behaviour.] £M3 and the other broad aggregates give a good indication of the growth of liquidity.

TL

But they do not measure money immediately available for current spending. In defining policy it is therefore helpful also to make specific reference to narrower measures of money which do provide such a guide.

[But a large proportion of this money is deposited in ways which earn interest. In defining policy it is therefore helpful also to make specific reference to measures of money which bear very little interest, and provide a good guide to the immediate potential for spending.]

s (M1) specifically (MP) which

That is why we M1 (MP)

M1 was for this reason introduced as a target aggregate but it has not proved entirely satisfactory for that purpose. With the rapid growth of interest-bearing sight deposits, M1 has become an increasingly poor measure of money held to finance current spending. The signs are that this will continue.

32. [M1 was for this reason] introduced as a target aggregate, but it has not proved entirely satisfactory for that purpose. Its behaviour has been dominated by changes in its large interest-bearing component, which has grown rapidly, and now accounts for 25 per cent of the total. That looks as though it will continue (MP) With the introduction of new, interest bearing chequing accounts, the signs are that this will continue.

[deletion of distinction on whether earn interest]

33. Other measures of narrow money have not been distorted to the same extent. In particular, not (MP) MO, which consists mainly of currency, [has not been subject to this development.] It has been affected by other innovations that have reduced people's need for cash, but [the pace of change has not diminished its value as an indicator of financial conditions.] I believe it is likely to be a better indicator of financial conditions than M1 (TL) There is also the new aggregate M2, which was specifically devised to provide a comprehensive measure of transactions balances and which may in time prove a useful guide, but still needs to be interpreted with particular care.

34. In the past two years, it has been possible to set a single target range for both broad and narrow measures of money. But this will not normally be the case; for narrow monetary aggregates tend to grow more slowly than broader measures. And this year's Red Book sets out two separate ranges.

35. The target range for broad money will continue to apply to £M3, and for the coming year will be set at 6-10 per cent, as indicated in last year's MTFS. The target range for narrow money will apply to MO and for next year will be set at 4-8 per cent. To avoid any possible misunderstanding, I stress that the use of MO as a target aggregate will not involve any change in methods of monetary control.

36. Both target ranges will have equal importance in formulating policy. And we shall continue to take into account other measures of money, especially M2 and PSL2, as well as wider evidence of financial conditions, including the exchange rate. As in the past, we shall seek to influence monetary conditions by an appropriate combination of fiscal policy, funding and ~~operations in the money market.~~ short-term interest rates (TL)

37. So far as funding is concerned, the role of the National Savings movement will remain important. This year's target of £3 billion is likely to be achieved: the target for the coming year will again ~~by~~ be £3 billion.

38. ~~Precise~~ The monetary targets for the later years will be decided nearer the time. But to give a broad indication of the

objectives of monetary policy, the new MTFS, like previous versions, shows monetary ranges for a number of years ahead. These ranges are consistent with a continuing downward trend in inflation: they demonstrate the Government's intention to make further progress towards stable prices.

BUDGET SECRET

PUBLIC SECTOR BORROWING ETC

Any

39. I turn now to public borrowing, [for just as the classical] formula for financial discipline [- the gold standard and the balanced budget - had] both a monetary and a fiscal component, [so does the] medium term financial strategy. makes this quite explicit [PEM]

(PEM disputes expl) must have

The

40. The MTFS has always envisaged that the Public Sector Borrowing Requirement would fall as a percentage of Gross Domestic Product over the medium term. And it has, notably as a result of the courageous Budget introduced by my predecessor in 1981, which brought the PSBR down to 3½ per cent of GDP in 1981-82.

41. Since then there has been little further fall. The latest estimate of the PSBR for the current year, 1983-84, remains what it was in November: around £10 billion, equivalent to 3¼ per cent of GDP. This is significantly above what was intended at the time of last year's Budget, and would of course have been higher still had it not been for the measures taken last July.

42. We now need a further substantial reduction in borrowing, in order to help bring interest rates down further as monetary growth slows down. Sterling interest rates are, of course, also influenced by dollar interest rates and so by [the US situation which I have already described]: but that makes it all the more

conditions in America (MP)

the influences of the US (TL)

important to curb domestic pressures. In contrast to virtually the whole of the post-war period, UK longer-term rates are now lower than American rates. As long as American rates remain near their current level, it is highly desirable that this advantage be maintained.

We are planning an (MP)

43. [The] higher level of asset sales [planned] as the privatisation programme gathers pace, That (MP) is a further reason for reducing the PSBR significantly in the coming year. Asset sales reduce the Government's need to borrow. But their effect on interest (PEM) rates ~~is~~ may be less than the effect of some other ~~direct~~ [redacted] reductions in Government spending programmes.

44. Last year's MTFS showed an illustrative PSBR for 1984-85 of 2½ per cent of GDP, equivalent to around £8 billion. But ~~I~~ we (MP) believe that it is possible, and indeed prudent, to aim for a somewhat lower figure. [I have] We are therefore [decided to] provide ing (MP) for a PSBR next year of 2¼ per cent of GDP, or roughly £7 billion. 11 7¼

45. The House will recall that in November I warned that on conventional assumptions, including the 1983 Red Book's PSBR figure of £8 billion for next year, ~~I~~ we (MP) might have to increase taxes slightly in the Budget. I am glad to report that the latest, and more buoyant, forecasts of tax revenue in the coming year, [coupled with the decisions taken in the Public Expenditure Survey and the continuing effects of the July measures,] have changed the picture. Bringing the PSBR down to £7 billion will not

12

no

(on our latest forecasts (72)

require such an increase in taxation. In fact it will require no overall net increase at all. So the measures I shall shortly announce will, after indexation, be broadly neutral in their effects on revenue in 1984-85.

46. Better still, they will reduce taxation in 1985-86 by some £1¾ billion. And the MTFS published today shows that there should be room for further tax cuts not only in 1985-86, but throughout the remainder of this Parliament, provided that we stick firmly to our published plans for public expenditure to 1986-87, and maintain an equally firm control of public spending thereafter.

PUBLIC EXPENDITURE

47. The Public Expenditure White Paper setting out our spending plans for the next three years was approved by the House last week. Today I want to consider [the critically important issue of] government spending in a rather wider perspective.

MP

48. For far too long, spending has grown faster than has the economy as a whole. The trend has seemed inexorable, and the result has been that the great mass of the population have had to pay more and more in tax. To take just one example: as recently as 1963-64 no married man had to pay a penny of income tax unless his taxable income was at least 45 per cent of the average earnings level. Today the tax threshold is down to ~~little more than~~ under a third of average earnings. [We must reverse Over the years the tendency for more and more people on lower and lower incomes have been brought into income tax.]

PM

49. We have seen a steady enlargement in the role of the State, at the expense of the individual, and a ~~steady~~ increase in the ~~dead~~ weight of taxation [holding back the nation's economic progress dragging down our economic performance as a nation.]

(PM)

50. [Clearly] this ~~dangerous~~ process has to stop. Of course, much public spending is directed to eminently desirable ends. But there is an important choice to be made; [and] it is not

MP

about what levels of tax a public spending are desirable (MP)

enough simply to make marginal changes in spending programmes from year to year. The choice needs more fundamental national
take account of the (MP)
consideration and debate; and it needs to [be set within a]
term prospects (MP)
longer [time horizon.]

The Government is (MP)
51. [I am] therefore publishing today, in addition to the customary Budget documents, a Green Paper on the prospects for public spending and taxation in the next ten years. It examines
the (MP)
past trends; discusses pressures for still higher spending;
people (MP)
and examines the rewards for [the individual] if these pressures can be contained.

52. The Green Paper concludes that, without firm control over public spending, there can be no prospect of bringing the burden of tax back to more reasonable levels. On the assumptions made in the Green Paper, the burden of taxation will be reduced to the levels of the early 1970s only if public spending does not rise in real terms over the next ten years. If, on the other
we fail to hold public spending, it will be very difficult to reduce the tax burden. If it (MP)
hand, [spending] grows by 1 per cent a year in real terms after
just (MP) in 1993 still (MP)
1988-89, the tax burden MP [would [by 1993] be only just below the 1978-79 level, and [still] well above its level in the 1960s,
And those figures are based on the assumption that (MP)
[even if] the economy grows by about 2 per cent a year over the
Whether that proves over optimistic or not is itself partly depends on whether we can reduce taxation because
ten years. [And of course] excessive taxation slows the whole
down
economy. (MP)

53. The Government believes that the issues discussed in the Green Paper merit the attention of the House and the country.

MP

It is a discussion document - descriptive not prescriptive - and we shall welcome the fullest possible discussion.

There is (MP)

54. I can at once inform the House of a further innovation. This year (MP)

in that

In contrast to previous years, I have no specific public expenditure measures to announce in this Budget. The White Paper plans stand.

MP   have

55. But lest the innovation seems too sweeping, I can make one small announcement, which I think the House will welcome.

we are (MP).   ing

Within the plans we have been able to provide the National

extra money (MP)

Heritage Memorial Fund with additional resources which will enable them, among other things, to secure the future of Calke Abbey. My Rt Hon Friend the Secretary of State for the Environment is providing £6.3 million from his planned expenditure for this year and next, and I have accepted a claim on the Reserve of £2 million for next year.

56. The House will recall that the proposals for the new rates of social security benefit to come into force in November are not now made on Budget day. Following last year's legislation

the new rates are calculated

to return to the historic method of uprating, price protection

from (MP)

is measured by reference to the Retail Price Index for May.

So (MP)

Accordingly, my Rt Hon Friend the Secretary of State for Social Services will be announcing the new rates of social security benefits, including Child Benefit, in June.

BUDGET SECRET

leaving (MP)
57. Before turning from Government spending to Government
MP
revenue, I should add a word on public sector manpower. At the beginning of the last Parliament, the Government set itself the target of reducing the size of the Civil Service from 732,000 in April 1979 to 630,000 by April of this year. That target has been achieved. We have now set ourselves the further
we are (MP)
target of 593,000 by April 1988, and I am confident that it too
the (MP)
will be achieved, and that a leaner Civil Service will continue to
improve its (MP)   MP
operate with increasing efficiency. Speaking for my own Departments, the tax changes I shall be announcing today will
in my Departments (MP)
reduce manpower requirements by at least 1000 which will help towards meeting the 1988 target.

TAX REFORM

said (MP)

58. I [mentioned] at the outset that this will be a radical, tax-reforming, Budget. It will also significantly reduce the overall burden of tax over the next two years taken together [~~- and indeed over the whole MTFS period -~~] and *even after allowing for the continued effects in future years* I hope to have scope for further reductions in tax in subsequent Budgets.

too dangerous to be so specific [PEM]

59. My proposals for reform are guided by two basic principles. First, the need to make changes that will improve our economic performance [over the longer term.] *MP* Second, the desire to make life a little simpler for the taxpayer.

60. But I am well aware that the tax reformer's path is a stony one. Any change in the system is bound, at least in the short term, to bring benefits to some and disadvantages to others. And, if I may borrow a phrase from the Rt Hon member for Leeds East, the howls of anguish from the latter group tend to be rather more audible than the murmurings of satisfaction from the former.

61. ~~Reform must succeed, but need not be, in this sense, a howling success. So~~ *Some [experts] have suggested* I have rejected the extreme suggestion, popular in some quarters, that ~~I should scrap~~ our income-based tax system ~~and replace it with a brand~~ *should be scrapped + replaced* new expenditure-based system. A reform of this kind would produce, in the real world, an *appalling* upheaval [of mind-boggling dimensions.] *(MP)* *and would be totally unrealistic*

PM

62. But I don't believe we can afford to opt for the quiet life and do nothing. So ~~I~~ we (MP) have chosen [the middle way:] to work for improvements, some [I believe] very substantial, [but] within [the framework of] our existing income-based system. [I shall also be proposing transitional arrangements where I believe it fair and appropriate to do so.]

AE

63. The changes [I shall be proposing today] fall into three broad categories. [These are] the taxation of savings and investment, business taxation, and the taxation of personal income and spending.

SAVINGS AND INVESTMENT

64. First, the taxation of savings and investment. The proposals I am about to make should improve [both] MP the [direction] structure (PEM) and quality of both. And they will contribute further to the creation of a property-owning and share-owning democracy, in which more decisions are made by individuals rather than by intermediary institutions.

65. First, stamp duty. This was doubled from its long-standing 1 per cent by the post-war Labour Government in 1947, reduced by the Macmillan Government in 1963, and once again doubled to 2 per cent in the first Budget presented by the [Rt Hon member for Leeds East] Labour Government (MP - radio audience) in 1974. At its present level it is an impediment to mobility and is incompatible with the welcome move[ment] MP to greater competition in the City, following the withdrawal of the Stock Exchange case from the Restrictive Practices Court.

66. I therefore propose to halve the rate of stamp duty to 1 per cent. [Transactions from today will benefit from the new (PEM - delete) rate, unless documents have to be stamped before 20 March, which is the earliest date on which the change will have legal effect.]

67. For the home buyer, the new flat rate 1 per cent stamp duty will start at (an increased threshold of) £30,000. Below this level no duty will [in future] MP be payable, and 90 per cent of first time home buyers will therefore not [be liable for] have to pay (MP) stamp duty at all.

c f what

68. Reducing the rate of duty on share transfers will remove an important disincentive to [direct] investment in equities and increase the international competitiveness of our stock market. It should also help British companies to raise equity finance.

69. In addition, I have three proposals to encourage the issue of corporate bonds. I shall go ahead with the new arrangements for deep discount stock and the reliefs for companies issuing Eurobonds and convertible loan stock which were announced but not enacted last year. And I propose to exempt from Capital Gains Tax certain corporate fixed interest securities provided they are held for more than a year. Since such securities are already exempt from stamp duty ~~- an exemption I can confirm also extends to certain convertible loan stocks -~~ this means that the tax concessions for Government borrowing in the gilt-edged market will now be virtually the same as for private sector borrowing in the corporate bond market.

X

X

[PEM - discuss comeback on NS v. banks/building socs]

70. The reductions in stamp duty will cost £450 million in 1984-85, of which £160 million is the cost of the relief on share transfers, and £290 million the cost of the relief on transfers of houses and other property (MP) [real estate.]

71. Next, life assurance. I have concluded that there is no longer any justification for Premium Relief on Life Assurance,

to end

which is now only one of a number of savings channels for ordinary people. The main effect of the relief today is to encourage institutional rather than direct investment, and to spawn a multiplicity of well-advertised tax management schemes. I propose to withdraw the relief on all new policies made after today. I stress that this change will apply only to new (or newly enhanced) policies, taken out or increased after today. Existing policies will not be affected at all. The change is estimated to yield about £90 million in 1984-85. [IR]

72. We must also review unjustified penalties on direct personal investment. The Investment Income Surcharge is an unfair and anomalous tax on savings and on the rewards of successful enterprise. It hits the small businessman who reaches retirement without the cushion of a company pension scheme, and impedes the creation of farm tenancies. In the vast majority of cases it is a tax on savings made in the first place out of hard-earned and fully-taxed income. More than half of those who pay the investment income surcharge are over 65, and of these ~~more than~~ half would otherwise be liable to tax at only the basic rate.

IR.

73. I have therefore decided that the investment income surcharge should be abolished. The cost in 1984-85 will be some £25 million, and in a full year around £350 million.

74. Finally, I propose to draw more closely together the tax treatment of depositors in banks and building societies.

These institutions compete in the same market for personal deposits. I believe that they should be able to do so on more equal terms as far as tax is concerned.

75. One inequality has already been removed, with the recent change made on legal advice in the tax treatment of building societies' profits from gilt-edged securities. They are now treated in the same way as those of the banks have always been.
Other inequalities will be removed by measures to which I shall come later in the speech (PEM)

76. But the major inequality of treatment, against which the banks in particular have frequently complained, is (MP) lies with the special arrangement for interest paid by building societies, MP under which the societies pay tax at a special rate - the "composite rate" - on the interest paid to the depositor who receives credit for income tax at the full basic rate.

77. This system, which has worked well for the past 90 years, has both an advantage and a disadvantage. The disadvantage is that a minority of depositors, who are below the income tax threshold, still have tax deducted (MP) suffer the deduction of tax at the composite rate. However, it is always open to such depositors to put their savings elsewhere, such as National Savings. The advantage of the scheme is its extreme simplicity, particularly for the taxpayer; most taxpayers are spared the bother of paying tax on interest through PAYE or individual assessment, while the Revenue are spared the need to recruit an additional 2000 staff to collect the tax due on interest paid without deduction.

78. In common with my predecessors of all Parties over the past 90 years, I am satisfied that the advantage of the composite rate arrangement outweighs the disadvantage. It follows that equal treatment of building societies and banks should be achieved, not by removing the composite rate from the societies, but by extending it to the banks and other licensed deposit takers.

will (MP

79. Non-taxpayers [would] ~~of course~~ continue to be able to receive interest gross, should they wish to do so, by putting their money into appropriate National Savings facilities, where they can obtain a much better pre-tax interest rate (PEM). But the purpose of the move is not, of course, to attract savings into Government hands: as I have already announced, next year's target for National Savings will be the same as this year's and last year's, and the total Government appetite for savings, which is measured by the size of the Public Sector Borrowing Requirement, is being significantly reduced. [Moreover I have decided to reduce substantially the permitted maximum size of future holdings in the National Savings Investment Account and in Income Bonds.]

PEM - doesn't sound right - looks as though non-taxpayers' opportunities are being squeezed - thanks to PN

80. The true purpose of the move is simple: simplicity itself. Unless they are higher rate taxpayers, individual bank customers will, when it comes to tax, be able to forget about bank interest altogether, for all the tax due on it will be deducted at source. The Inland Revenue will be able to make staff savings of up to an extra 1000 civil servants. Moreover, this figure takes no account of the extra numbers that would have

been required to operate the present system as the trend towards the payment of interest on current accounts develops, or of the numbers required if I had taken the other course and removed the composite rate for building societies (PEM)

So (MP)

81. [Accordingly,] I propose to extend the composite rate arrangements to interest received by UK resident individuals from banks and other licensed deposit takers with effect from 1985-86. The composite rate will not apply either to non-residents or to the corporate sector. Arrangements will also be made to exclude from the scheme Certificates of Deposit and Time Deposits of £50,000 or more.

reforms (MP)

82. Taken together, the major [proposals] I have just announced on stamp duty, life assurance relief, the investment income surcharge and the composite rate, coupled with other minor proposals, will provide a simpler and more straightforward tax system for savings and investment. They will remove biases which have discouraged the individual saver from investing directly in industry. And they will reinforce the Government's policy of encouraging competition in the financial sector, as in the economy as a whole.

BUSINESS TAXATION

business (NM)

83. I now turn to company taxation.

84. In this area, Government has two responsibilities towards British business and industry. The first is to ensure that they do not have to bear an excessive burden of taxation. The second is to ensure that, given a particular burden, it is structured in the way that does least damage to the nation's economic performance.

85. The measures I am announcing today will, taking the next two years together, result in a ~~[illegible]~~ substantial reduction in the burden of taxation on British business (NM) industry. And ~~in addition~~ (PEM) I shall be proposing a far-reaching reform of the NM structure of company taxation.

Responses to the Corporation Tax Green Paper published in 1982 showed a strong general desire to retain the imputation system. I accept that. But other changes are needed (MP)

86. The current rates of Corporation Tax are far too high, penalising profit and success, and blunting the cutting edge of enterprise. They are ~~[illegible] (JOS)~~ the product of too many special reliefs, indiscriminately applied and of diminishing relevance to the conditions of today. Some of these reliefs reflect economic priorities or circumstances which have long vanished, and now serve only to distort investment decisions and choices about finance. Others were introduced to meet short-term pressures, notably the upward surge of inflation. With

(PEM - numbers don't help) inflation down to 5 per cent and clearly set to go lower, this is clearly the time to take a fresh look. And with unemployment as high as it is today, it is particularly difficult to justify

(NM) loss-making

a tax system which encourages low-yielding or even [unprofitable] investment at the expense of jobs.

87. My purpose therefore is to phase out some unnecessary reliefs, in order to bring about, over time, a markedly lower rate of tax on company profits.

88. First, capital allowances. Over virtually the whole of the post-war period there have been incentives for investment in both plant and machinery and industrial (though not commercial) buildings. But there is little evidence that these incentives have strengthened the economy or improved the quality of investment. Quite the contrary: the evidence suggests that businesses have invested substantially in assets yielding a lower rate of return than the investments made by our principal competitors. Too much ~~of~~ NM British investment has been made because the tax allowances make it look profitable, rather than because it would be truly productive.

(PEM - pro rated of 100 95 or 101)

89. The nation needs more high quality investment, ~~and~~ The 6 per cent increase forecast for this year takes account of the measures I have announced is encouraging. [But the greatest benefits flow from investment] But higher investment will only bring proper returns to the nation when business decisions based on are (AR) [analysis of] MP future market assessments, not future tax assessments.] This is a most encouraging prospect

90. I propose to restructure the capital allowances in three annual stages. In the case of plant and machinery, and assets whose allowances are linked with them, the first

year allowance will be reduced from 100 per cent to 75 per cent for all such expenditure incurred after today, and to 50 per cent for expenditure incurred after 31 March next year. After 31 March 1986 there will be no first year allowances, and all expenditure on plant and machinery will qualify for annual allowances on a 25 per cent reducing balance basis.

91. In addition, from next year annual allowances will be given as soon as the expenditure is incurred, and not, as they are today, when the asset comes into use. This will [bring forward the entitlement to annual allowances for those] assets, such as ships and oil rigs, for which some payment is normally made well in advance of their being brought into use.

be of great benefit to owners of (MP)

92. For industrial buildings, I propose that the initial allowance should fall from 75 per cent to 50 per cent from tonight, and be further reduced to 25 per cent from 31 March next year. After 31 March 1986 the initial allowance will be abolished, and expenditure will be written off on an annual 4 per cent straight line basis. I should add that, when these changes have all taken place, [in respect of] both plant and machinery and industrial buildings, tax allowances will still on average be rather more generous than would be provided by a strict system of [economic] depreciation.

for 2 (MP)

commercial (NM)

93. The changes in the rates of allowances will not apply to payments under binding contracts entered into on or before today, provided that the expenditure is incurred within the

next three years.

94. After consulting my Rt Hon Friend the Secretary of State for Trade and Industry, I have decided to make transitional tax arrangements for certain investment projects in the regions. Existing capital allowances will continue to apply to expenditure on projects in Development Areas and special Development Areas for which regional development grants are available and offers of selective assistance have already been made between 1 April 1980 and today. Similar arrangements were announced for regional development grants in my Rt Hon Friend's White Paper on Regional Industrial Development last December.

95. Over the same period to 31 March 1986 most other capital allowances will be brought into line with the main changes I have announced. The Inland Revenue will be issuing a press notice tonight giving full details of these proposals.

(Taken in 89 - PEM)

96. Next, stock relief. As the House will recall, this was introduced by the last Labour Government as a rough and ready form of emergency help to businesses facing the ravages of high inflation. Th[o (MP)]ese days are past; and relief is no longer necessary; [for] (MP) company liquidity has improved and, (MP) [above all], inflation has fallen sharply ~~and will be falling further during this Parliament.~~ So (MP) [Accordingly], I propose to abolish stock relief from this month.

? reframe it (MP)

MP

97. The changes [I have] just announced, in capital allowances
the Government to make
and stock relief, enable [me to embark on a] major [programme of
MP
progressive] reductions in the main rate of Corporation Tax. For profits earned in the year just ending, on which tax is generally payable in 1984-85, the rate will be cut from 52 per cent to 50 per cent. For profits earned in 1984-85 the rate will be further cut to 45 per cent. Looking further ahead, to profits earned in 1985-86, the rate will go down to 40 per cent; and for profits earned in 1986-87 the main rate of Corporation Tax will be 35 per cent. That will mean a cut of no less than 17 percentage points over 3 years (NM)

98. All these rates for the years ahead will be included in this year's Finance Bill.

MP - earlier
99. And they will bring a further benefit. [Responses to the Corporation Tax Green Paper published in 1982 revealed a strong and general desire to retain] our imputation system of
(NM) which will be kept MP
Corporation Tax. [This] allows a company to offset in full all
offset (NM - technical)
interest paid. But only a partial [deduction] for dividends is allowed. Companies thus have an unhealthy incentive to finance themselves through borrowing, in particular bank borrowing, rather than by raising equity capital. The closer the Corporation Tax rate comes to the basic rate of income tax, the smaller this undesirable distortion becomes.

100. Of course, the majority of companies are not liable to pay the main rate of Corporation Tax at all. For them it is the small companies' rate, at present 38 per cent, which applies.

I propose to reduce this rate forthwith to 30 per cent, for profits earned in 1983-84 and thereafter.

101. The Corporation Tax measures I have just announced will cost £280 million in 1984-85. In 1985-86 the cost will be £~~600~~ 450 (NM) million - made up of £1,1~~50~~ 00 (NM) million by way of reductions in the rates, only partially offset by a £~~550~~ 650 (NM) million reduction in the value of the reliefs. The estimated costs for later years, which have been provided for in the MTFS figures contained in the Budget Red Book, have been drawn up on a cautious basis. Thus business and industry can go ahead confidently on the basis of the Corporation Tax rates I have announced today, and which set the framework of company taxation for the rest of this Parliament.

[Take in 89? PEM]

MP - omit?

[102. I expect these changes to have both a somewhat different impact in the short and long term. In the short term, some investment should be brought (NM) forward over the next two years, to take advantage of high first year capital allowances while they last - a prospect made all the more alluring for business by virtue of the fact that profits earned will be taxed at the new lower, rates. But the more] important and durable long term (NM) effect will be to encourage the search for investment projects with a genuinely worthwhile return, and to discourage uneconomic investment.

103. It is doubtful ~~if~~ whether (MP) it was ever really sensible to subsidise capital investment (NM) irrespective of the true rate of return. Certainly,

with over three million unemployed it cannot make sense to do so.

MP - put after 102

[104. These changes hold out an exciting opportunity for British industry as a whole: an opportunity further to improve its profitability, and to expand, building on the recovery that is already well under way. Higher ~~net~~ NM profits after tax (NM) should encourage and reward enterprise and stimulate [higher current expenditure ~~and~~ on] NM innovation in all its forms - research and development and work on new products, processes and markets.] They are the centre-piece, for business, of this Budget and the tax strategy for this Parliament.

105. ~~But~~ NM I have further measures to announce that are relevant to business.

106. First, the Business Expansion Scheme, introduced last year as a successor to the Business Start Up Scheme, has been widely welcomed as a highly imaginative scheme for encouraging individuals to invest in small companies. It is already proving a considerable success. It now needs time to settle down, and I have only one change to propose this year.

I don't think it appropriate to apply this to md -

107. The scheme was designed to offer generous incentives for investment in high risk areas by new or expanding companies. Farming is clearly not an area which falls within this category, and I therefore propose that from today farming should cease to be treated as a qualifying trade under the scheme. I am

also ready to consider tightening the scheme further, if it becomes clear at any time in the future that it is being used for purposes for which it was clearly not designed.

which will (MP)

108. Secondly, as a measure [of] help [to] small firms, I propose to raise the VAT registration threshold with effect from midnight tonight from £18,000 to £18,700.

in line with Draft

109. Thirdly, in keeping with what I have said about removing distortions, I propose to abolish two reliefs in the personal tax field which were introduced at a time when this country suffered from excessively high rates of income tax. As we have reduced those rates, the reliefs are no longer justified.

110. The first distortion is the 50 per cent tax deduction (falling after 9 years to 25 per cent) applied to ~~given from~~ the [emoluments] pay (MP) of foreign domiciled (NM) employees working here for foreign employers. These (NM) ~~Foreign~~ employees are often paying much less tax here than they would either at home or in most other European countries. At present income tax rates, the need for the relief has clearly disappeared. Moreover it is open to widespread abuse. It is, for example, possible for the son of an immigrant, working here for a foreign company, to pay tax on only 75 per cent of his salary, even if he himself has lived in this country all his life. I therefore propose to withdraw the relief entirely for all new cases from today, and to withdraw the 25 per cent deduction from existing beneficiaries from 6 April next. For those already here (NM) The 50 per cent deduction will be phased out over the

5 years to 5 April 1989.

111. I also propose to withdraw the so-called foreign earnings relief for United Kingdom residents who work (MP) [perform their duties] both here and overseas and who spend at least 30 days abroad in a tax year. This relief was justified in (MP) [too has lost its rationale, which harks back to] the days of penalty high income tax rates but not now (MP). It too has been exploited, in particular by those who prolong their overseas visits purely in order to gain a tax advantage. For ~~the same reason~~ similar reasons (NM), I propose to withdraw the matching relief for the self-employed who spend 30 days abroad, and for resident employees and the self-employed who have separate employments or separate trades carried on wholly abroad. The relief will be halved to 12½ per cent in 1984-85 and removed entirely from 6 April 1985. However, I have also authorised the Inland Revenue to consult interested parties about a possible relaxation in the rules governing the taxation of expenses reimbursed to employees for travel overseas. I am not making any change to the 100 per cent deduction given for absences abroad of 365 days or more. (MP)

112. The abolition of these reliefs will eventually yield revenue savings of over £150 million; and represents another useful step in the removal of complexity and distortions.

113. I need to set the car benefit scales for 1985-86 for those provided with the use of a car by their employer.

Despite the increases over recent years, the levels still fall short of any realistic measure of the true benefit. So I am [accordingly] proposing an increase of 10 per cent in both the car and car fuel scales with effect from April 1985.

MP

114. Unnecessarily high rates of tax discourage enterprise and risk taking. This is true of the capital taxes, just as it is of the corporation and income taxes. It is a matter of particular concern to those involved in running unquoted family businesses. The highest rates of capital transfer tax are way out of line with comparable rates abroad, and with the top rates of other taxes in this country. I propose therefore to reduce the highest rate of capital transfer tax from 75 per cent to 60 per cent and to raise the threshold to £64,000 in line with indexation. [For lifetime gifts I further propose to ~~make~~ the rate one-half ~~of~~ that on death ~~over the whole scale.~~] (NM)

inflation

simplify the scale so that

on lifetime gifts generally will be

misleading

[PSM - incomprehensible]

115. For capital gains tax I will, as promised, bring forward in the Finance Bill proposals to double the limit for retirement relief to a figure of £100,000, backdated to April 1983. A consultative document on other possible changes in this relief is being issued next week. I am proposing no other changes this year in capital gains tax beyond the statutory indexation of the exempt amount from £5,300 to £5,600. However, the tax continues to attract criticism - not least for its complexity - and that is a matter to which I hope to return in a later year.

116. We have done much to improve the Development Land Tax. Early in the last Parliament, my predecessor increased the threshold from £10,000 to £50,000. I now propose a further increase to £75,000, which will reduce the number~~s~~ of cases (NM) affected by the tax by more than one-third.

117. Next share options. The measures introduced in the last Parliament to improve employee involvement through profit sharing and savings related share option schemes have been a notable success. The numbers (MP) of all these employee schemes open to all employees (NM) have increased from about 30 in 1979 to over 670 now, benefiting some half a million employees. To maintain and build on this progress I propose to increase the monthly limit on contributions to savings related share option schemes from £50 to £100. I have also authorised the Inland Revenue to double the tax-free limits under the concession on long service awards and to include the gift of shares within those limits (NM) in the employee's company.

118. But beyond this, [I am convinced that] MP we need to do more to attract top calibre company management and to increase the incentives and motivation of existing executives and key personnel by linking their rewards to performance. I propose therefore that, subject to certain necessary limits and conditions, share options generally will be taken out of income tax, leaving any gain to be charged to capital gains tax on ultimate disposal of the shares. The new rules will

apply to options meeting the conditions which are granted from 6 April.

119. I am sure that all these changes will be welcomed as measures to encourage the commitment of employees to the success of their companies and to improve the performance, competitiveness and profitability of British industry.

120. Before turning to North Sea taxation, I should like to remind the House of the Government's concern at the threat which the spread of unitary taxation in certain US states has posed to the US subsidiaries of British firms. With our European partners we are monitoring the situation closely, and await with keen interest the imminent report of ~~a~~ Secretary Regan's Working Group ~~under my US counterpart~~. It is very important that a satisfactory solution be speedily implemented.

I'd want out — too much of hint of retaliation. Shouldn't highlight oil — no one in US wd go to stake for oil & oil investment v. impt to UK. Also MP ?NM

[~~121. This issue isnot wholly irrelevant to the North Sea, for US firms operating there, or elsewhere in this country, are not of course taxed on a unitary basis, taking account of world-wide profits.~~]

122. Last year's North Sea tax changes were well received, and there has been encouraging progress in the number of development projects coming forward, as well as in exploration and appraisal. The Government is already committed to a study of the economics of investment in [incremental development in] new projects within (MP) existing fields. This is of increasing importance and in consultation with my rt hon friend the Secretary of State for Energy I

therefore propose to review this area with the industry, and to legislate as appropriate next year to improve the position. To prevent projects being deferred pending this review, the (MP) any changes will apply to all projects which receive development consent after today.

(PEM) The measures I have just announced will have considerable benefits for North Sea companies. So

123. Meanwhile, I am taking two measures to prevent an unjustified loss of tax in the North Sea. First, in addition to the PRT measures on farmouts which I announced last September, I am limiting the potential Corporation Tax cost of such deals. Second, I propose to repeal the provision which allows Advance Corporation Tax to be repaid where Corporation Tax is reduced by PRT. ~~I have concluded that this can no longer be justified.~~ I have also reviewed the case for extending last year's future field concessions to the Southern Basin, but have concluded that additional incentives here are not needed.

124. I have just two further changes affecting business to propose, both of which will come into force on 1 October.

125. Ever since VAT was introduced in this country, we have treated imports differently from the way ~~in which they are treated by~~ our main European Community competitors that them (MP). In a nutshell, they require VAT on imported goods to be paid in the same way as customs duties. We do not. Under our system an importer does not have to account for VAT on his

imports until he makes his normal VAT return, on average some 11 weeks later. During this time the importer enjoys free credit at the taxpayer's expense. This is an advan-
goods produced at home competing with
(MP) tage not enjoyed by [the home-produced equivalent of the] imports, since businesses buying from UK suppliers have to pay VAT when they pay their suppliers.

126. The UK system does indeed have many advantages, which is why the European Commission has for some years now been seeking to get it adopted throughout the Community, with the full support of both my predecessor and myself. But the plain fact is that in all that time the Commission has made no progress whatever.

127. I must tell the House that I am not prepared to put British industry at a competitive disadvantage in the home market any longer. Should our European partners at any time undergo a Damascene conversion, and [redacted] agree that the Commission's proposal should be accepted after all, then of course we would [gladly] revert to the present system. But in the meantime I propose to move to the system used by our major competitors and charge VAT straight away on imports, providing the same facilities for deferring payment as apply to customs duties. That means that most importers will be able to defer payment of VAT by on average one month from the date of importation. But that is all.

[PEM - Do we want to say why we have not made special arrangements for raw materials / exporters]

[AR - reference needed to tell people this won't involve disruption at ports & frontiers.]

128. As I have said, this change will apply from 1 October. By bringing forward VAT receipts, it will bring in an extra £1.2 billion in 1984-85, some of which will of course be born ~~carried~~ by foreign producers and manufacturers. There will naturally be no increased revenue in subsequent years.

129. The second change I propose to make on 1 October concerns the National Insurance Surcharge. This, once tax on jobs again, was a unhappy brainchild of the Labour Government - in particular (MP-radio) Rt Hon member for Leeds East. Having introduced it in 1977 at the rate of 2 per cent, he then raised it in 1978 to 3½ per cent. During the last Parliament, this Government reduced (MP) [my predecessor succeeded in reducing] it to 1 per cent, and we are pledged to abolish it during the lifetime of this Parliament.

130. Given the impact that this tax has, not only on industrial costs but also - at a time of high unemployment - on jobs, I have decided to take the opportunity of this my first Budget to fulfil that pledge. Abolition of the National Insurance Surcharge from October will reduce private sector employers' costs by almost £350 million in 1984-85, and over 900 (NM) ~~£850~~ million in a full year. Its abolition is thus of continuing help to British industry (PEM).

131. Thus my proposals offer British business the abolition of the tax on jobs and the reduction of the rate of taxation on profits. They also sweep away a number of out-dated reliefs, reduce distortions, and assist enterprise.

INDIRECT TAXES

131. Having announced major reforms of both the taxation of savings and investment and the taxation of business, I turn now to the third and final area in which I propose to make progress on tax reform. This is the taxation of personal income and spending.

132. The broad principle was clearly set out in the Manifesto on which we were first elected in 1979 and which emphasised the need for a switch from taxes on earnings to taxes on spending. My predecessor made an important move in this direction in his first budget, and the time has come to make a further move today. To reduce direct taxation by this means is important in two ways. It improves incentives and makes it more worthwhile to work, and it increases the freedom of choice of the individual.

check quotation

133. I do not however see the excise duties - with certain exceptions - as an area for major change. I shall of course need to raise most of the duties broadly in line with inflation, so as to maintain their real value: not to do so would run counter to the philosophy I outlined a moment ago. But with inflation now as low as it is, the necessary increases are on the whole mercifully modest. Only for a few particular duties do I envisage steeper rises.

134. One significant exception is tobacco, where I ~~am~~ believe it is right ~~convinced of the need~~ to raise the duty in real terms, given ~~to help cut smoking and thus reduce~~ the potential danger to health. I therefore propose an increase in the tobacco duty which, including VAT, will put 10p on the price of a packet of cigarettes, with corresponding increases for hand-rolling tobacco and cigars. This will do no more than restore the tax on tobacco to its 1965 level. I do not propose to increase the duty on in pipe tobacco, at all (MP) which is important for a great many pensioners. These changes will take effect from midnight on Thursday.

135. For the duties on petrol and derv I propose simply to raise them broad in line with prices than (MP) [revalorisation, which] means increases which, again including VAT, will raise ~~increase~~ the price at the pumps by 4½p and 3½p a gallon respectively. I do not propose to increase the duty on heavy fuel oil, which is of particular importance to industrial costs. These changes will take effect for oil delivered from refineries and warehouses from six o'clock this evening.

136. There is one excise duty which I propose to do away with altogether. Many of those who find it hardest to make ends meet, including in particular many pensioners, use paraffin stoves to heat their homes, and it is with them in mind that I propose to abolish the duty on kerosene from six o'clock tonight. I am sure that this will be welcomed on all sides of the House.

137. The various rates of Vehicle Excise Duty will, once again, go up roughly in line with prices. Thus the duty for cars and light vans will be increased by £5, from £85 to £90 a year. However, in the light of the reassessment given the further evidence my Rt Hon Friend the Secretary of State has made of HGVs) now received on the wear and tear that various types of vehicle cause to the roads, there will be reductions in duty for the lightest lorries, offset by higher increases for some heavier lorries. All these changes in Vehicle Excise Duty will take effect from tomorrow.

138. However, I propose to exempt from Vehicle Excise Duty all recipients of the War Pensioners' Mobility Supplement.

~~139.~~ And I have decided to widen the specific ~~VAT reliefs~~ reliefs for the disabled in this ~~the important~~ area ~~of transport~~. In addition The existing VAT relief for motor vehicles designed or adapted for use by the handicapped will be extended, and matched by a new Car Tax relief. The effect will be that neither VAT nor car tax will apply to family cars designed for disabled people or substantially adapted for their use.

140. I now come to the most difficult decision I have to take in the excise duty field. As the House will be aware, the rules of the European Community, so far as alcoholic drinks are concerned, are designed to prevent a Member state from protecting its own domestic product by imposing a significantly higher duty on competing imports. In pursuit of this, the Commission has taken a number of countries to the European Court of Justice.

141. In our case, the Commission contended that we were protecting beer by under-taxing it in relation to wine. We fought the case, but lost; and I am now implementing the judgement handed down by the Court last year. Accordingly, I propose to increase the duty on beer, ~~not by the 7p a pint which has been widely rumoured in the press, but~~ by the minimum amount needed to comply with the judgement and maintain revenue: 2p on a typical pint of beer, including VAT. At the same time, the duty on table wine will be reduced by the equivalent of about 18p a bottle, again including VAT.

forecast

small

142. I cannot, however, ignore the fact that while we comply with the judgement of the European Court, one of our partners appears determined not to do so. I refer to Italy, which has been ordered by the Court to remove forthwith its discrimination against Scotch whisky, but as yet shows no sign whatever of complying. I have therefore decided to introduce a temporary duty surcharge on vermouth of some 20p a bottle on top of the basic increase, to which I shall come in a moment. This surcharge will come into operation on 1 September unless the Italian Government has - as I very much hope it will - implemented the Court's judgement by that date, and it will lapse as soon as I am satisfied that it has complied.

MP

143. As for the rest of the alcoholic drinks, cider, which increasingly competes with beer but attracts a lower duty, will go up by 3p a pint. The duties on made-wine will be aligned with those on other wine. And I propose to increase the duty on sparkling wine, fortified wine and spirits by about 10p a

bottle, including VAT. All these changes~~, except the vermouth surcharge,~~ will take effect from midnight tonight.

144. These changes in excise duties will, all told, bring in some £840 million in 1984-85, some £200m more than is required to keep pace with inflation. The addition is of course ~~largely~~ due to the increase in tobacco duty.

145. But much of the extra revenue I need to make a substantial switch this year from taxes on earnings to taxes on spending will come from VAT. I propose no change in the rate of VAT. Instead, I intend to broaden the base of the tax by extending the 15 per cent rate to two areas of expenditure that have hitherto been zero-rated.

146. First, alterations to buildings. At present repairs and maintenance are taxed, but alterations are not. The borderline between these two categories is the most confused in the whole field of VAT. I propose to end this confusion and illogicality by bringing all alterations into tax. However, to allow a reasonable time for existing commitments to be completed or adjusted, the change will be deferred until 1 June.

147. Secondly, food. Most food is zero-rated. But food served in restaurants is taxed, together with a miscellaneous range of items including ice-cream, confectionery, soft drinks and crisps, which were brought into tax by the Labour Government (MP) [Rt Hon Member for Leeds East.] Take-away food clearly competes with other

forms of catering, and I therefore intend to bring into tax hot take-away food and drinks, with effect from 1 May.

148. The total effect of the extensions of the VAT coverage which I have proposed will be to increase the yield of the tax by £375 million in 1984-85 and by ~~almost~~ £650 million in 1985-86.

149. The total impact effect on the Retail Price Index of the VAT changes and excise duty changes taken together will be less than three-quarters of one per cent. This has already been taken into account in the forecast which I have given to the House of a decline in inflation to 4½ per cent by the end of the year.

150. The extra revenue raised in this way will enable me within the overall framework of a neutral Budget to lighten the burden of income tax.

PERSONAL TAXATION

151. Since we took office in 1979, we have cut the basic rate of income tax from 33 per cent to 30 per cent and sharply reduced the confiscatory higher rates inherited from the last Labour Government. We have increased the main tax allowances not simply in line with prices but by around 8 per cent in real terms. It is a good record. But it is not enough. The burden of income tax is still too heavy.

152. During the lifetime of this Parliament, I intend to carry much further the progress we have already made. For the most part, this will have to wait for future Budgets, particularly since I have thought it right this year to concentrate on setting a new regime of business taxation for the lifetime of a Parliament - and beyond. But as a result of the changes to taxes on spending which I have just announced, I can make a start now.

153. I propose to make no change this year in the rates of income tax. So far as the allowances and thresholds are concerned, I must clearly increase these by the amounts set out in the statutory indexation formula, based on the 5.3 per cent increase in the Retail Price Index to December. The question is how much more I can do, and how to direct it.

154. I have decided that, this year, the right course is to use every penny I have in hand, within the framework of a revenue neutral Budget, to lift the level of the basic tax thresholds, for the married and single alike. It is fundamentally wrong that we *makes no sense to be collecting* collect income tax from people *who are at the same time receiving* whose incomes are so low that they are entitled to social security benefits *means-tested benefits* on grounds of need. Moreover low tax thresholds make the poverty and unemployment traps much worse, so that the financial incentive to find a better job or even *not* any job may decline almost to zero. There is, alas, no quick or cheap solution to these problems. But that is all the more reason to make a start on solving them now.

155. I propose to increase most thresholds in line with the statutory requirement, and by no more. The first higher rate of 40 per cent will apply when taxable income reaches £15,400 a year and the top rate of 60 per cent to taxable income of £38,100 or more. The single age allowance will rise from £2,360 to £2,490 and the married age allowance from £3,755 to £3,955.

156. For the basic thresholds, statutory indexation would mean putting the single and married allowances up by £100 and £150 respectively. I am glad to say that I can do considerably better than that. I propose to increase the basic thresholds by well over double what is required by indexation. The single person's threshold will be increased by £220, from £1,785 to £2,005; and the married threshold by £360, from £2,795 to £3,155. ~~The special allowances for widows, and for single parents, will as a consequence go up by some 14 per cent.~~

157. This is an increase of around 12½ per cent, or some 7 per cent in real terms. It brings the married man's tax threshold for 1984-85 to its highest level in real terms since the war. It means that every tax-paying married couple in the land will enjoy an income tax cut of at least £2 a week. And it means that a large number of people, those with the smallest incomes of all, are taken out of income tax altogether. ~~And~~ Some 850,000 people - over 100,000 of them widows - will not pay tax in 1984-85 who would have paid if thresholds had not been

will pay no tax in 1984-85 - that is (MP)

increased. And 400,000 fewer than if the allowances had merely been indexed.

158. All these changes will take effect under PAYE on the first pay day after 10 May. Their cost is considerable: some £1.8 billion in 1984-85, of which roughly half represents the cost of indexation.

159. This is as far as I can go on income tax this year, within a broadly revenue-neutral Budget for 1984-85. But as I have already said, so long as we hold to our published planned levels

and while we keep to the (MP)

of public spending, there is an excellent prospect consistent

Government (MP) There is an excellent prospect

with the necessary downward path of public borrowing of further tax cuts in next year's Budget. These would be on top of the measures I have announced in this Budget which, as I have already told the House, will reduce taxation in 1985-86 by some £1¾ billion, with business taking the lion's share. So for next year I would hope to be concentrating on further help to people

especially cuts

individuals, and principally on income tax. (MP)

CONCLUSION

160. I have, Mr Deputy Speaker, completed the course I charted at the outset this afternoon. I have described the recovery, and how the Government plans to sustain it, by working for further reductions in inflation, by maintaining sound money and by curbing borrowing. I have described a three part reform strategy for a fairer, simpler tax system. And I have been able to propose substantial tax reductions over two years in a Budget that is revenue-neutral for 1984-85. It is a Budget for responsibility and reform; and I commend it to the House.

FEV1f

BUDGET CONFIDENTIAL

FROM: A. M. BAILEY

8th March, 1984.

MR. KERR

c.c. Mr. Scholar

Mr. Hopkinson

CALKE ABBEY

You asked for some sentences (not to appear in the written text). I suggest adding after the first sentence of Block G:

54/55. ~~Are~~ But lest the innovation seem too sweeping, I can make

55. [~~Within th~~ese ~~plans, I have only~~ one small anouncement, ~~to make~~ within the plans, which I think the House will welcome. We have been able to provide the National Heritage Memorial Fund with additional resources which will enable them among other things to secure the future of Calke Abbey. My Right Hon friend the Secretary of State for the Environment is providing £6.~~5~~3 million from his planned expenditure for this year and next, and I have accepted a claim on the Reserve of £2 million for next year.]

Then amend following sentence to read:

Today I want to consider the public expenditure issue in a wider perspective.

AMB

A. M. BAILEY

B(84) 1018.

PWP

Agreed

FROM: T LANKESTER
DATE: 8 March 1984

MISS J C SIMPSON

cc Mr Pirie

BUDGET SPEECH, BLOCK I: SAVINGS AND INVESTMENT

There is one further amendment I should like to suggest to this Block. In paragraph 12, it would be better if the phrase - "which are coming to resemble each other more and more closely" - were deleted. Including this phrase will be something of a hostage to fortune in the context of the Building Societies' Green Paper, in which we are planning to take a fairly conservative line on what the Societies will be allowed to do in future. Ideally, the last sentence of paragraph 12 should also be amended so that it reads:-

> "They should be able to do so on more equal terms as far as tax is concerned".

T LANKESTER

Ch/Ex Ref No B(84)549

FROM: J O KERR
DATE: 8 MARCH 1984

Mr Kerr
Pretty good stuff. Some comments inked in.
PM

Sir P Middleton

cc Sir T Burns
Mr Battishill
Mr Folger
Mr Portillo

Mr Fraser: C & E

... I attach the latest complete draft of the Budget Speech, and would be most grateful if any suggested amendments could reach me by lunchtime on 9 March. Sections of the Speech are of course being circulated more widely.

JOK.

J O KERR

INTRODUCTION

This Budget will set the Government's course for this Parliament. It is founded on the policies which we have consistently followed since 1979.

2. Consistency of purpose is the hallmark of this Government. It is the only way to improve economic performance and lay the foundations for future prosperity, more jobs and lower taxation. Above all, it is the only way to defeat inflation and achieve our ultimate objective of stable prices.

3. The results of the Medium Term Financial Strategy introduced in 1980 can be seen in ~~four~~ three years of falling inflation, down now to the lowest levels since the sixties. And that in turn has brought a steady recovery of output, rising living standards and, more recently, rising employment.

4. The facts speak for themselves. They are a tribute to the courage and foresight of the five Budgets presented from this Despatch Box by my distinguished predecessor, the present Foreign Secretary, whose duties sadly keep him in Brussels today.

5. Today's Budget has two themes: first, the further reduction of inflation, which will further improve the prospects

for jobs; and second, the reform and simplification of the tax system~~, which will make it fairer for all~~.

6. I shall begin by reviewing the economic background to the Budget. I shall then deal with the medium term financial strategy; with monetary policy and the monetary targets for next year; and with public borrowing and the appropriate PSBR for the coming year. I shall then turn to public expenditure, including the prospects for the longer term. Finally I shall deal with taxation, and the changes in the structure of taxation which will pave the way for cuts in taxes in subsequent years. Some of these cuts I shall announce today, for this is in a sense a Budget for two years. In a wider sense it is a tax reform Budget, setting out a tax strategy for this Parliament.

7. As usual, a number of press releases, ~~will be issued today~~, filling out the details of my tax proposals, will be available from the Vote Office as soon as I have sat down.

THE ECONOMIC BACKGROUND

8. But I start with the economic background, and the convincing evidence of recovery: a recovery that springs from the monetary and fiscal policies to which we shall hold.

9. Since 1980, inflation has fallen steadily from a peak of over 20 per cent. Last year it was down to about 4½ per cent, the lowest figure since the sixties. And with lower inflation have come lower interest rates.

10. The underlying strength of the recovery is clear. Whereas in some previous cycles recovery has come from a self-defeating stimulus to monetary demand, this time its roots are in our commitment to sound finance and honest money. Lower inflation and lower interest rates benefit industry, business, and consumer confidence. Falling inflation has made room for real growth, as we always said it would.

11. Across the economy, total money incomes grew in 1983 by about 8 per cent, of which 3 per cent represented real growth in output. Although there is still room for improvement, this ~~clearly~~ is a very much healthier division between inflation and real growth than the nation experienced in the 1970s. Output in the second half of 1983 is now reckoned to have exceeded the previous peak, before the world recession set in, and is still rising strongly.

12. Productivity too has continued to improve rapidly. Just as over the past year many have wrongly predicted an end to the recovery, so some have tried to dismiss the sharp rise in productivity as a flash in the pan. Yet during 1983 manufacturing productivity grew by 6 per cent with no sign of slowing down. Unit labour costs across the whole economy are likely to show the smallest annual increase since the 1960s. This has allowed a welcome and necessary recovery in real levels of profitability.

13. Higher profits lead to more jobs. The number of people in employment increased by about 85,000 between March and September last year. The loss of jobs in manufacturing has slowed down sharply, while jobs in services increased by getting on for 200,000 in the first nine months of last year. This is encouraging news for the unemployed and those who will be leaving school this summer.

14. But further progress ~~on productivity~~ is needed: although our unit wage costs in manufacturing rose by under 3 per cent last year, such costs actually fell in the US, Japan and Germany, our three biggest competitors. The employment prospect would be significantly improved if a bigger contribution to improved competitiveness ~~productivity~~ were to come from lower pay rises. Good sense about pay remains vital.

15. Demand, output, profits and employment all rose last year. Home demand has played the major part in the recovery so far. Lower inflation reduced people's need to save and real

incomes rose. Personal consumption increased by over $3\frac{1}{2}$ per cent compared with 1982. Fixed investment rose rather faster than consumption, with investment in housing and services particularly strong.

16. Imports rose a little faster than home demand last year, as the UK emerged from recession ahead of our main trading partners - our rate of economic growth last year was the highest in the European Community. For much of 1983 our export performance reflected the weakness in many of our overseas markets. But by the end of last year world trade was clearly moving ahead again, and in the three months to January manufacturing exports increased very substantially. The balance of payments on current account last year is estimated to have been in surplus by about £2 billion.

17. Our critics have been confounded by the combination of recovery and low inflation. Even the pessimists have been forced to acknowledge the strength of the recovery. It is set to continue throughout this year at an annual rate of 3 per cent. Inflation is expected to remain low, edging back down to $4\frac{1}{2}$ per cent by the end of this year. With rising incomes and low inflation, personal consumption will continue at a higher level. to grow. And the recovery is already becoming more broadly based. Encouraged by improved profitability and better long-term growth prospects, investment is expected to rise by 6 per cent this year.

18. Looking abroad, economic prospects are also more favourable than for some time. Output in the United States should continue to grow strongly this year. And recovery is spreading to the rest of the world.

19. Of course, there are inevitable risks and uncertainties. The size and continued growth of the United States budget deficit causes widespread concern, not least among Americans, and keeps American, and hence international, interest rates high. This acts as a brake on world recovery and worsens the problems of the debtor countries. Another consequence is a massive and still growing deficit in the US current balance of payments, financed by inflows of foreign capital, and leading to mounting pressures for protectionism within the United States, and sharp exchange rate movements. It is an unstable situation, creating worrying uncertainties.

20. A second potential risk is disruption in the oil market. The immediate prospects are less obviously volatile than they were a year ago. But uncertainties remain, and the United Kingdom, and indeed the world economy, inevitably remains vulnerable to any major disturbances.

21. But despite these risks there is a growing sense throughout the industrialised world that the recovery this time ~~is not merely cyclical, but~~ ~~one which~~ can be sustained. The essential requirement is the continued pursuit of prudent monetary and fiscal policies.

is not a temporary upward blip but can ..

we have not completely abolished the cycle

THE MTFS

22. For the United Kingdom, the Medium Term Financial Strategy has been the cornerstone of such policies. It will continue to play that role; to provide a framework and discipline for Government and to set out clearly, to industry and the financial markets, the guidelines of policy. Too often in the past Governments have abandoned financial discipline whenever the going got rough, and been driven to stagger from one short-term policy expedient to another. The temptation to accommodate inflationary pressures proved irresistible, and the nation's longer-term economic performance was progressively undermined.

23. The discipline of the MTFS was designed to ensure consistency between monetary and fiscal policies, and a proper balance in the economy. It is so designed to ensure that the more inflation and inflationary expectations come down, the more room is available for output and employment to grow.

24. People now know that the Government intends to stick to its medium term objectives. They understand that the faster inflation comes down, the faster output and employment recover. Increasing realism, and flexibility in the economy, owes much to the pursuit of firm and consistent policies within the MTFS framework.

25. Originally the MTFS covered four years. In this first Budget of a new Parliament we have thought it is appropriate to carry it forward for five years. So the MTFS published today in the Financial Statement and Budget Report -the Red Book - shows a continuing downward path for the monetary target ranges over the next five years, and a path for public borrowing consistent with that reduction. It takes full account of important influences such as the pattern of North Sea oil revenues, and the level of asset sales arising from the privatisation programme. For the last two years of the new MTFS, which lie beyond the period covered in last years Public Expenditure Survey and last month's White Paper, the Government has not yet made firm plans for public spending. But the MTFS assumption - and it is no more than an assumption - is that the level of public spending in 1987-88 and 1988-89 will be the same in real terms as that currently planned for 1986-87.

26. The precise figures set out in the MTFS are not of course a rigid framework, lacking all flexibility. As in the past, there may well need to be adjustments to take account of changing circumstances. But such changes will be made only when they will not jeopardise the consistent pursuit of the Government's objectives.

MONETARY POLICY

27. Monetary policy will continue to play a central role. For further reductions in monetary growth are needed to achieve still lower inflation.

28. Over the twelve months to mid-February the growth of £M3 has been well within the 7-11 per cent target range, with M1 and PSL2 at or a little above the top of it. While in the early months of the target period most measures of money showed signs of accelerating, growth in all the target aggregates has since the summer been comfortably within the range.

29. Other evidence confirms that monetary conditions are satisfactory. The effective exchange rate has remained fairly stable, despite the international uncertainties and instability which I have described. And nominal interest rates have continued to decline in line with falling inflation.

30. To maintain sound monetary conditions in the years ahead the monetary targets must reflect changes in the financial system and in the significance of different measures of money. There is nothing new in this. Over the years we have altered the target ranges and aggregates to take account of such changes. But the thrust of the strategy has been maintained.

31. One important development has been the attempt to give a more explicit role to the narrow measures of money. Even when targets were set solely in terms of £M3, we recognised the significance of their behaviour. £M3 and the other broad aggregates give a good indication of the growth of liquidity. But a large proportion of this money is deposited in ways which earn interest. In defining policy it is therefore helpful also to make specific reference to measures of money which bear very little interest, and provide a good guide to the immediate potential for spending.

32. M1 was for this reason introduced as a target aggregate, but it has not proved entirely satisfactory for that purpose. Its behaviour has been dominated by changes in its large interest-bearing component, which has grown rapidly, and now accounts for 25 per cent of the total. With the introduction of new, interest bearing chequing accounts, the signs are that this will continue.

33. Other measures of narrow money have not been distorted to the same extent. In particular, MO, which consists mainly of currency, has not been subject to this development. It has been affected by other innovations that have reduced people's need for cash, but the pace of change has not diminished its value as an indicator of financial conditions. There is also the new aggregate M2, which was specifically devised to provide a comprehensive measure of transactions balances and which may in time prove a useful guide, but still needs to be interpreted with particular care.

34. In the past two years, it has been possible to set a single target range for both broad and narrow measures of money. But this will not normally be the case; for narrow monetary aggregates tend to grow more slowly than broader measures. And this year's Red Book sets out two separate ranges.

35. The target range for broad money will continue to apply to £M3, and for the coming year will be set at 6-10 per cent, as indicated in last year's MTFS. The target range for narrow money will apply to MO and for next year will be set at 4-8 per cent. To avoid any possible misunderstanding, I stress that the use of MO as a target aggregate will not involve any change in methods of monetary control.

36. Both target ranges will have equal importance in formulating policy. And we shall continue to take into account other measures of money, especially M2 and PSL2, as well as wider evidence of financial conditions, including the exchange rate. As in the past, we shall seek to influence monetary conditions by an appropriate combination of funding and operations in the money market.

37. So far as funding is concerned, the role of the National Savings movement will remain important. This year's target of £3 billion is likely to be achieved: the target for the coming year will again by £3 billion.

~~[illegible]~~ so far
£2.8bn so far

38. Precise monetary targets for the later years will be decided nearer the time. But to give a broad indication of the

objectives of monetary policy, the new MTFS, like previous versions, shows monetary ranges for a number of years ahead. These ranges are consistent with a continuing downward trend in inflation: they demonstrate the Government's intention to make further progress towards stable prices.

The gold standard ref will help with some, but will scare a lot of others. I'd drop it

PUBLIC SECTOR BORROWING ETC

39. I turn now to public borrowing. f~~or just as the classical~~ Any formula for financial discipline ~~- the gold standard and the balanced budget - had~~ must have both a monetary and a fiscal component. ~~so does~~ The medium term financial strategy makes this quite explicit.

?

40. The MTFS has always envisaged that the Public Sector Borrowing Requirement would fall as a percentage of Gross Domestic Product over the medium term. And it has, notably as a result of the courageous Budget introduced by my predecessor in 1981, which brought the PSBR down to 3½ per cent of GDP in 1981-82.

41. Since then there has been little further fall. The latest estimate of the PSBR for the current year, 1983-84, remains what it was in November: around £10 billion, equivalent to 3¼ per cent of GDP. This is significantly above what was intended at the time of last year's Budget, and would of course have been higher still had it not been for the measures taken last July.

42. We now need a further substantial reduction in borrowing, in order to help bring interest rates down further as monetary growth slows down. Sterling interest rates are, of course, also influenced by dollar interest rates and so by the US situation which I have already described: but that makes it all the more

important to curb domestic pressures. In contrast to virtually the whole of the post-war period, UK longer-term rates are now lower than American rates. As long as American rates remain near their current level, it is highly desirable that this advantage be maintained.

43. The higher level of asset sales planned as the privatisation programme gathers pace is a further reason for reducing the PSBR significantly in the coming year. Asset sales reduce the Government's need to borrow. But their effect on interest rates ~~is~~ may be less than the effect of some other [direct reductions in Government spending programmes.

44. Last year's MTFS showed an illustrative PSBR for 1984-85 of 2½ per cent of GDP, equivalent to around £8 billion. But I believe that it is possible, and indeed prudent, to aim for a somewhat lower figure. I have therefore decided to provide for a PSBR next year of 2¼ per cent of GDP, or roughly £7 billion.

45. The House will recall that in November I warned that on conventional assumptions, including the 1983 Red Book's PSBR figure of £8 billion for next year, I might have to increase taxes slightly in the Budget. I am glad to report that the latest, and more buoyant, forecasts of tax revenue in the coming year, [coupled with the decisions taken in the Public Expenditure Survey and the continuing effects of the July measures,] have changed the picture. Bringing the PSBR down to £7 billion will not

require such an increase in taxation. In fact it will require no overall net increase at all. So the measures I shall shortly announce will, after indexation, be broadly neutral in their effects on revenue in 1984-85.

46. Better still, they will reduce taxation in 1985-86 by some £1¾ billion. And the MTFS published today shows that there should be room for further tax cuts not only in 1985-86, but throughout the remainder of this Parliament, provided that we stick firmly to our published plans for public expenditure to 1986-87, and maintain an equally firm control of public spending thereafter.

PUBLIC EXPENDITURE

47. The Public Expenditure White Paper setting out our spending plans for the next three years was approved by the House last week. Today I want to consider the critically important issue of government spending in a rather wider perspective.

48. For far too long, spending has grown faster than has the economy as a whole. The trend has seemed inexorable, and the result has been that the great mass of the population have had to pay more and more in tax. To take just one example: as recently as 1963-64 no married man had to pay a penny of income tax unless his taxable income was at least 45 per cent of the average earnings level. Today the tax threshold is down to ~~little more than~~ under a third of average earnings. Over the years more and more people on lower and lower incomes have been brought into income tax.

49. We have seen a steady enlargement in the role of the State, at the expense of the individual, and a steady increase in the dead weight of taxation dragging down our economic performance as a nation.

50. Clearly this ~~dangerous~~ process has to stop. Of course, much public spending is directed to eminently desirable ends. But there is an important choice to be made; and it is not

enough simply to make marginal changes in spending programmes from year to year. The choice needs more fundamental national consideration and debate; and it needs to be set within a longer time horizon.

51. I am therefore publishing today, in addition to the customary Budget documents, a Green Paper on the prospects for public spending and taxation in the next ten years. It examines past trends; discusses pressures for still higher spending; and examines the rewards for the individual if these pressures can be contained.

52. The Green Paper concludes that, without firm control over public spending, there can be no prospect of bringing the burden of tax back to more reasonable levels. On the assumptions made in the Green Paper, the burden of taxation will be reduced to the levels of the early 1970s only if public spending does not rise in real terms over the next ten years. If, on the other hand, spending grows by 1 per cent a year in real terms after 1988-89, the tax burden would by 1993 be only just below the 1978-79 level, and still well above its level in the 1960s, even if the economy grows by about 2 per cent a year over the ten years. And of course excessive taxation slows the whole economy.

53. The Government believes that the issues discussed in the Green Paper merit the attention of the House and the country.

57. Before turning from Government spending to Government revenue, I should add a word on public sector manpower. At the beginning of the last Parliament, the Government set itself the target of reducing the size of the Civil Service from 732,000 in April 1979 to 630,000 by April of this year. That target has been achieved. We have now set ourselves the further target of 593,000 by April 1988, and I am confident that it too will be achieved, and that a leaner Civil Service will continue to operate with increasing efficiency. Speaking for my own Departments, the tax changes I shall be announcing today will reduce manpower requirements by at least 1000 which will help towards meeting the 1988 target.

TAX REFORM

58. I mentioned at the outset that this will be a radical, tax-reforming, Budget. It will also significantly reduce the overall burden of tax over the next two years taken together ~~- and indeed over the whole MTFS period~~ - and I hope to have scope for further reductions in tax in subsequent Budgets.

even after allowing for the continued effects in future years

Too dangerous in this specific form. Delivery dependent on PSBR etc as was said earlier

59. My proposals for reform are guided by two basic principles. First, the need to make changes that will improve our economic performance over the longer term. Second, the desire to make life a little simpler for the taxpayer.

60. But I am well aware that the tax reformer's path is a stony one. Any change in the system is bound, at least in the short term, to bring benefits to some and disadvantages to others. And, if I may borrow a phrase from the Rt Hon member for Leeds East, the howls of anguish from the latter group tend to be rather more audible than the murmurings of satisfaction from the former.

61. ~~Reform must succeed, but need not be, in this sense, a howling success. So~~ I have rejected the extreme suggestion, popular in some quarters, that I should scrap our income-based tax system and replace it with a brand new expenditure-based system. A reform of this kind would produce, in the real world, an upheaval of mind-boggling dimensions.

62. But I don't believe we can afford to opt for the quiet life and do nothing. So I have chosen the middle way: to work for improvements, some I believe very substantial, but within the framework of our existing income-based system. I shall also be proposing transitional arrangements where I believe it fair and appropriate to do so.

63. The changes I shall be proposing today fall into three broad categories. These are the taxation of savings and investment, business taxation, and the taxation of personal income and spending.

SAVINGS AND INVESTMENT

64. First, the taxation of savings and investment. The proposals I am about to make should improve both the (direction) structure ? and quality of both. And they will contribute further to the creation of a property-owning and share-owning democracy, in which more decisions are made by individuals rather than by intermediary institutions.

primary uses

65. First, stamp duty. This was doubled from its long-standing 1 per cent by the post-war Labour Government in 1947, reduced by the Macmillan Government in 1963, and once again doubled to 2 per cent in the first Budget presented by the Rt Hon member for Leeds East in 1974. At its present level it is an impediment to mobility and incompatible with the welcome movement to greater competition in the City, following the withdrawal of the Stock Exchange case from the Restrictive Practices Court.

66. I therefore propose to halve the rate of stamp duty to 1 per cent. [Transactions from today will benefit from the new rate, unless documents have to be stamped before 20 March, which is the earliest date on which the change will have legal effect.]

A.P.N. point. delete

67. For the home buyer, the new flat rate 1 per cent stamp duty will start at (an increased threshold of) £30,000. Below this level no duty will in future be payable, and 90 per cent of first time home buyers will therefore not be liable for stamp duty at all.

68. Reducing the rate of duty on share transfers will remove an important disincentive to direct investment in equities and increase the international competitiveness of our stock market. It should also help British companies to raise equity finance.

69. In addition, I have three proposals to encourage the issue of corporate bonds. I shall go ahead with the new arrangements for deep discount stock and the reliefs for companies issuing Eurobonds and convertible loan stock which were announced but not enacted last year. And I propose to exempt from Capital Gains Tax certain corporate fixed interest securities provided they are held for more than a year. Since such securities are already exempt from stamp duty ~~- an exemption I can confirm also extends to certain convertible loan stocks -~~ this means that the tax concessions for Government borrowing in the gilt-edged market will now be virtually the same as for private sector borrowing in the corporate bond market.

70. The reductions in stamp duty will cost £450 million in 1984-85, of which £160 million is the cost of the relief on share transfers, and £290 million the cost of the relief on transfers of houses and other real estate.

71. Next, life assurance. I have concluded that there is no longer any justification for Premium Relief on Life Assurance,

~~Bit~~ OK. but there is an obvious comeback on nationalising of [illegible] which is now only one of a number of savings channels for ordinary people. The main effect of the relief today is to encourage institutional rather than direct investment, and to spawn a multiplicity of well-advertised tax management schemes. I propose to withdraw the relief on all new policies made after today. I stress that this change will apply only to new (or newly enhanced) policies, taken out or increased after today. Existing policies will not be affected at all. The change is estimated to yield £90 million in 1984-85.

72. We must also review unjustified penalties on direct personal investment. The Investment Income Surcharge is an unfair and anomalous tax on savings and on the rewards of successful enterprise. It hits the small businessman who reaches retirement without the cushion of a company pension scheme,and impedes the creation of farm tenancies. In the vast majority of cases it is a tax on savings made in the first place out of hard-earned and fully-taxed income. More than half of those who pay the investment income surcharge are over 65, and of these more than half would otherwise be liable to tax at only the basic rate.

73. I have therefore decided that the investment income surcharge should be abolished. The cost in 1984-85 will be some £25 million, and in a full year around £350 million.

74. Finally, I propose to draw more closely together the tax treatment of depositors in banks and building societies.

These institutions compete in the same market for personal deposits. I believe that they should be able to do so on more equal terms as far as tax is concerned.

75. One inequality has already been removed, with the recent change made on legal advice in the tax treatment of building societies' profits from gilt-edged securities. They are now treated in the same way as those of the banks have always been. Other inequalities will be removed by measures to which I shall come later in the speech

(leasing)

76. But the major inequality of treatment, against which the banks in particular have frequently complained, lies with the special arrangement for interest paid by building societies, under which the societies pay tax at a special rate - the "composite rate" - on the interest paid to the depositor who receives credit for income tax at the full basic rate.

77. This system, which has worked well for the past 90 years, has both an advantage and a disadvantage. The disadvantage is that a minority of depositors, who are below the income tax threshold, still suffer the deduction of tax at the composite rate. However, it is always open to such depositors to put their savings elsewhere, such as National Savings. The advantage of the scheme is its extreme simplicity, particularly for the taxpayer; most taxpayers are spared the bother of paying tax on interest through PAYE or individual assessment, while the Revenue are spared the need to recruit an additional 2000 staff to collect the tax due on interest paid without deduction.

78. In common with my predecessors of all Parties over the past 90 years, I am satisfied that the advantage of the composite rate arrangement outweighs the disadvantage. It follows that equal treatment of building societies and banks should be achieved, not by removing the composite rate from the societies, but by extending it to the banks and other licensed deposit takers.

79. Non-taxpayers would ~~of course~~ continue to be able to receive interest gross, should they wish to do so, by putting their money into appropriate National Savings facilities. But the purpose of the move is not, of course, to attract savings into Government hands: as I have already announced, next year's target for National Savings will be the same as this year's and last year's, and the total Government appetite for savings, which is measured by the size of the Public Sector Borrowing Requirement, is being significantly reduced. Moreover I have decided to reduce substantially the permitted maximum size of future holdings in the National Savings Investment Account and in Income Bonds.

Where they can obtain a much better pre tax interest rate £.

This does not sound right. Cannot be left for the PN. It looks as if the non taxpayers opportunities are being squeezed rather than maintained as they are

80. The true purpose of the move is simple: simplicity itself. Unless they are higher rate taxpayers, individual bank customers will, when it comes to tax, be able to forget about bank interest altogether, for all the tax due on it will be deducted at source. The Inland Revenue will be able to make staff savings of up to an extra 1000 civil servants. Moreover, this figure takes no account of the extra numbers that would have

been required to operate the present system as the trend towards the payment of interest on current accounts develops.

- or of the numbers required if I had taken the other course and removed the composite rate for building societies.

81. Accordingly, I propose to extend the composite rate arrangements to interest received by UK resident individuals from banks and other licensed deposit takers with effect from 1985-86. The composite rate will not apply either to non-residents or to the corporate sector. Arrangements will also be made to exclude from the scheme Certificates of Deposit and Time Deposits of £50,000 or more.

82. Taken together, the major proposals I have just announced on stamp duty, life assurance relief, the investment income surcharge and the composite rate, coupled with other minor proposals, will provide a simpler and more straightforward tax system for savings and investment. They will remove biases which have discouraged the individual saver from investing directly in industry. And they will reinforce the Government's policy of encouraging competition in the financial sector, as in the economy as a whole.

BUSINESS TAXATION

83. I now turn to company taxation.

84. In this area, Government has two responsibilities towards British business and industry. The first is to ensure that they do not have to bear an excessive burden of taxation. The second is to ensure that, given a particular burden, it is structured in the way that does least damage to the nation's economic performance.

85. The measures I am announcing today will, taking the next two years together, result in a ~~very~~ substantial reduction in ?
the burden of taxation on British industry. And ~~in addition~~ I shall be proposing a far-reaching reform of the structure of company taxation.

86. The current rates of Corporation Tax are far too high, penalising profit and success, and blunting the cutting edge of enterprise. They are the product of too many special reliefs, indiscriminately applied and of diminishing relevance to the conditions of today. Some of these reliefs reflect economic priorities or circumstances which have long vanished, and now serve only to distort investment decisions and choices about finance. Others were introduced to meet short-term pressures, notably the upward surge of inflation. With

I don't think the numbers help here

inflation down to 5 per cent and clearly set to go lower, this is ~~clearly~~ the time to take a fresh look. And with unemployment as high as it is today, it is particularly difficult to justify

a tax system which encourages low-yielding or even unprofitable investment at the expense of jobs.

87. My purpose therefore is to phase out some unnecessary reliefs, in order to bring about, over time, a markedly lower rate of tax on company profits.

88. First, capital allowances. Over virtually the whole of the post-war period there have been incentives for investment in both plant and machinery and industrial (though not commercial) buildings. But there is little evidence that these incentives have strengthened the economy or improved the quality of investment. Quite the contrary: the evidence suggests that businesses have invested substantially in assets yielding a lower rate of return than the investments made by our principal competitors. Too much of British investment has been made because the tax allowances make it look profitable, rather than because it would be truly productive.

high quality investment ~~high capability~~ T

89. The nation needs more investment, ~~and~~ the 6 per cent increase forecast for this year takes account of the measures I have announced ~~is encouraging. But the~~ ~~takes acco~~ ~~greatest benefits flow from investment decisions~~ based on ~~analysis of future market~~ assessments, not future tax assess~~ments~~. This is a most encouraging prospect.

Should this not come at the end of the section? Investment will be ~~[illegible]~~ a 6% year forecast taking account of the measures).

90. I propose to restructure the capital allowances in three annual stages. In the case of plant and machinery, and assets whose allowances are linked with them, the first

after 95 and 102

year allowance will be reduced from 100 per cent to 75 per cent for all such expenditure incurred after today, and to 50 per cent for expenditure incurred after 31 March next year. After 31 March 1986 there will be no first year allowances, and all expenditure on plant and machinery will qualify for annual allowances on a 25 per cent reducing balance basis.

91. In addition, from next year annual allowances will be given as soon as the expenditure is incurred, and not, as they are today, when the asset comes into use. This will bring forward the entitlement to annual allowances for those assets, such as ships and oil rigs, for which some payment is normally made well in advance of their being brought into use.

92. For industrial buildings, I propose that the initial allowance should fall from 75 per cent to 50 per cent from tonight, and be further reduced to 25 per cent from 31 March next year. After 31 March 1986 the initial allowance will be abolished, and expenditure will be written off on an annual 4 per cent straight line basis. I should add that, when these changes have all taken place, in respect of both plant and machinery and industrial buildings, tax allowances will still on average be rather more generous than would be provided by a strict system of economic depreciation.

93. The changes in the rates of allowances will not apply to payments under binding contracts entered into on or before today, provided that the expenditure is incurred within the

next three years.

94. After consulting my Rt Hon Friend the Secretary of State for Trade and Industry, I have decided to make transitional tax arrangements for certain investment projects in the regions. Existing capital allowances will continue to apply to expenditure on projects in Development Areas and special Development Areas for which regional development grants are available and offers of selective assistance have already been made between 1 April 1980 and today. Similar arrangements were announced for regional development grants in my Rt Hon Friend's White Paper on Regional Industrial Development last December.

95. Over the same period to 31 March 1986 most other capital allowances will be brought into line with the main changes I have announced. The Inland Revenue will be issuing a press notice tonight giving full details of these proposals.

Take in 89

96. Next, stock relief. As the House will recall, this was introduced by the last Labour Government as a rough and ready form of emergency help to businesses facing the ravages of high inflation. These days are past; and relief is no longer necessary; for company liquidity has improved and, above all, inflation has fallen sharply. ~~and will be falling further during this Parliament.~~ Accordingly, I propose to abolish stock relief from this month.

97. The changes I have just announced, in capital allowances and stock relief, enable me to embark on a major programme of progressive reductions in the main rate of Corporation Tax. For profits earned in the year just ending, on which tax is generally payable in 1984-85, the rate will be cut from 52 per cent to 50 per cent. For profits earned in 1984-85 the rate will be further cut to 45 per cent. Looking further ahead, to profits earned in 1985-86, the rate will go down to 40 per cent; and for profits earned in 1986-87 the main rate of Corporation Tax will be 35 per cent.

98. All these rates for the years ahead will be included in this year's Finance Bill.

99. And they will bring a further benefit. Responses to the Corporation Tax Green Paper published in 1982 revealed a strong and general desire to retain our imputation system of Corporation Tax. This allows a company to offset in full all interest paid. But only a partial deduction for dividends is allowed. Companies thus have an unhealthy incentive to finance themselves through borrowing, in particular bank borrowing, rather than by raising equity capital. The closer the Corporation Tax rate comes to the basic rate of income tax, the smaller this undesirable distortion becomes.

100. Of course, the majority of companies are not liable to pay the main rate of Corporation Tax at all. For them it is the small companies' rate, at present 38 per cent, which applies.

I propose to reduce this rate forthwith to 30 per cent, for profits earned in 1983-84 and thereafter.

101. The Corporation Tax measures I have just announced will cost £280 million in 1984-85. In 1985-86 the cost will be £600 million - made up of £1,150 million by way of reductions in the rates, only partially offset by a £550 million reduction in the value of the reliefs. The estimated costs for later years, which have been provided for in the MTFS figures contained in the Budget Red Book, have been drawn up on a cautious basis. Thus business and industry can go ahead confidently on the basis of the Corporation Tax rates I have announced today, and which set the framework of company taxation for the rest of this Parliament.

102. I expect these changes to have both a somewhat different impact in the short and long term. In the short term, some investment should be brought forward over the next two years, to take advantage of high first year capital allowances while they last - a prospect made all the more alluring for business by virtue of the fact that profits earned will be taxed at the new lower, rates. But the more important and durable effect will be to encourage the search for investment projects with a genuinely worthwhile return, and to discourage uneconomic investment.

89 here?

103. It is doubtful if it was ever really sensible to subsidise capital irrespective of the true rate of return. Certainly,

with over three million unemployed it cannot make sense to do so.

104. These changes hold out an exciting opportunity for British industry as a whole: an opportunity further to improve its profitability, and to expand, building on the recovery that is already well under way. Higher net profits should encourage and reward enterprise and stimulate ~~higher current expenditure~~ and innovation in all its forms - research and development and work on new products, processes and markets. They are the centre-piece, for business, of this Budget and the tax strategy for this Parliament.

105. But I have further measures to announce that are relevant to business.

106. First, the Business Expansion Scheme, introduced last year as a successor to the Business Start Up Scheme, has been widely welcomed as a highly imaginative scheme for encouraging individuals to invest in small companies. It is already proving a considerable success. It now needs time to settle down, and I have only one change to propose this year.

107. The scheme was designed to offer generous incentives for investment in high risk areas by new or expanding companies. Farming is clearly not an area which falls within this category, and I therefore propose that from today farming should cease to be treated as a qualifying trade under the scheme. I am

also ready to consider tightening the scheme further, if it becomes clear at any time in the future that it is being used for purposes for which it was clearly not designed.

108. Secondly, as a measure of help to small firms, I propose to raise the VAT registration threshold with effect from midnight tonight from £18,000 to £18,700.

109. Thirdly, in keeping with what I have said about removing distortions, I propose to abolish two reliefs in the personal tax field which were introduced at a time when this country suffered from excessively high rates of income tax. As we have reduced those rates, the reliefs are no longer justified.

110. The first distortion is the 50 per cent tax deduction (falling after 9 years to 25 per cent) applied to ~~given from~~ the emoluments of foreign employees working here for foreign employers. Foreign employees are often paying much less tax here than they would either at home or in most other European countries. At present income tax rates, the need for the relief has clearly disappeared. Moreover it is open to widespread abuse. It is, for example, possible for the son of an immigrant, working here for a foreign company, to pay tax on only 75 per cent of his salary, even if he himself has lived in this country all his life. I therefore propose to withdraw the relief entirely for all new cases from today, and to withdraw the 25 per cent deduction from existing beneficiaries from 6 April next. The 50 per cent deduction will be phased out over the

5 years to 5 April 1989.

111. I also propose to withdraw the so-called foreign earnings relief for United Kingdom residents who perform their duties both here and overseas and who spend at least 30 days abroad in a tax year. This relief too has lost its rationale, which harks back to the days of penalty high income tax rates. It too has been exploited, in particular by those who prolong their overseas visits purely in order to gain a tax advantage. For the same reason, I propose to withdraw the matching relief for the self-employed who spend 30 days abroad, and for resident employees and self-employed who have separate employments or separate trades carried on wholly abroad. The relief will be halved to 12½ per cent in 1984-85 and removed entirely from 6 April 1985. However, I have also authorised the Inland Revenue to consult interested parties about a possible relaxation in the rules governing the taxation of expenses reimbursed to employees for travel overseas. I am not making any change to the 100 per cent deduction given for absences abroad of 365 days or more.

112. The abolition of these reliefs will eventually yield revenue savings of over £150 million; and represents another useful step in the removal of complexity and distortions.

113. I need to set the car benefit scales for 1985-86 for those provided with the use of a car by their employer.

Despite the increases over recent years, the levels still fall short of any realistic measure of the true benefit. I am accordingly proposing an increase of 10 per cent in both the car and car fuel scales with effect from April 1985.

114. Unnecessarily high rates of tax discourage enterprise and risk taking. This is true of the capital taxes, just as it is of the corporation and income taxes. It is a matter of particular concern to those involved in running unquoted family businesses. The highest rates of capital transfer tax are way out of line with comparable rates abroad, and with the top rates of other taxes in this country. I propose therefore to reduce the highest rate of capital transfer tax from 75 per cent to 60 per cent and to raise the threshold to £64,000 in line with indexation. [For lifetime gifts I further propose to make the rate one-half of that on death over the whole scale.]

misleading

incomprehensible.

115. For capital gains tax I will, as promised, bring forward in the Finance Bill proposals to double the limit for retirement relief to a figure of £100,000, backdated to April 1983. A consultative document on other possible changes in this relief is being issued next week. I am proposing no other changes this year in capital gains tax beyond the statutory indexation of the exempt amount from £5,300 to £5,600. However, the tax continues to attract criticism - not least for its complexity - and that is a matter to which I hope to return in a later year.

116. We have done much to improve the Development Land Tax. Early in the last Parliament, my predecessor increased the threshold from £10,000 to £50,000. I now propose a further increase to £75,000, which will reduce the numbers affected by the tax by more than one-third.

117. Next share options. The measures introduced in the last Parliament to improve employee involvement through profit sharing and savings related share option schemes have been a notable success. The numbers of all these employee schemes have increased from about 30 in 1979 to over 670 now, benefiting some half a million employees. To maintain and build on this progress I propose to increase the monthly limit on contributions to savings related share option schemes from £50 to £100. I have also authorised the Inland Revenue to double the tax-free limits under the concession on long service awards and to include the gift of shares in the employee's company.

118. But beyond this, I am convinced that we need to do more to attract top calibre company management and to increase the incentives and motivation of existing executives and key personnel by linking their rewards to performance. I propose therefore that, subject to certain necessary limits and conditions, share options generally will be taken out of income tax, leaving any gain to be charged to capital gains tax on ultimate disposal of the shares. The new rules will

apply to options meeting the conditions which are granted from 6 April.

119. I am sure that all these changes will be welcomed as measures to encourage the commitment of employees to the success of their companies and to improve the performance, competitiveness and profitability of British industry.

120. Before turning to North Sea taxation, I should like to remind the House of the Government's concern at the threat which the spread of unitary taxation in certain US states has posed to the US subsidiaries of British firms. With our European partners we are monitoring the situation closely, and await with keen interest the imminent report of a Working Group under my US counterpart. It is very important that a satisfactory solution be speedily implemented.

121. This issue isnot wholly irrelevant to the North Sea, for US firms operating there, or elsewhere in this country, are not of course taxed on a unitary basis, taking account of world-wide profits.

122. Last year's North Sea tax changes were well received, and there has been encouraging progress in the number of development projects coming forward, as well as in exploration and appraisal. The Government is already committed to a study of the economics of investment in incremental development in existing fields. This is of increasing importance and in consultation with my rt hon friend the Secretary of State for Energy I

therefore propose to review this area with the industry, and to legislate as appropriate next year to improve the position. To prevent projects being deferred pending this review, any changes will apply to all projects which receive development consent after today.

The measures I have just announced will have considerable benefits for North Sea companies. So

123. Meanwhile, I am taking two measures to prevent an unjustified loss of tax in the North Sea. First, in addition to the PRT measures on farmouts which I announced last September, I am limiting the potential Corporation Tax cost of such deals. Second, I propose to repeal the provision which allows Advance Corporation Tax to be repaid where Corporation Tax is reduced by PRT. I have concluded that this can no longer be justified. I have also reviewed the case for extending last year's future field concessions to the Southern Basin, but have concluded that additional incentives here are not needed.

124. I have just two further changes affecting business to propose, both of which will come into force on 1 October.

125. Ever since VAT was introduced in this country, we have treated imports differently from the way in which they are treated by our main European Community competitors. In a nutshell, they require VAT on imported goods to be paid in the same way as customs duties. We do not. Under our system an importer does not have to account for VAT on his

imports until he makes his normal VAT return, on average some 11 weeks later. During this time the importer enjoys free credit at the taxpayer's expense. This is an advantage not enjoyed by the home-produced equivalent of the import, since businesses buying from UK suppliers have to pay VAT when they pay their suppliers.

126. The UK system does indeed have many advantages, which is why the European Commission has for some years now been seeking to get it adopted throughout the Community, with the full support of both my predecessor and myself. But the plain fact is that in all that time the Commission has made no progress whatever.

127. I must tell the House that I am not prepared to put British industry at a competitive disadvantage in the home market any longer. Should our European partners at any time undergo a Damascene conversion, and [redacted] agree that the Commission's proposal should be accepted after all, then of course we would gladly revert to the present system. But in the meantime I propose to move to the system used by our major competitors and charge VAT straight away on imports, providing the same facilities for deferring payment as apply to customs duties. That means that most importers will be able to defer payment of VAT by on average one month from the date of importation. But that is all.

Do we want to say why we have not made special arrangements for raw materials/exporters

128. As I have said, this change will apply from 1 October. By bringing forward VAT receipts, it will bring in an extra £1.2 billion in 1984-85, some of which will of course be borne ~~carried~~ by foreign producers and manufacturers. There will naturally be no increased revenue in subsequent years.

129. The second change I propose to make on 1 October concerns the National Insurance Surcharge. This, once again, was a brainchild of the Rt Hon member for Leeds East. Having introduced it in 1977 at the rate of 2 per cent, he then raised it in 1978 to 3½ per cent. During the last Parliament, my predecessor succeeded in reducing it to 1 per cent, and we are pledged to abolish it during the lifetime of this Parliament.

130. Given the impact that this tax has, not only on industrial costs but also - at a time of high unemployment - on jobs, I have decided to take the opportunity of this my first Budget to fulfil that pledge. Abolition of the National Insurance Surcharge from October will reduce private sector employers' costs by almost £350 million in 1984-85, and over £850 million in a full year. Its abolition is thus of continuing help to British industry.

131. Thus my proposals offer British business the abolition of the tax on jobs and the reduction of the rate of taxation on profits. They also sweep away a number of out-dated reliefs, reduce distortions, and assist enterprise.

INDIRECT TAXES

131. Having announced major reforms of both the taxation of savings and investment and the taxation of business, I turn now to the third and final area in which I propose to make progress on tax reform. This is the taxation of personal income and spending.

132. The broad principle was clearly set out in the Manifesto on which we were first elected in 1979 and which emphasised the need for a switch from taxes on earnings to taxes on spending. My predecessor made an important move in this direction in <u>his</u> first budget, and the time has come to make a further move today. To reduce direct taxation by this means is important in two ways. It improves incentives and makes it more worthwhile to work, and it increases the freedom of choice of the individual.

check quotation

133. I do not however see the excise duties - with certain exceptions - as an area for major change. I shall of course need to raise most of the duties broadly in line with inflation, so as to maintain their real value: not to do so would run counter to the philosophy I outlined a moment ago. But with inflation now as low as it is, the necessary increases are on the whole mercifully modest. Only for a few particular duties do I envisage steeper rises.

134. One significant exception is tobacco, where I ~~am convinced of the need~~ believe it is right to raise the duty in real terms, ~~to help cut smoking and thus reduce~~ given the potential danger to health. I therefore propose an increase in the tobacco duty which, including VAT, will put 10p on the price of a packet of cigarettes, with corresponding increases for hand-rolling tobacco and cigars. This will do no more than restore the tax on tobacco to its 1965 level. I do not propose to increase the duty in pipe tobacco, which is important for a great many pensioners. These changes will take effect from midnight on Thursday.

135. For the duties on petrol and derv I propose simply broad revalorisation, which means increases which, again including VAT, will ~~increase~~ raise the price at the pumps by 4½p and 3½p a gallon respectively. I do not propose to increase the duty on heavy fuel oil, which is of particular importance to industrial costs. These changes will take effect for oil delivered from refineries and warehouses from six o'clock this evening.

136. There is one excise duty which I propose to do away with altogether. Many of those who find it hardest to make ends meet, including in particular many pensioners, use paraffin stoves to heat their homes, and it is with them in mind that I propose to abolish the duty on kerosene from six o'clock tonight. I am sure that this will be welcomed on all sides of the House.

137. The various rates of Vehicle Excise Duty will, once again, go up roughly in line with prices. Thus the duty for cars and light vans will be increased by £5, from £85 to £90 a year. However, given the further evidence my Rt Hon Friend the Secretary of State has now received on the wear and tear that various types of vehicle cause to the roads, there will be reductions in duty for the lightest lorries, offset by higher increases for some heavier lorries. All these changes in Vehicle Excise Duty will take effect from tomorrow.

138. However, I propose to exempt from Vehicle Excise Duty all recipients of the War Pensioners' Mobility Supplement.

139. And I have decided to widen the specific VAT reliefs for the disabled in the important area of transport. The existing VAT relief for motor vehicles designed or adapted for use by the handicapped will be extended, and matched by a new Car Tax relief. The effect will be that neither VAT nor car tax will apply to family cars designed for disabled people or substantially adapted for their use.

140. I now come to the most difficult decision I have to take in the excise duty field. As the House will be aware, the rules of the European Community, so far as alcoholic drinks are concerned, are designed to prevent a Member state from protecting its own domestic product by imposing a significantly higher duty on competing imports. In pursuit of this, the Commission has taken a number of countries to the European Court of Justice.

141. In our case, the Commission contended that we were protecting beer by under-taxing it in relation to wine. We fought the case, but lost; and I am now implementing the judgement handed down by the Court last year. Accordingly, I propose to increase the duty on beer, not by the 7p a pint which has been widely rumoured in the press, but by the minimum amount needed to comply with the judgement and maintain revenue: 2p on a typical pint of beer, including VAT. At the same time, the duty on table wine will be reduced by the equivalent of about 18p a bottle, again including VAT.

142. I cannot, however, ignore the fact that while we comply with the judgement of the European Court, one of our partners appears determined not to do so. I refer to Italy, which has been ordered by the Court to remove forthwith its discrimination against Scotch whisky, but as yet shows no sign whatever of complying. I have therefore decided to introduce a temporary duty surcharge on vermouth of some 20p a bottle on top of the basic increase, to which I shall come in a moment. This surcharge will come into operation on 1 September unless the Italian Government has - as I very much hope it will - implemented the Court's judgement by that date, and it will lapse as soon as I am satisfied that it has complied.

143. As for the rest of the alcoholic drinks, cider, which increasingly competes with beer but attracts a lower duty, will go up by 3p a pint. The duties on made-wine will be aligned with those on other wine. And I propose to increase the duty on sparkling wine, fortified wine and spirits by about 10p a

bottle, including VAT. All these changes, except the vermouth surcharge, will take effect from midnight tonight.

144. These changes in excise duties will, all told, bring in some £840 million in 1984-85, some £200m more than is required to keep pace with inflation. The addition is of course ~~largely~~ due to the increase in tobacco duty.

145. But much of the extra revenue I need to make a substantial switch this year from taxes on earnings to taxes on spending will come from VAT. I propose no change in the rate of VAT. Instead, I intend to broaden the base of the tax by extending the 15 per cent rate to two areas of expenditure that have hitherto been zero-rated.

146. First, alterations to buildings. At present repairs and maintenance are taxed, but alterations are not. The borderline between these two categories is the most confused in the whole field of VAT. I propose to end this confusion and illogicality by bringing all alterations into tax. However, to allow a reasonable time for existing commitments to be completed or adjusted, the change will be deferred until 1 June.

147. Secondly, food. Most food is zero-rated. But food served in restaurants is taxed, together with a miscellaneous range of items including ice-cream, confectionery, soft drinks and crisps, which were brought into tax by the Rt Hon Member for Leeds East. Take-away food clearly competes with other

forms of catering, and I therefore intend to bring into tax hot take-away food and drinks, with effect from 1 May.

148. The total effect of the extensions of the VAT coverage which I have proposed will be to increase the yield of the tax by £375 million in 1984-85 and by almost £650 million in 1985-86.

149. The total impact effect on the Retail Price Index of the VAT changes and excise duty changes taken together will be less than three-quarters of one per cent. This has already been taken into account in the forecast which I have given to the House of a decline in inflation to 4½ per cent by the end of the year.

150. The extra revenue raised in this way will enable me within the overall framework of a neutral Budget to lighten the burden of income tax.

PERSONAL TAXATION

151. Since we took office in 1979, we have cut the basic rate of income tax from 33 per cent to 30 per cent and sharply reduced the confiscatory higher rates inherited from the last Labour Government. We have increased the main tax allowances not simply in line with prices but by around 8 per cent in real terms. It is a good record. But it is not enough. The burden of income tax is still too heavy.

152. During the lifetime of this Parliament, I intend to carry much further the progress we have already made. For the most part, this will have to wait for future Budgets, particularly since I have thought it right this year to concentrate on setting a new regime of business taxation for the lifetime of a Parliament - and beyond. But as a result of the changes to taxes on spending which I have just announced, I can make a start now.

153. I propose to make no change this year in the rates of income tax. So far as the allowances and thresholds are concerned, I must clearly increase these by the amounts set out in the statutory indexation formula, based on the 5.3 per cent increase in the Retail Price Index to December. The question is how much more I can do, and how to direct it.

154. I have decided that, this year, the right course is to use every penny I have in hand, within the framework of a revenue neutral Budget, to lift the level of the basic tax thresholds, for the married and single alike. It is fundamentally wrong that we collect income tax from people whose incomes are so low that they are entitled to social security benefits on grounds of need. Moreover low tax thresholds make the poverty and unemployment traps much worse, so that the financial incentive to find a better job or even any job may decline almost to zero. There is, alas, no quick or cheap solution to these problems. But that is all the more reason to make a start on solving them now.

155. I propose to increase most thresholds in line with the statutory requirement, and by no more. The first higher rate of 40 per cent will apply when taxable income reaches £15,400 a year and the top rate of 60 per cent to taxable income of £38,100 or more. The single age allowance will rise from £2,360 to £2,490 and the married age allowance from £3,755 to £3,955.

156. For the basic thresholds, statutory indexation would mean putting the single and married allowances up by £100 and £150 respectively. I am glad to say that I can do considerably better than that. I propose to increase the basic thresholds by well over double what is required by indexation. The single person's threshold will be increased by £220, from £1,785 to £2,005; and the married threshold by £360, from £2,795 to £3,155. ~~The special allowances for widows, and for single parents, will as a consequence go up by some 14 per cent.~~

157. This is an increase of around 12½ per cent, or some 7 per cent in real terms. It brings the married man's tax threshold for 1984-85 to its highest level in real terms since the war. It means that every tax-paying married couple in the land will enjoy an income tax cut of at least £2 a week. And it means that a large number of people, those with the smallest incomes of all, are taken out of income tax altogether. ~~And~~ Some 850,000 people - over 100,000 of them widows - will not pay tax in 1984-85 who would have paid if thresholds had not been increased. And 400,000 fewer than if the allowances had merely been indexed.

158. All these changes will take effect under PAYE on the first pay day after 10 May. Their cost is considerable: some £1.8 billion in 1984-85, of which roughly half represents the cost of indexation.

159. This is as far as I can go on income tax this year, within a broadly revenue-neutral Budget for 1984-85. But as I have already said, so long as we hold to our published planned levels of public spending, there is an excellent prospect consistent with the necessary downward path of public borrowing of further tax cuts in next year's Budget. These would be on top of the measures I have announced in this Budget which, as I have already told the House, will reduce taxation in 1985-86 by some £1¾ billion, with business taking the lion's share. So for next year I would hope to be concentrating on further help to individuals, and principally on income tax.

CONCLUSION

160. I have, Mr Deputy Speaker, completed the course I charted at the outset this afternoon. I have described the recovery, and how the Government plans to sustain it, by working for further reductions in inflation, by maintaining sound money and by curbing borrowing. I have described a three part reform strategy for a fairer, simpler tax system. And I have been able to propose substantial tax reductions over two years in a Budget that is revenue-neutral for 1984-85. It is a Budget for responsibility and reform; and I commend it to the House.

NM

BUSINESS TAXATION

[Section goes wider than Companies]

83. I now turn to ~~company~~ business taxation.

84. In this area, Government has two responsibilities towards British business and industry. The first is to ensure that they do not have to bear an excessive burden of taxation. The second is to ensure that, given a particular burden, it is structured in the way that does least damage to the nation's economic performance.

[There is a reduction for business as a whole, but little or none for manufacturing industry]

85. The measures I am announcing today will, taking the next two years together, result in a [redacted] substantial reduction in the burden of taxation on British ~~industry~~ business. And in addition I shall be proposing a far-reaching reform ~~of the structure~~ of company taxation.

[John O-S for accuracy. No need in my view NM.]

86. The current rates of Corporation Tax are far too high, penalising profit and success, and blunting the cutting edge of enterprise. They are ~~the product of~~ associated with too many special reliefs, indiscriminately applied and of diminishing relevance to the conditions of today. Some of these reliefs reflect economic priorities or circumstances which have long vanished, and now serve only to distort investment decisions and choices about finance. Others were introduced to meet short-term pressures, notably the upward surge of inflation. With inflation down to 5 per cent and set to go lower, this is clearly the time to take a fresh look. And with unemployment as high as it is today, it is particularly difficult to justify

loss-making

a tax system which encourages low-yielding or even ~~unprofitable~~ investment at the expense of jobs.

87. My purpose therefore is to phase out some unnecessary reliefs, in order to bring about, over time, a markedly lower rate of tax on company profits.

88. First, capital allowances. Over virtually the whole of the post-war period there have been incentives for investment in both plant and machinery and industrial (though not commercial) buildings. But there is little evidence that these incentives have strengthened the economy or improved the quality of investment. Quite the contrary: the evidence suggests that businesses have invested substantially in assets yielding a lower rate of return than the investments made by our principal competitors. Too much ~~of~~ British investment has been made because the tax allowances make it look profitable, rather than because it would be truly productive.

89. The nation needs more investment, and the 6 per cent increase forecast for this year is encouraging. But ~~the~~ higher investment will only bring proper returns to the nation when business ~~greatest benefits flow from investment~~ decisions are based on analysis of future market assessments, not future tax assessments.

A Ridley

90. I propose to restructure the capital allowances in three annual stages. In the case of plant and machinery, and assets whose allowances are linked with them, the first

year allowance will be reduced from 100 per cent to 75 per cent for all such expenditure incurred after today, and to 50 per cent for expenditure incurred after 31 March next year. After 31 March 1986 there will be no first year allowances, and all expenditure on plant and machinery will qualify for annual allowances on a 25 per cent reducing balance basis.

91. In addition, from next year annual allowances will be given as soon as the expenditure is incurred, and not, as they are today, when the asset comes into use. This will bring forward the entitlement to annual allowances for those assets, such as ships and oil rigs, for which some payment is normally made well in advance of their being brought into use.

92. For industrial buildings, I propose that the initial allowance should fall from 75 per cent to 50 per cent from tonight, and be further reduced to 25 per cent from 31 March next year. After 31 March 1986 the initial allowance will be abolished, and expenditure will be written off on an annual 4 per cent straight line basis. I should add that, when these changes have all taken place, in respect of both plant and machinery and industrial buildings, tax allowances will still on average be rather more generous than would be provided by a strict system of ~~economic~~ commercial depreciation.

["economic" suggests replacement cost]

93. The changes in the rates of allowances will not apply to payments under binding contracts entered into on or before today, provided that the expenditure is incurred within the

next three years.

94. After consulting my Rt Hon Friend the Secretary of State for Trade and Industry, I have decided to make transitional tax arrangements for certain investment projects in

95. Over the same period to 31 March 1986 most other capital allowances will be brought into line with the main changes I have announced. The Inland Revenue will be issuing a press notice tonight giving full details of these proposals.

96. Next, stock relief. As the House will recall, this was introduced by the last Labour Government as a rough and ready form of emergency help to businesses facing the ravages of high inflation. These days are past; and relief is no longer necessary; for ~~company~~ liquidity has improved and, above all, inflation has fallen sharply, ~~and will be falling further during this Parliament.~~ Accordingly, I propose to abolish stock relief from this month.

[applies to unincorporated too]

97. The changes I have just announced, in capital allowances and stock relief, enable me to embark on a major programme of progressive reductions in the main rate of Corporation Tax. For profits earned in the year just ending, on which tax is generally payable in 1984-85, the rate will be cut from 52 per cent to 50 per cent. For profits earned in 1984-85 the rate will be further cut to 45 per cent. Looking further ahead, to profits earned in 1985-86, the rate will go down to 40 per cent; and for profits earned in 1986-87 the main rate of Corporation Tax will be 35 per cent. That will mean a cut of no less than 17 percentage points over 3 years

98. All these rates for the years ahead will be included in this year's Finance Bill.

99. And they will bring a further benefit. Responses to the Corporation Tax Green Paper published in 1982 revealed a strong and general desire to retain our imputation system of Corporation Tax which will continue. This allows a company to offset in full all interest paid. But only a partial ~~deduction~~ offset for dividends is allowed. Companies thus have an unhealthy incentive to finance themselves through borrowing, in particular bank borrowing, rather than by raising equity capital. The closer the Corporation Tax rate comes to the basic rate of income tax, the smaller this undesirable distortion becomes.

["deduction" technical term & wrong?]

100. Of course, the majority of companies are not liable to pay the main rate of Corporation Tax at all. For them it is the small companies' rate, at present 38 per cent, which applies.

I propose to reduce this rate forthwith to 30 per cent, for profits earned in 1983-84 and thereafter.

101. The Corporation Tax measures I have just announced will cost £280 million in 1984-85. In 1985-86 the cost will be £~~600~~ 450 million - made up of £1,1~~50~~00 million by way of reductions in the rates, only partially offset by a £~~550~~ 650 million reduction in the value of the reliefs. The estimated costs for later years, which have been provided for in the MTFS figures contained in the Budget Red Book, have been drawn up on a cautious basis. Thus business and industry can go ahead confidently on the basis of the Corporation Tax rates I have announced today, and which set the framework of company taxation for the rest of this Parliament.

102. I expect these changes to have ~~both~~ a somewhat different impact in the short and long term. In the short term, some investment should be brought forward over the next two years, to take advantage of high first year capital allowances while they last - a prospect made all the more alluring for business by virtue of the fact that profits earned will be taxed at the new lower, rates. But the more important and durable long term effect will be to encourage the search for investment projects with a genuinely worthwhile return, and to discourage uneconomic investment.

103. It is doubtful if it was ever really sensible to subsidise capital investment irrespective of the true rate of return. Certainly,

with over three million unemployed it cannot make sense to do so.

104. These changes hold out an exciting opportunity for British industry as a whole: an opportunity further to improve its profitability, and to expand, building on the recovery that is already well under way. Higher ~~net~~ profits after tax should encourage and reward enterprise and stimulate higher current expenditure ~~and~~ on innovation in all its forms - research and development and work on new products, processes and markets. They are the centre-piece, for business, of this Budget and the tax strategy for this Parliament.

105. ~~But~~ I have further measures to announce that are relevant to business.

106. First, the Business Expansion Scheme, introduced last year as a successor to the Business Start Up Scheme, has been widely welcomed as a highly imaginative scheme for encouraging individuals to invest in small companies. It is already proving a considerable success. It now needs time to settle down, and I have only one change to propose this year.

107. The scheme was designed to offer generous incentives for investment in high risk areas by new or expanding companies. Farming is clearly not an area which falls within this category, and I therefore propose that from today farming should cease to be treated as a qualifying trade under the scheme. I am

also ready to consider tightening the scheme further, if it becomes clear at any time in the future that it is being used for purposes for which it was clearly not designed.

108. Secondly, as a measure of help to small firms, I propose to raise the VAT registration threshold with effect from midnight tonight from £18,000 to £18,700.

109. Thirdly, in keeping with what I have said about removing distortions, I propose to abolish two reliefs in the personal tax field which were introduced at a time when this country suffered from excessively high rates of income tax. As we have reduced those rates, the reliefs are no longer justified.

110. The first distortion is the 50 per cent tax deduction (falling after 9 years to 25 per cent) applied to ~~given from~~ the emoluments of foreign domiciled employees working here for foreign employers. These ~~Foreign~~ employees are often paying much less tax here than they would either at home or in most other European countries. At present income tax rates, the need for the relief has clearly disappeared. Moreover it is open to widespread abuse. It is, for example, possible for the son of an immigrant, working here for a foreign company, to pay tax on only 75 per cent of his salary, even if he himself has lived in this country all his life. I therefore propose to withdraw the relief entirely for all new cases from today, and to withdraw the 25 per cent deduction from existing beneficiaries from 6 April next. For those already here the 50 per cent deduction will be phased out over the

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112. The abolition of these reliefs will eventually yield revenue savings of over £150 million; and represents another useful step in the removal of complexity and distortions.

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Despite the increases over recent years, the levels still fall short of any realistic measure of the true benefit. I am accordingly proposing an increase of 10 per cent in both the car and car fuel scales with effect from April 1985.

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misleading

115. For capital gains tax I will, as promised, bring forward in the Finance Bill proposals to double the limit for retirement relief to a figure of £100,000, backdated to April 1983. A consultative document on other possible changes in this relief is being issued next week. I am proposing no other changes this year in capital gains tax beyond the statutory indexation of the exempt amount from £5,300 to £5,600. However, the tax continues to attract criticism - not least for its complexity - and that is a matter to which I hope to return in a later year.

116. We have done much to improve the Development Land Tax. Early in the last Parliament, my predecessor increased the threshold from £10,000 to £50,000. I now propose a further increase to £75,000, which will reduce the ~~numbers~~ number of cases affected by the tax by more than one-third.

117. Next share options. The measures introduced in the last Parliament to improve employee involvement through profit sharing and savings related share option schemes have been a notable success. The numbers of ~~all these employee~~ schemes open to all employees have increased from about 30 in 1979 to over 670 now, benefiting some half a million employees. To maintain and build on this progress I propose to increase the monthly limit on contributions to savings related share option schemes from £50 to £100. I have also authorised the Inland Revenue to double the tax-free limits under the concession on long service awards and to include within those limits the gift of shares in the employee's company.

118. But beyond this, I am convinced that we need to do more to attract top calibre company management and to increase the incentives and motivation of existing executives and key personnel by linking their rewards to performance. I propose therefore that, subject to certain necessary limits and conditions, share options generally will be taken out of income tax, leaving any gain to be charged to capital gains tax on ultimate disposal of the shares. The new rules will

apply to options meeting the conditions which are granted from 6 April, [redacted].

119. I am sure that all these changes will be welcomed as measures to encourage the commitment of employees to the success of their companies and to improve the performance, competitiveness and profitability of British industry.

120. Before turning to North Sea taxation, I should like to remind the House of the Government's concern at the threat which the spread of unitary taxation in certain US states has posed to the US subsidiaries of British firms. With our European partners we are monitoring the situation closely, and await with keen interest the imminent report of a Working Group under my US counterpart. It is very important that a satisfactory solution be speedily implemented.

[May be a bridging passage but likely to be read as veiled threat. Only include as conscious choice. Official advice not timely or right to mix up with N. Sea]

[121. This issue isnot wholly irrelevant to the North Sea, for US firms operating there, or elsewhere in this country, are not of course taxed on a unitary basis, taking account of world-wide profits.]

122. Last year's North Sea tax changes were well received, and there has been encouraging progress in the number of development projects coming forward, as well as in exploration and appraisal. The Government is already committed to a study of the economics of investment in incremental development in existing fields. This is of increasing importance and in consultation with my rt hon friend the Secretary of State for Energy I

therefore propose to review this area with the industry, and to legislate as appropriate next year to improve the position. To prevent projects being deferred pending this review, any changes will apply to all projects which receive development consent after today.

123. Meanwhile, I am taking two measures to prevent an unjustified loss of tax in the North Sea. First, in addition to the PRT measures on farmouts which I announced last September, I am limiting the potential Corporation Tax cost of such deals. Second, I propose to repeal the provision which allows Advance Corporation Tax to be repaid where Corporation Tax is reduced by PRT. I have concluded that this can no longer be justified. I have also reviewed the case for extending last year's future field concessions to the Southern Basin, but have concluded that additional incentives here are not needed.

124. I have just two further changes affecting business to propose, both of which will come into force on 1 October.

125. Ever since VAT was introduced in this country, we have treated imports differently from the way in which they are treated by our main European Community competitors. In a nutshell, they require VAT on imported goods to be paid in the same way as customs duties. We do not. Under our system an importer does not have to account for VAT on his

imports until he makes his normal VAT return, on average some 11 weeks later. During this time the importer enjoys free credit at the taxpayer's expense. This is an advantage not enjoyed by the home-produced equivalent of the import, since businesses buying from UK suppliers have to pay VAT when they pay their suppliers.

126. The UK system does indeed have many advantages, which is why the European Commission has for some years now been seeking to get it adopted throughout the Community, with the full support of both my predecessor and myself. But the plain fact is that in all that time the Commission has made no progress whatever.

127. I must tell the House that I am not prepared to put British industry at a competitive disadvantage in the home market any longer. Should our European partners at any time undergo a Damascene conversion, and [redacted] agree that the Commission's proposal should be accepted after all, then of course we would gladly revert to the present system. But in the meantime I propose to move to the system used by our major competitors and charge VAT straight away on imports, providing the same facilities for deferring payment as apply to customs duties. That means that most importers will be able to defer payment of VAT by on average one month from the date of importation. But that is all.

[Surely a reference here is needed to tell people this will not create disruption at ports & frontiers]

A Ridley
– not yet checked with Customs

128. As I have said, this change will apply from 1 October. By bringing forward VAT receipts, it will bring in an extra £1.2 billion in 1984-85, some of which will of course be borne ~~carried~~ by foreign producers and manufacturers. There will naturally be no increased revenue in subsequent years.

129. The second change I propose to make on 1 October concerns the National Insurance Surcharge. This, once again, was a brainchild of the Rt Hon member for Leeds East. Having introduced it in 1977 at the rate of 2 per cent, he then raised it in 1978 to 3½ per cent. During the last Parliament, my predecessor succeeded in reducing it to 1 per cent, and we are pledged to abolish it during the lifetime of this Parliament.

130. Given the impact that this tax has, not only on industrial costs but also - at a time of high unemployment - on jobs, I have decided to take the opportunity of this my first Budget to fulfil that pledge. Abolition of the National Insurance Surcharge from October will reduce private sector employers' costs by almost £350 million in 1984-85, and over £~~850~~ 900 million in a full year.

131. Thus my proposals offer British business the abolition of the tax on jobs and the reduction of the rate of taxation on profits. They also sweep away a number of out-dated reliefs, reduce distortions, and assist enterprise.

Tax Reform

63A. The changes to the taxation of savings and investment have been designed to make the ~~tax~~ system more even-handed between institutional savings and individual savings; and between different kinds of financial institutions. The changes ~~I am proposing~~ to business taxation are designed to ~~make more even-handed the taxation of investment and employment; to reduce differences between the taxation of different types of investment and different ways of financing investment~~. And finally I ~~will~~ shall be seeking to improve the balance between the taxation of earnings and spending~~, and between different types of spending~~. ~~The emphasis is upon balance, fairness and even-handedness~~. By reducing the myriad ~~of~~ distortions ~~with~~in our tax system, ~~That is the way~~ we can help to improve efficiency and simplify life for the taxpayer.

Remove distortions which impair ~~effic~~ decision-making and

BUDGET SECRET

B(84)538

FROM : N C MUNRO

INLAND REVENUE
POLICY DIVISION
SOMERSET HOUSE

8 March 1984

(14)

ECONOMIC SECRETARY

FRIENDLY SOCIETIES : TAX EXEMPT BUSINESS

... In the light of Mr Ellis' minute of today, I attach a draft Budget Day press release for your consideration. If you are content, I should be grateful if your private secretary could let me know by telephone as soon as possible.

NCM.

N C MUNRO

cf The EST's decisions were £750 and £60,000.

B.

✓ N

cc Chancellor of the Exchequer
Chief Secretary
Financial Secretary
Minister of State
Sir Peter Middleton
Mr Cassell
Mr Battishill
Mr Monger
Mr Lankester
Mr Bridgeman) Registry of
Mr Wilson) Friendly Socs.

Mr Isaac
Mr O'Leary
Mr Newstead
Mr Williams T1/6
Mr J P O Lewis
PS/IR
Mr Munro

INLAND REVENUE
Press Release

INLAND REVENUE PRESS OFFICE, SOMERSET HOUSE, STRAND, LONDON WC2R 1LB
PHONE: 01-438 6692 OR 6706

[3x] 13 March 1984

REGISTERED FRIENDLY SOCIETIES

The Chancellor proposes in his Budget two changes to the tax treatment of registered friendly societies. First, he proposes to withdraw the special rules for 'tax exempt' friendly societies and bring them into line with 'mixed business' societies. Second, he proposes to increase the exempt limits previously applicable to the life or endowment business of friendly societies, to sums assured of £750 (previously £500) or annuities of £156 (previously £104). These new limits will apply to profits arising from all new friendly society business written after midnight tonight.

---

1. Under Section 332 of the 1970 Taxes Act, registered friendly societies are exempt from income and corporation tax subject to certain conditions. A society whose rules effectively limit it to life or endowment business with gross sums assured up to £2000 or annual annuities up to £416 is entirely exempt from tax on its profits. Such societies are known as 'tax exempt' friendly societies. Other - 'mixed business' - societies, whose rules contain no such restriction on their life or endowment business, enjoy exemption only in respect of profits arising from life or endowment business with gross sums assured up to £500 or annual annuities up to £104.

2. In recent years several new friendly societies have been established specifically in order to take advantage of the preferential tax treatment of 'tax exempt' societies. These societies were set up for purely commercial reasons, far removed from the traditional purpose of the Friendly Society movement.

3. The Chancellor therefore proposes to remove the distinction between 'tax exempt' and 'mixed business' friendly societies, so far as concerns new life or endowment business carried on after midnight tonight. Henceforth, all friendly societies profits arising from new life or endowment business will be exempt only if it is within the lower limits applicable to 'mixed business' societies. However, these limits are to be increased from £500 to £750 (capital sums assured) and from £104 to £156 (annuities).

Copy No. 2

R(84)529

BUDGET SECRET

FROM: A M ELLIS
DATE: 8 March 1984

MR BRIDGEMAN - RFS

cc PPS
PS/Chief Secretary
PS/Financial Secretary
PS/Minister of State
Sir P Middleton
Mr Cassell
Mr Battishill
Mr Monger
Mr Lankester
Mr O'Leary - IR
Mr Munro - IR
PS/IR

FRIENDLY SOCIETIES: TAX EXEMPT BUSINESS

The Economic Secretary has discussed with you the outstanding questions raised in your minutes of 6 and 7 February in the light of the Chancellor's comments (Miss Simpson's minute, forthcoming).

He has concluded that the two limits for taxable business, now brought together, should be £750 rather than £500 or £1,000. He was persuaded that this figure would not be unduly harsh on the material business of a material number of societies and that both presentationally and substantively there is a strong case for the figures.

Secondly, he has concluded that the limit on taxable business should br raised to £60,000 (and not £75,000) - the figure would be welcome to the Society without giving rise to concern from a prudential point of view.

AE

A M ELLIS

BUDGET SECRET

CH/EX REF. NO. B(84)520

FROM: MISS J C SIMPSON
DATE: 8 March 1984

cc PS/Chief Secretary
PS/Financial Secretary
PS/Minister of State
Sir P Middleton
Mr Cassell
Mr Battishill
Mr Monger
Mr Lankester
Mr O'Leary - IR
Mr Munroe - IR
PS/IR
Mr Bridgeman - RFS

PS/ECONOMIC SECRETARY

FRIENDLY SOCIETIES: TAX-EXEMPT BUSINESS

The Chancellor has seen Mr Bridgeman's minute of 7 March to the Economic Secretary.

2. He has commented that clearly, the government will want to harmonize the limits, and that the choice lies between £500 all round and £750 all round. He is inclined, on the balance of evidence presented in these papers (including the cost of a "co-op" funeral) to favour £750, but he is content that the final decision should be made by the Economic Secretary.

3. He has also commented that there is clearly much force in Mr Bridgeman's point in his earlier note that the choice must be considerably influenced by whether the change is to be seen as an interim holding operation or the only likely substantive change in the foreseeable future. If it is taken as the latter, which Mr Bridgeman favours, therefore pointing to a limit of £500, the question then to be considered is how much mayhem and aggravation it would cause, compared with £750. He has also suggested that it is worth considering, if the Government does go for £500 in particular, whether the taxable limit might not be raised to £75,000.

JS

MISS J C SIMPSON

B(84)541

FROM: A J G ISAAC

THE BOARD ROOM
INLAND REVENUE
SOMERSET HOUSE

8 March 1984

ECONOMIC SECRETARY

BUDGET SPEECH

I think that this morning's decision on Friendly Societies rates a mention in the Budget Speech. If you agree, I suggest the form of words below. This might come immediately after paragraph 9 in block I: Savings and Investment, in the edition of 6 March.

> 'I am also proposing to withdraw the special - and widely abused - privileges for certain so-called 'tax exempt' Friendly Societies and bring them into line with the normal rules for the Friendly Societies doing 'mixed' business; but at the same time to increase from £500 to £750 the limits within which in future all Friendly Societies will be able to write assurance on a tax exempt basis.'

A J G ISAAC

---

c	Chancellor of the Exchequer	Mr Isaac
	Chief Secretary	Mr O'Leary
	Financial Secretary	Mr Painter
	Minister of State	Mr Munro
	Mr Middleton	Mr Newstead
	Mr Cassell	PS/IR
	Mr Monger	
	Mr Lord	

B(84) 1029.

BUDGET SECRET

FROM: H M GRIFFITHS
8 March 1984

cc Mr Walton

MR MONGER

BUDGET SPEECH BLOCK K: PERSONAL TAXATION/INDIRECT TAXES

There is one point on the paragraph relating to VED (para 7) which I did not pick up yesterday but where I think some amendment is needed.

The third sentence refers to "the further evidence my rhf the Secretary of State has now received ..." This is not strictly correct. Mr Ridley issued a consultation document proposing changes in the allocation of road costs to various types of vehicles: but this reflected a reassessment of the methodology rather than new factual evidence.

I suggest amending the opening of the sentence to read:

> "However, in the light of the reassessment my Rt Hon Friend the Secretary of State has made of the contribution etc."

H M GRIFFITHS

Miss O'Mara,

PS/Chancellor

cc Mr Griffiths

Could you make this small change?

8/3

4.93

BUDGET SECRET

CH/EX REF. NO. [illegible]

FROM: MISS M O'MARA

DATE: 6 March 1984

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Littler
Mr Cassell
Mr Monck
Mr Battishill
Mr Odling-Smee
Mr Folger
Mr Norgrove
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
PS/C&E

cc Mr Griffiths

MR MONGER

BUDGET SPEECH BLOCK K: PERSONAL TAXATION/INDIRECT TAXES

I attach Block K of the Budget speech on which the Chancellor worked over the weekend. I should be grateful if comments could reach this office by mid-morning tomorrow.

Mom

MISS M O'MARA

644

785

BLOCK K: PERSONAL TAXATION/INDIRECT TAXES

I have announced major reforms of both the taxation of savings and investment and the taxation of businesses. The third and final area in which I propose to make progress on tax reform is the taxation of personal income and spending.

2. The broad principle was clearly set out in the Manifesto on which we were first elected in 1979. [Quote from 1979 Manifesto] My predecessor made an important move in this direction in <u>his</u> first budget, and the time has come to make a further move today. A change of this kind is important in two ways. It improves incentives and makes it more worthwhile to work, and it increases the freedom of choice of the individual.

3. I do not however see the excise duties as an area for major change this year. I shall of course need to raise the duties broadly in line with inflation, so as to maintain their real value: not to do so would run counter to the philosophy I outlined a moment ago. But broadly speaking I do not intend to do any more than revalorise the excise duties, and with inflation now as low as it is, the necessary increases are mercifully modest.

4. I propose an increase in the tobacco duty which, including VAT, will put 4p on the price of a packet of

cigarettes, with corresponding increases for hand-rolling tobacco and cigars. But I do not propose to increase the duty on pipe tobacco, which is important for a great many pensioners. These changes will take effect from midnight on Thursday.

5. I propose increases in the duties on petrol and derv which, again including VAT, will increase the price at the pumps by 4½p and 3½p a gallon respectively. I do not propose to increase the duty on heavy fuel oil, which is of particular importance to industrial costs. These changes will take effect for oil delivered from refineries and warehouses from six o'clock this evening.

6. There is one excise duty which I propose to do away with altogether. Many of those who find it hardest to make ends meet, including in particular many old age pensioners, use paraffin stoves to heat their homes. Accordingly, I propose to abolish the duty on kerosene from six o'clock this evening. I am sure that this will be welcomed on all sides of the House.

7. The various rates of Vehicle Excise Duty will, once again, go up roughly in line with prices. Thus the duty for cars and light vans will be increased by £5, from £85 to £90 a year. However, given the further evidence my Rt Hon Friend the Secretary of State has now received on the

contribution that various types of vehicle make to the wear and tear caused to the roads, there will be reductions in duty for the lightest lorries, offset by higher increases for some heavier lorries. All these changes in Vehicle Excise Duty will take effect from tomorrow.

Pre-1947 vehicles.

8. In addition, however, I propose to exempt from Vehicle Excise Duty all recipients of the War Pensioners' Mobility Supplement.

9. I now come to the most difficult decision I have to take in the excise duty field. As the House will be aware, the rules of the European Community, so far as alcoholic drink is concerned, are designed to prevent a Member state from protecting its own domestic product by imposing a significantly higher duty on imported competitors, the comparison being made broadly on the basis of relative alcoholic content. In pursuit of this, the Commission has taken a number of countries to the European Court of Justice.

10. In our case, the Commission contended that we were protecting beer by under-taxing it in relation to wine. We fought the case, but lost; and I am now obliged to implement the judgement handed down by the Court last year. Accordingly, I propose to increase the duty on beer, not by the 7p a pint which has been widely rumoured in the press, but by the minimum amount needed to comply with the judgement: 2p on

Car tax + VAT disabled.

a typical pint of beer, including VAT. At the same time, the duty on table wine will be reduced by the equivalent of about 18p a bottle, again including VAT.

11. I cannot, however, ignore the fact that while we comply with the judgement of the European Court, one of our partners appears determined not to do so. I refer to Italy, which has been clearly ordered by the Court to remove its discrimination against Scotch whisky forthwith, and shows no sign whatever of complying. I have therefore decided to introduce a temporary duty surcharge on vermouth of some 20p a bottle on top of the regular revalorisation increase. This surcharge will come into operation on 1 September unless the Italian Government has - as I very much hope - implemented the Court's judgement by that date, and it will lapse as soon as I am satisfied that it has complied.

12. As for the rest of the alcoholic drinks, cider, which increasingly competes with beer but attracts a lower duty, will go up by 3p a pint. The duties on made-wine will be aligned with those on other wine. And I propose to increase the duty on sparkling wine, fortified wine and spirits by about 10p a bottle, including VAT. /When to come into force?/

13. These changes in excise duties will, all told, bring

? full yr figure

in some £650 million in 1984-85. But that is of course ~~merely~~ broadly what is needed to keep pace with inflation.

14. The extra revenue I need to make the switch this year from taxes on earnings to taxes on spending must therefore come from VAT. I propose no change in the rate of VAT. Instead, I intend to broaden the base of the tax by extending the 15 per cent rate to three areas of expenditure that have hitherto been zero-rated.

15. First, alternations to buildings. At present repairs and maintenance are taxed, but alternations are not. The borderline between these two categories is the most confused in the whole field of VAT. /An example?/ I propose to end this confusion, not to mention the illogicality of the difference, by bring all alterations into tax. However, to allow a reasonable time for existing commitments to be completed or adjusted, the change will be deferred until 1 June.

16. Second, I propose to bring into tax newspapers (including newspaper advertisements) and all other pirnted matter, with the sole exception of books, which will remain zero-rated. [Other news media, of course, are already subject to tax. /Check/] This change will apply from 1 April.

17. Third, food. Most food is zero-rated. But food served in restaurants, and a miscellaneous range of items including ice-cream, confectionery, soft drinks and crisps were brought

into tax by the Rt Hon Member for Leeds East. Take-away food clearly competes with these forms of catering, and I therefore intend to bring into tax hot take-away food and drinks, with effect from 1 May.

18. The total effect of the extensions of the VAT coverage which I have proposed will be to increase the yield of the tax by £600 million in 1984-85 and by almost £1 billion in 1985-86.

19. The total impact effect on the Retail Price Index of the VAT changes and excise duty changes taken together will be three-quarters of one per cent. This has already been taken into account in the forecast I gave to the House earlier of a decline in inflation to 4½ per cent by the end of the year.

[20. The revenue raised by the broadening of the VAT base will enable me to lighten the burden of income tax, within the overall framework of a neutral Budget.]

B(84) 1030

Ch/Ex Ref No B(84)549

FROM: J O KERR
DATE: 8 MARCH 1984

Sir P Middleton

cc Sir T Burns
Mr Battishill
Mr Folger
Mr Portillo
Mr Fraser: C & E

PORTILLO

... I attach the latest complete draft of the Budget Speech, and would be most grateful if any suggested amendments could reach me by lunchtime on 9 March. Sections of the Speech are of course being circulated more widely.

J O KERR

+3
112

INTRODUCTION

This Budget will set the Government's course for this Parliament. It is founded on the policies which we have consistently followed since 1979.

The "It" may confuse when heard not read. ?

2. Consistency of purpose is the hallmark of this Government. ~~It is~~ Those policies offer the only way to improve economic performance and ~~lay~~ they have laid the foundations for future prosperity, more jobs and lower taxation. Above all, ~~it is~~ they provide the only way to defeat inflation and achieve our ultimate objective of stable prices.

3. The results of the Medium Term Financial Strategy introduced in 1980 can be seen in true (AB) four years of falling inflation, down now to the lowest levels since the sixties. And that in turn has brought a steady recovery of output, rising living standards and, more recently, rising employment.

4. The facts speak for themselves. They are a tribute to the courage and foresight of the five Budgets presented from this Despatch Box by my distinguished predecessor, the present Foreign Secretary, whose duties sadly keep him in Brussels today.

5. Today's Budget has two themes: first, the further reduction of inflation, which will further improve the prospects

for jobs; and second, the reform and simplification of the tax system~~, which will make it fairer for all~~.

6. I shall begin by reviewing the economic background to the Budget. I shall then deal with the medium term financial strategy; with monetary policy and the monetary targets for next year; and with public borrowing and the appropriate PSBR for the coming year. I shall then turn to public expenditure, including the prospects for the longer term. Finally I shall deal with taxation, and the changes in the structure of taxation which will pave the way for cuts in taxes in subsequent years. Some of these cuts I shall announce today, for this is in a sense a Budget for two years. In a wider sense it is a tax reform Budget, setting out much of our ~~a~~ tax strategy for this Parliament.

7. As usual, a number of press releases will be available from ~~issued today, filling out the details of ~~our~~ ~~my~~ tax proposals.~~ the Vote Office as soon as I have sat down.

THE ECONOMIC BACKGROUND

No "But": you said you would.

8. ~~But~~ I start with the economic background, and the convincing evidence of recovery: a recovery that springs from the monetary and fiscal policies to which we shall hold.

9. Since 1980, inflation has fallen steadily from a peak of over 20 per cent. Last year it was down to about 4½ per cent, the lowest figure since the sixties. And with lower inflation have come lower interest rates.

10. The underlying strength of the recovery is clear. Whereas in some previous cycles recovery has come from a self-defeating stimulus to monetary demand, this time ~~its roots are~~ it has sprung from ~~in our~~ the Government's commitment to sound finance and honest money. Lower inflation and lower interest rates benefit industry, business, and consumer confidence. Falling inflation has made room for real growth, as we always said it would.

?

11. Across the economy, total money incomes grew in 1983 by about 8 per cent, of which 3 per cent represented real growth in output. Although there is still room for improvement, this ~~clearly~~ is a very much healthier division between inflation and real growth than the nation experienced in the 1970s. Output in the second half of 1983 is ~~now reckoned~~ calculated to have exceeded the previous peak, before the world recession set in, and is still rising strongly.

?

12. Productivity too has continued to improve rapidly. Just as over the past year many have wrongly predicted an end to the recovery, so some have tried to dismiss the sharp rise in productivity as a flash in the pan. Yet during 1983 manufacturing productivity grew by 6 per cent with no sign of slowing down. Unit labour costs across the whole economy are likely to show the smallest annual increase since the 1960s. This has allowed a welcome and necessary recovery in real levels of profitability.

13. Higher profits lead to more jobs. The number of people in employment increased by about 85,000 between March and September last year. The loss of jobs in manufacturing has slowed down sharply, while jobs in services increased by ~~getting~~ nearly ~~on for~~ 200,000 in the first nine months of last year. This is encouraging news for the unemployed and for those who will be leaving school this summer.

14. But further progress ~~on productivity~~ is needed: although our unit wage costs in manufacturing rose by under 3 per cent last year, such costs actually fell in the US, Japan and Germany, our three biggest competitors. ~~The employment~~ Lower pay rises could increase our competitiveness; and that would ~~prospect would be significantly improved if a bigger~~ help the prospects for employment. ~~contribution to improved productivity were to come from lower pay rises.~~ Good sense about pay remains vital.

15. Demand, output, profits and employment all rose last year. Home demand has played the major part in the recovery so far. Lower inflation ~~has~~ reduced people's need to save and real

incomes ~~rose~~ have risen. Last year ~~P~~personal consumption increased by over 3½ per cent compared with 1982. Fixed investment rose rather faster than consumption, with investment in housing and services particularly strong.

Positive point first!

16. ~~Imports rose a little faster than home demand last year,~~ ~~a~~As the UK emerged from recession ahead of our main trading partners ~~- o~~Our rate of economic growth last year was the highest in the European Community. For much of 1983 our export performance reflected the weakness ~~in~~ of many of our overseas markets. But by the end of last year world trade was ~~clearly~~ moving ahead again, and in the three months to January manufacturing exports increased very substantially. We estimate that ~~T~~the balance of payments on current account ~~last year is estimated to have been~~ was in surplus by about £2 billion last year.

imports rose a little faster than home demand.

17. Our critics have been confounded by the combination of recovery and low inflation. Even the pessimists have been forced to acknowledge the strength of the recovery. It is set to continue throughout this year at an annual rate of 3 per cent. Inflation is expected to remain low, edging back down to 4½ per cent by the end of this year. With rising incomes and low inflation, personal consumption will continue to grow. ~~And~~ But the recovery is ~~already becoming~~ more broadly based. Encouraged by improved profitability and better long-term growth prospects, investment is expected to rise by 6 per cent this year.

18. Looking abroad, economic prospects are also more favourable than for some time. Output in the United States should continue to grow strongly this year. And recovery is spreading to the rest of the world.

19. Of course, there are ~~inevitable~~ risks and uncertainties. The size and continued growth of the United States budget deficit causes widespread concern, not least among Americans, and keeps American, and hence international, interest rates high. This acts as a brake on world recovery and worsens the problems of the debtor countries. Another consequence is a massive and still growing deficit in the US current balance of payments, financed by inflows of foreign capital, and leading to mounting pressures for protectionism within the United States, and sharp exchange rate movements. The ~~It is an unstable~~ situation is unstable and that causes anxiety. ~~creating worrying uncertainties.~~

Is a risk "inevitable"?

20. There is a ~~A second potential~~ risk of ~~is~~ disruption in the oil market. ~~The immediate prospects are less obviously volatile than they were a year ago. But uncertainties remain, and~~ The United Kingdom, and indeed the world economy, ~~inevitably~~ remains vulnerable to any major disturbances.

? could live to regret?

"inevitable" favourite word

21. But despite these risks there is a growing sense throughout the industrialised world that the recovery this time is not merely cyclical, but one which can be sustained. ~~The essential requirement is~~ The continued pursuit of prudent monetary and fiscal policies is essential to that.

THE MTFS

22. For the United Kingdom, the Medium Term Financial Strategy has been the cornerstone of such policies. It will continue to ~~play that role;~~ be so; ~~and~~ It ~~to~~ provides a framework and discipline for Government and ~~to~~ sets out clearly, to industry and the financial markets, the guidelines of policy. Too often in the past Governments have abandoned financial discipline whenever the going got rough, and ~~been driven to~~ have had to stagger from one short-term policy expedient to another. The temptation to accommodate inflationary pressures proved irresistible, and the nation's longer-term economic performance was progressively undermined.

"cornerstone"? "a role"

23. The discipline of the MTFS was designed to ensure consistency between monetary and fiscal policies, and a proper balance in the economy. It is ~~so~~ designed to ensure that the more inflation and inflationary expectations come down, the more room ~~is available~~ there is for output and employment to grow.

24. People now know that the Government intends to stick to its medium term objectives. They understand that the faster inflation comes down, the faster output and employment recover. Increasing realism, and flexibility in the economy, owe~~s~~ much to the pursuit of firm and consistent policies within the MTFS framework.

25. Originally the MTFS covered four years. In this first Budget of a new Parliament ~~we have thought~~ it is appropriate to carry it forward for five years. So the MTFS published today in the Financial Statement and Budget Report -the Red Book - shows a continuing downward path for the monetary target ranges over the next five years, and a path for public borrowing consistent with that reduction. It takes full account of important influences such as the pattern of North Sea oil revenues, and the level of asset sales arising from the privatisation programme. For the last two years of the new MTFS, which lie beyond the period covered in last year's Public Expenditure Survey and last month's White Paper, the Government has not yet made firm plans for public spending. But the MTFS assumption - and it is ~~no more than~~ just an assumption - is that the level of public spending in 1987-88 and 1988-89 will be the same in real terms as that currently planned for 1986-87.

? 26. The [precise] figures ~~set out~~ in the MTFS are not of course a rigid framework, lacking all flexibility. As in the past, there may ~~well need~~ have to be adjustments to take account of changing circumstances. But ~~such~~ no changes will be made ~~only when they~~ ~~will not~~ that jeopardise the consistent pursuit of the Government's objectives.

Less clumsy
More positive

MONETARY POLICY

27. ~~Monetary policy will continue to play a central role. For~~ Further reductions in monetary growth are needed to achieve still lower inflation.

28. Over the twelve months to mid-February the growth of £M3 has been well within the 7-11 per cent target range, with M1 and PSL2 at or a little above the top of it. ~~While~~ In the early months of the target period most measures of money showed signs of accelerating. But growth in all the target aggregates has since the summer been comfortably within the range.

29. Other evidence confirms that monetary conditions are satisfactory. The effective exchange rate has remained fairly stable, despite the international ~~uncertainties and~~ instability. ~~which I have described.~~ And nominal interest rates have continued to decline in line with falling inflation.

30. ~~To maintain sound monetary conditions in the years ahead the monetary targets must reflect changes~~ in the financial system and in the significance of different measures of money. ~~There is nothing new in this.~~ Over the years we have altered the target ranges and aggregates to take account of ~~such~~ the changes. ~~But the thrust of the strategy has been maintained.~~

Less defensive

That has not changed the thrust of our strategy. To maintain sound monetary conditions, the monetary targets must continue to reflect such changes in the years ahead.

Do we have to say "attempt"?

31. ~~One important development has been the~~ We have attempted to give a more explicit role to the narrow measures of money. Even when targets were set solely in terms of £M3, we recognised the significance of ~~their behaviour.~~ the narrow measures, £M3 and the other broad aggregates give a good indication of the growth of liquidity. But a large proportion of this money is deposited in ways which earn interest. In defining policy ~~it is~~ ~~was~~ it therefore help~~ful~~s also to ~~make specific~~ refer~~ence~~ specifically to measures of money which bear very little interest, and which provide a good guide to the immediate potential for spending.

Ambiguous "their" = "targets"

32. ~~M1 was for this reason~~ That is why we introduced M1 as a target aggregate, but it has not proved entirely satisfactory for that purpose. Its behaviour has been dominated by changes in its large interest-bearing component, which has grown rapidly, and now accounts for 25 per cent of the total. That looks as though it will continue, With the introduction of new, interest bearing chequing accounts~~, the signs are that this will continue.~~

– ~~in particular M1 which consists~~

33. Other measures of narrow money have not been distorted to the same extent. ~~In particular,~~ not M0, ~~which~~ consists mainly of currency, ~~has not been subject to this development~~. It has been affected by other innovations that have reduced people's need for cash, but the pace of change has not diminished its value as an indicator of financial conditions. There is also the new aggregate M2, which was specifically devised to provide a comprehensive measure of transactions balances and which may in time prove a useful guide, but still needs to be interpreted with particular care.

stet

; in particular not M0,

34. In the past two years, it has been possible to set a single target range for both broad and narrow measures of money. But this will not normally be the case; for narrow monetary aggregates tend to grow more slowly than broader measures. And this year's Red Book sets out two separate ranges.

35. The target range for broad money will continue to apply to £M3, and for the coming year will be set at 6-10 per cent, as indicated in last year's MTFS. The target range for narrow money will apply to MO and for next year will be set at 4-8 per cent. To avoid any possible misunderstanding, I stress that the use of MO as a target aggregate will not involve any change in methods of monetary control.

36. Both target ranges will have equal importance in formulating policy. And we shall continue to take into account other measures of money, especially M2 and PSL2, as well as wider evidence of financial conditions, including the exchange rate. As in the past, we shall seek to influence monetary conditions by an appropriate combination of funding and operations in the money market.

37. So far as funding is concerned, the role of the National Savings movement will remain important. This year's target of £3 billion is likely to be achieved: the target for the coming year will again ~~by~~ be £3 billion.

38. Precise monetary targets for the later years will be decided nearer the time. But to give a broad indication of the

objectives of monetary policy, the new MTFS, like previous versions, shows monetary ranges for a number of years ahead. These ranges are consistent with a continuing downward trend in inflation: they demonstrate the Government's intention to make further progress towards stable prices.

PUBLIC SECTOR BORROWING ETC

39. I turn now to public borrowing, for just as the classical formula for financial discipline - the gold standard and the balanced budget - had both a monetary and a fiscal component, so does the medium term financial strategy.

40. The MTFS has always envisaged that the Public Sector Borrowing Requirement would fall as a percentage of Gross Domestic Product over the medium term. And it has, notably as a result of the courageous Budget introduced by my predecessor in 1981, which brought the PSBR down to 3½ per cent of GDP in 1981-82.

41. Since then there has been little further fall. The latest estimate of the PSBR for the current year, 1983-84, remains what it was in November: around £10 billion, equivalent to 3¼ per cent of GDP. This is significantly above what was intended at the time of last year's Budget, and would of course have been higher still had it not been for the measures taken last July.

42. We now need a further substantial reduction in borrowing, in order to help bring interest rates down further as monetary growth slows down. Sterling interest rates are, of course, also influenced by dollar interest rates and so by ~~the US situation which I have already described:~~ conditions in America. But that makes it all the more

important to curb domestic pressures. In contrast to virtually the whole of the post-war period, UK longer-term rates are now lower than American rates. As long as American rates remain near their current level, it is highly desirable that this advantage be maintained.

43. ~~The~~ We are planning a higher level of asset sales ~~planned~~ as the privatisation programme gathers pace. That is a further reason for reducing the PSBR significantly in the coming year. Asset sales reduce the Government's need to borrow. But their effect on interest rates is less than the effect of direct reductions [redacted] in Government spending programmes.

44. Last year's MTFS showed an illustrative PSBR for 1984-85 of 2½ per cent of GDP, equivalent to around £8 billion. But ~~I~~ we believe that it is possible, and indeed prudent, to aim for a somewhat lower figure. ~~I have~~ We are therefore ~~decided to~~ providing for a PSBR next year of 2¼ per cent of GDP, or roughly £7 billion.

45. The House will recall that in November I warned that on conventional assumptions, including the 1983 Red Book's PSBR figure of £8 billion for next year, ~~I~~ we might have to increase taxes slightly in the Budget. I am glad to report that the latest, and more buoyant, forecasts of tax revenue in the coming year, [coupled with the decisions taken in the Public Expenditure Survey and the continuing effects of the July measures,] have changed the picture. Bringing the PSBR down to £7 billion will not

require such an increase in taxation. In fact it will require no overall net increase at all. So the measures I shall shortly announce will, after indexation, be broadly neutral in their effects on revenue in 1984-85.

46. Better still, they will reduce taxation in 1985-86 by some £1¾ billion. And the MTFS published today shows that there should be room for further tax cuts not only in 1985-86, but throughout the remainder of this Parliament, provided that we stick firmly to our published plans for public expenditure to 1986-87, and maintain an equally firm control of public spending thereafter.

PUBLIC EXPENDITURE

47. The Public Expenditure White Paper setting out our spending plans for the next three years was approved by the House last week. Today I want to consider the critically important issue of government spending in a rather wider perspective.

48. For far too long, spending has grown faster than has the economy as a whole. The trend has seemed inexorable, and the result has been that the great mass of the population have had to pay more and more in tax. To take just one example: as recently as 1963-64 no married man had to pay a penny of income tax unless his taxable income was at least 45 per cent of the average earnings level. Today the tax threshold is down to ~~little more than~~ under a third of average earnings. Over the years more and more people on lower and lower incomes have been brought into income tax.

49. We have seen a steady enlargement in the role of the State, at the expense of the individual, and a steady increase in the dead weight of taxation dragging down our economic performance as a nation.

50. ~~Clearly~~ This ~~dangerous~~ process has to stop. Of course, much public spending is directed to eminently desirable ends. But there is an important choice to be made about what levels of tax and public spending are desirable. ~~and~~ It is not

Horrid phrase!

enough simply to make marginal changes in spending programmes from year to year. The choice needs more fundamental national consideration and debate; and it needs to ~~be set within a~~ take account of the longer ~~time horizon~~ term prospects.

51. ~~I am~~ The Government is therefore publishing today, in addition to the customary Budget documents, a Green Paper on the prospects for public spending and taxation in the next ten years. It examines past trends; discusses the pressures for still higher spending; and examines the rewards for ~~the individual~~ people if these pressures can be contained.

52. The Green Paper concludes that, without firm control over public spending, there can be no prospect of bringing the burden of tax back to more reasonable levels. On the assumptions made in the Green Paper, the burden of taxation will be reduced to the levels of the early 1970s only if public spending does not rise in real terms over the next ten years. If, on the other hand, we fail to hold public spending, it will be very difficult to reduce the tax burden. If it ~~spending~~ grows by just 1 per cent a year in real terms after 1988-89, the tax burden would in 1993 ~~by 1990~~ still be only just below the 1978-79 level, and ~~still~~ well above its level in the 1960s. And those figures are based on the assumption that ~~even if~~ the economy grows by about 2 per cent a year over the ten years. Whether that proves over optimistic or not partly depends in itself on ~~And of course excessive taxation slows the whole economy.~~ whether we can reduce taxes, because excessive taxation slows down the whole economy.

53. The Government believes that the issues discussed in the Green Paper merit the attention of the House and the country.

Not entirely true

It is a discussion document ~~- descriptive not prescriptive -~~ and we shall welcome the fullest possible discussion.

54. There is a further ~~I can at once inform the House of a further~~ innovation this year in that ~~In contrast to previous years,~~ I have no specific public expenditure measures to announce in this Budget. The White Paper plans stand.

55. But ~~lest the innovation seems too sweeping,~~ I have ~~can~~ make one small announcement, which I think the House will welcome. We are ~~Within the plans we have been able to~~ providing ~~provide~~ the National Heritage Memorial Fund with extra money ~~additional resources~~ which will enable them, among other things, to secure the future of Calke Abbey. My Rt Hon Friend the Secretary of State for the Environment is providing £6.3 million from his planned expenditure for this year and next, and I have accepted a claim on the Reserve of £2 million for next year.

56. The House will recall that the proposals for the new rates of social security benefit to come into force in November are not now made on Budget day. Following last year's legislation to return to the historic method of uprating, the new rates are ~~price protection~~ calculated from ~~is measured by reference to~~ the Retail Price Index for May. So, ~~Accordingly,~~ my Rt Hon Friend the Secretary of State for Social Services will be announcing the new rates of social security benefits, including Child Benefit, in June.

57. Before ~~turning from~~ leaving Government spending ~~to Government revenue~~, I should add a word on public sector manpower. At the beginning of the last Parliament, the Government set itself the target of reducing the size of the Civil Service from 732,000 in April 1979 to 630,000 by April of this year. That target has been achieved. We have now set ourselves the further target of 593,000 by April 1988, and ~~I am~~ we are confident that it too will be achieved, and that ~~a leaner~~ the Civil Service will continue to ~~operate with increasing~~ improve its efficiency. ~~Speaking for my own Departments,~~ The tax changes I shall be announcing today will reduce manpower requirements by at least 1000 in my Departments which will help towards meeting the 1988 target.

?

TAX REFORM

58. I ~~mentioned~~ said at the outset that this will be a radical, tax-reforming, Budget. It will also significantly reduce the overall burden of tax over the next two years taken together [- and indeed over the whole MTFS period -] and I hope to have scope for further reductions in tax in subsequent Budgets.

59. My proposals for reform are guided by two basic principles. First, the need to make changes that will improve our economic performance [over the longer term]. Second, the desire to make life a little simpler for the taxpayer.

?

60. But I am well aware that the tax reformer's path is a stony one. Any change in the system is bound, at least in the short term, to bring benefits to some and disadvantages to others. And, if I may borrow a phrase from the Rt Hon member for Leeds East, the howls of anguish from the latter group tend to be rather more audible than the murmurings of satisfaction from the former.

61. ~~Reform must succeed, but need not be, in this sense, a howling success. So~~ I have rejected the extreme suggestion, popular in some quarters, that I should scrap our income-based tax system and replace it with a brand new expenditure-based system. A reform of this kind would produce, in the real world, an appalling upheaval ~~of mind-boggling dimensions.~~

Jargon

62. But I don't believe we can afford to opt for the quiet life and do nothing. So ~~I~~ we have chosen ~~the middle way:~~ to work for improvements, some ~~I believe~~ very substantial, ~~but~~ within ~~the framework of~~ our existing income-based system. ~~I shall also be proposing transitional arrangements where I believe it fair and appropriate to do so.~~

63. The changes ~~I shall be proposing today~~ fall into three broad categories: ~~These are~~ the taxation of savings and investment, business taxation, and the taxation of personal income and spending.

SAVINGS AND INVESTMENT

64. First, the taxation of savings and investment. The proposals I am about to make should improve ~~both~~ the direction and quality of both. And they will contribute further to the creation of a property-owning and share-owning democracy, in which more decisions are made by individuals rather than by intermediary institutions.

Remember radio

65. First, stamp duty. This was doubled from its long-standing 1 per cent by the post-war Labour Government in 1947, reduced by the Macmillan Government in 1963, and once again doubled to 2 per cent in the first Budget presented by the Labour Government ~~the Rt Hon member for Leeds East~~ in 1974. At its present level it ~~is an~~ imped~~iment to~~es mobility and is incompatible with the welcome move~~ment~~ to greater competition in the City, following the withdrawal of the Stock Exchange case from the Restrictive Trade Practices Court.

? Trade

66. I therefore propose to halve the rate of stamp duty to 1 per cent. [Transactions from today will benefit from the new rate, unless documents have to be stamped before 20 March, which is the earliest date on which the change will have legal effect.]

67. For the home buyer, the new flat rate 1 per cent stamp duty will start at (an increased threshold of) £30,000. Below this level no duty will ~~in future~~ be payable, and 90 per cent of first time home buyers will therefore not have to pay ~~be liable for~~ stamp duty at all.

68. Reducing the rate of duty on share transfers will remove an important disincentive to direct investment in equities and increase the international competitiveness of our stock market. It should also help British companies to raise equity finance.

69. In addition, I have three proposals to encourage the issue of corporate bonds. I shall go ahead with the new arrangements for deep discount stock and the reliefs for companies issuing Eurobonds and convertible loan stock which were announced but not enacted last year. And I propose to exempt from Capital Gains Tax certain corporate fixed interest securities provided they are held for more than a year. Since such securities are already exempt from stamp duty ~~- an exemption I can confirm also extends to certain convertible loan stocks -~~ this means that the tax concessions for Government borrowing in the gilt-edged market will now be virtually the same as for private sector borrowing in the corporate bond market.

70. The reductions in stamp duty will cost £450 million in 1984-85, of which £160 million is the cost of the relief on share transfers, and £290 million the cost of the relief on transfers of houses and other ~~real estate~~ property.

71. Next, life assurance. I have concluded that there is no longer any justification for Premium Relief on Life Assurance,

Next life assurance. Relief on premiums has been a feature of our tax system for many years, since the far-off days when ~~it~~ life policies provided [almost] the only way [for a man] to provide for [his] family's security. Now policies are taken out more often as an investment than as assurance. So the relief today unduly favours institutional rather than direct investment. And it has spawned a multiplicity --

which is now only one of a number of savings channels for ordinary people. The main effect of the relief today is to encourage institutional rather than direct investment, and to spawn a ~~multiplicity~~ mass of well-advertised tax management schemes. I propose to withdraw the relief on all new policies made after today. I stress that this change will apply only to new (or newly enhanced) policies, taken out or increased after today. Existing policies will not be affected at all. The change is estimated to yield £90 million in 1984-85.

72. We ~~must~~ have also reviewed unjustified penalties on direct personal investment. The Investment Income Surcharge is an unfair and anomalous tax on savings and on the rewards of successful enterprise. It hits the small businessman who reaches retirement without the cushion of a company pension scheme, and impedes the creation of farm tenancies. In the vast majority of cases it is a tax on savings made ~~in the first place~~ out of hard-earned and fully-taxed income. More than half of those who pay the investment income surcharge are over 65, and of these more than half would otherwise be liable to tax at only the basic rate.

No; particular thing.

73. ~~I have therefore decided that~~ The investment income surcharge ~~should~~ will therefore be abolished. The cost in 1984-85 will be some £25 million, and in a full year around £350 million.

74. Finally, I propose to draw more closely together the tax treatment of depositors in banks and building societies.

These institutions compete in the same market for personal deposits. I believe that they should be able to do so on more equal terms as far as tax is concerned.

75. One inequality has already been removed, with the recent change made on legal advice in the tax treatment of building societies' profits from gilt-edged securities. They are now treated in the same way as those of the banks have always been.

76. But the major inequality of treatment, against which the banks in particular have frequently complained, ~~lies with~~ is the special arrangement for interest paid by building societies. ~~under which~~ The societies pay tax at a special rate - the "composite rate" - on the interest paid to the depositor who receives credit for income tax at the full basic rate.

77. This system, which has worked well for the past 90 years, has both an advantage and a disadvantage. The disadvantage is that a minority of depositors, who are below the income tax threshold, still ~~suffer the deduction of tax~~ have tax deducted at the composite rate. However, it is always open to such depositors to put their savings elsewhere, such as National Savings. The advantage of the scheme is its extreme simplicity, particularly for the taxpayer; most taxpayers are spared the bother of paying tax on interest through PAYE or individual assessment, while the Revenue are spared the need to recruit an additional 2000 staff to collect the tax due on interest paid without deduction.

78. In common with my predecessors of all Parties over the past 90 years, I am satisfied that the advantage of the composite rate arrangement outweighs the disadvantage. It follows that equal treatment of building societies and banks should be achieved, not by removing the composite rate from the societies, but by extending it to the banks and other licensed deposit takers.

79. Non-taxpayers will ~~would of course~~ continue to be able to receive interest gross, should they wish to do so, by putting their money into appropriate National Savings facilities. But the purpose of the move is not, of course, to attract savings into Government hands: as I have already announced, next year's target for National Savings will be the same as this year's and last year's, and the total Government appetite for savings, which is measured by the size of the Public Sector Borrowing Requirement, is being significantly reduced. Moreover I have decided to reduce substantially the permitted maximum size of future holdings in the National Savings Investment Account and in Income Bonds.

80. The true purpose of the move is simple: simplicity itself. Unless they are higher rate taxpayers, individual bank customers will, when it comes to tax, be able to forget about bank interest altogether, for all the tax due on it will be deducted at source. The Inland Revenue will be able to make staff savings of up to an extra 1000 civil servants. Moreover, this figure takes no account of the extra numbers that would have

been required to operate the present system as the trend towards the payment of interest on current accounts develops.

81. ~~Accordingly,~~ So I propose to extend the composite rate arrangements to interest received by UK resident individuals from banks and other licensed deposit takers with effect from 1985-86. The composite rate will not apply either to non-residents or to the corporate sector. Arrangements will also be made to exclude from the scheme Certificates of Deposit and Time Deposits of £50,000 or more.

82. Taken together, the major ~~proposals~~ reforms I have just announced on stamp duty, life assurance relief, the investment income surcharge and the composite rate, coupled with other minor proposals, will provide a simpler and more straightforward tax system for savings and investment. They will remove biases which have discouraged the individual saver from investing directly in industry. And they will reinforce the Government's policy of encouraging competition in the financial sector, as in the economy as a whole.

BUSINESS TAXATION

83. I now turn to company taxation.

84. In this area, Government has two responsibilities towards British business and industry. The first is to ensure that they do not have to bear an excessive burden of taxation. The second is to ensure that, given a particular burden, it is structured in the way that does least damage to the nation's economic performance.

85. The measures I am announcing today will, taking the next two years together, result in a ~~very~~ substantial reduction in the burden of taxation on British industry. And in addition I shall be proposing a far-reaching reform of ~~the structure of~~ company taxation.

(see 99) 86.1 Responses to the Corporation Tax Green Paper published in 1982 showed a strong general desire to retain the imputation system. I accept that. But other changes are needed.

86. The current rates of Corporation Tax are far too high, penalising profit and success, and blunting the cutting edge of enterprise. They are the product of too many special reliefs, indiscriminately applied and of diminishing relevance to the conditions of today. Some of these reliefs reflect economic priorities or circumstances which have long vanished, and now serve only to distort investment decisions and choices about finance. Others were introduced to meet short-term pressures, notably the upward surge of inflation. With inflation down to 5 per cent and set to go lower, this is clearly the time to take a fresh look. And with unemployment as high as it is today, it is particularly difficult to justify

year allowance will be reduced from 100 per cent to 75 per cent for all such expenditure incurred after today, and to 50 per cent for expenditure incurred after 31 March next year. After 31 March 1986 there will be no first year allowances, and all expenditure on plant and machinery will qualify for annual allowances on a 25 per cent reducing balance basis.

91. In addition, from next year annual allowances will be given as soon as the expenditure is incurred, and not, as they are today, when the asset comes into use. This will ~~bring~~ be of great benefit to owners of ~~forward the entitlement to annual allowances for those~~ assets, such as ships and oil rigs, for which some payment is normally made well in advance of their being brought into use.

92. For industrial buildings, I propose that the initial allowance should fall from 75 per cent to 50 per cent from tonight, and be further reduced to 25 per cent from 31 March next year. After 31 March 1986 the initial allowance will be abolished, and expenditure will be written off on an annual 4 per cent straight line basis. I should add that, when these changes have all taken place, ~~in respect of~~ both plant and machinery and industrial buildings, tax allowances for will still on average be rather more generous than would be provided by a strict system of economic depreciation.

93. The changes in the rates of allowances will not apply to payments under binding contracts entered into on or before today, provided that the expenditure is incurred within the

next three years.

94. After consulting my Rt Hon Friend the Secretary of State for Trade and Industry, I have decided to make transitional tax arrangements for certain investment projects in the regions. Existing capital allowances will continue to apply to expenditure on projects in Development Areas and special Development Areas for which regional development grants are available and offers of selective assistance have already been made between 1 April 1980 and today. Similar arrangements were announced for regional development grants in my Rt Hon Friend's White Paper on Regional Industrial Development last December.

95. Over the same period to 31 March 1986 most other capital allowances will be brought into line with the main changes I have announced. The Inland Revenue will be issuing a press notice tonight giving full details of these proposals.

96. Next, stock relief. As the House will recall, this was introduced by the last Labour Government as a rough and ready form of emergency help to businesses facing the ravages of high inflation. Th~~e~~ose days are past; and relief is no longer necessary. ~~for~~ Company liquidity has improved and, ~~above all,~~ inflation has fallen sharply. ~~and will be falling further during this Parliament.~~ ~~Accordingly,~~ So, I propose to abolish stock relief from this month.

97. The changes ~~I have~~ just announced, in capital allowances and stock relief, enable ~~me to embark on a~~ the Government to make major ~~programme of progressive~~ reductions in the main rate of Corporation Tax. For profits earned in the year just ending, on which tax is generally payable in 1984-85, the rate will be cut from 52 per cent to 50 per cent. For profits earned in 1984-85 the rate will be further cut to 45 per cent. Looking further ahead, to profits earned in 1985-86, the rate will go down to 40 per cent; and for profits earned in 1986-87 the main rate of Corporation Tax will be 35 per cent.

98. All these rates for the years ahead will be included in this year's Finance Bill.

Wrong place try 86.

99. And they will bring a further benefit. Responses to the Corporation Tax Green Paper published in 1982 revealed a strong and general desire to retain our imputation system of Corporation Tax, ~~This~~ allows a company to offset in full all interest paid. But only a partial deduction for dividends is allowed. Companies thus have an unhealthy incentive to finance themselves through borrowing, in particular bank borrowing, rather than by raising equity capital. The closer the Corporation Tax rate comes to the basic rate of income tax, the smaller this undesirable distortion becomes.

100. Of course, the majority of companies are not liable to pay the main rate of Corporation Tax at all. For them it is the small companies' rate, at present 38 per cent, which applies.

a tax system which encourages low-yielding or even unprofitable investment at the expense of jobs.

87. My purpose therefore is to phase out some unnecessary reliefs, in order to bring about, over time, a markedly lower rate of tax on company profits.

88. First, capital allowances. Over virtually the whole of the post-war period there have been incentives for investment in both plant and machinery and industrial (though not commercial) buildings. But there is little evidence that these incentives have strengthened the economy or improved the quality of investment. Quite the contrary: the evidence suggests that businesses have invested substantially in assets yielding a lower rate of return than the investments made by our principal competitors. Too much of British investment has been made because the tax allowances make it look profitable, rather than because it would be truly productive.

89. The nation needs more investment, and the 6 per cent increase forecast for this year is encouraging. But the greatest benefits flow from investment decisions based on analysis of future market assessments, not future tax assessments.

90. I propose to restructure the capital allowances in three annual stages. In the case of plant and machinery, and assets whose allowances are linked with them, the first

I propose to reduce this rate forthwith to 30 per cent, for profits earned in 1983-84 and thereafter.

101. The Corporation Tax measures I have just announced will cost £280 million in 1984-85. In 1985-86 the cost will be £600 million - made up of £1,150 million by way of reductions in the rates, only partially offset by a £550 million reduction in the value of the reliefs. The estimated costs for later years, which have been provided for in the MTFS figures contained in the Budget Red Book, have been drawn up on a cautious basis. Thus business and industry can go ahead confidently on the basis of the Corporation Tax rates I have announced today, and which set the framework of company taxation for the rest of this Parliament.

Omit?

102. I expect these changes to have ~~both~~ a somewhat different impact in the short ~~term~~ from in the ~~and~~ long term. In the short term, some investment should be brought forward over the next two years, to take advantage of high first year capital allowances while they last - a prospect made all the more alluring for business by virtue of the fact that profits earned will be taxed at the new lower, rates. But the more important and durable effect will be to encourage the search for investment projects with a genuinely worthwhile return, and to discourage uneconomic investment.

103. It is doubtful ~~if~~ whether it was ever really sensible to subsidise capital irrespective of the true rate of return. Certainly,

with over three million unemployed it cannot make sense to do so.

Put above 102.

104. These changes hold out an exciting opportunity for British industry as a whole: an opportunity further to improve its profitability, and to expand, building on the recovery that is already well under way. Higher net profits should encourage and reward enterprise and stimulate [higher current expenditure and] innovation in all its forms - research and development and work on new products, processes and markets. They are the centre-piece, for business, of this Budget and the tax strategy for this Parliament.

105. But I have further measures to announce that are relevant to business.

106. First, the Business Expansion Scheme, introduced last year as a successor to the Business Start Up Scheme, has been widely welcomed as a highly imaginative scheme for encouraging individuals to invest in small companies. It is already proving a considerable success. It now needs time to settle down, and I have only one change to propose this year.

107. The scheme was designed to offer generous incentives for investment in high risk areas by new or expanding companies. Farming is clearly not an area which falls within this category, and I therefore propose that from today farming should cease to be treated as a qualifying trade under the scheme. I am

also ready to consider tightening the scheme further, if it becomes clear at any time in the future that it is being used for purposes for which it was clearly not designed.

108. Secondly, as a measure which will ~~of~~ help ~~to~~ small firms, I propose to raise the VAT registration threshold with effect from midnight tonight from £18,000 to £18,700.

109. Thirdly, in keeping with what I have said about removing distortions, I propose to abolish two reliefs in the personal tax field which were introduced at a time when this country suffered from excessively high rates of income tax. As we have reduced those rates, the reliefs are no longer justified.

Radio!

110. The first distortion is the 50 per cent tax deduction (falling after 9 years to 25 per cent) applied to ~~given from~~ the pay ~~emoluments~~ of foreign employees working here for foreign employers. Foreign employees are often paying much less tax here than they would either at home or in most other European countries. At present income tax rates, the need for the relief has clearly disappeared. Moreover it is open to widespread abuse. It is, for example, possible for the son of an immigrant, working here for a foreign company, to pay tax on only 75 per cent of his salary, even if he himself has lived in this country all his life. I therefore propose to withdraw the relief entirely for all new cases from today. ~~and~~ to withdraw the ~~those already receiving it~~

STET

25 per cent deduction from ~~existing beneficiaries~~ ~~for~~ from 6 April next. The 50 per cent deduction will be phased out over the

those already receiving it.

5 years to 5 April 1989.

111. I also propose to withdraw the so-called foreign earnings relief for United Kingdom residents who ~~perform~~ work ~~their duties~~ both here and ~~overseas~~ abroad and who spend at least 30 days abroad in a tax year. This relief ~~too has lost its~~ was justified ~~rationale, which harks back to the~~ in the days of ~~penalty~~ very high income tax rates, but not now. It too has been exploited, in particular by those who prolong their overseas visits purely in order to gain a tax advantage. For the same reason, I propose to withdraw the matching relief for the self-employed who spend 30 days abroad, and for resident employees and self-employed who have separate employments or separate trades carried on wholly abroad. The relief will be halved to 12½ per cent in 1984-85 and removed entirely from 6 April 1985. However, I have also authorised the Inland Revenue to consult interested parties about a possible relaxation in the rules governing the taxation of expenses reimbursed to employees for travel overseas. I am not making any change to the 100 per cent deduction given for absences abroad of 365 days or more.

112. The abolition of these reliefs will eventually yield revenue savings of over £150 million; and represents another useful step in the removal of complexity and distortions.

113. I need to set the car benefit scales for 1985-86 for those provided with the use of a car by their employer.

Despite the increases over recent years, the levels still fall short of any realistic measure of the true benefit. So I am ~~accordingly~~ proposing an increase of 10 per cent in both the car and car fuel scales with effect from April 1985.

114. Unnecessarily high rates of tax discourage enterprise and risk taking. This is true of the capital taxes, just as it is of the corporation and income taxes. It is a matter of particular concern to those involved in running unquoted family businesses. The highest rates of capital transfer tax are way out of line with comparable rates abroad, and with the top rates of other taxes in this country. I propose therefore to reduce the highest rate of capital transfer tax from 75 per cent to 60 per cent and to raise the threshold to £64,000 in line with indexation. [For lifetime gifts I further propose to make the rate one-half of that on death over the whole scale.]

misleading

115. For capital gains tax I will, as promised, bring forward in the Finance Bill proposals to double the limit for retirement relief to a figure of £100,000, backdated to April 1983. A consultative document on other possible changes in this relief is being issued next week. I am proposing no other changes this year in capital gains tax beyond the statutory indexation of the exempt amount from £5,300 to £5,600. However, the tax continues to attract criticism - not least for its complexity - and that is a matter to which I hope to return in a later year.

116. We have done much to improve the Development Land Tax. Early in the last Parliament, my predecessor increased the threshold from £10,000 to £50,000. I now propose a further increase to £75,000, which will reduce the numbers affected by the tax by more than one-third.

117. Next share options. The measures introduced in the last Parliament to improve employee involvement through profit sharing and savings related share option schemes have been a notable success. The number~~s~~ of all these employee schemes has ~~have~~ increased from about 30 in 1979 to over 670 now, benefiting some half a million employees. To maintain and build on this progress I propose to increase the monthly limit on contributions to savings related share option schemes from £50 to £100. I have also authorised the Inland Revenue to double the tax-free limits under the concession on long service awards and to include the gift of shares in the employee's company.

118. But beyond this, ~~I am convinced that~~ we need to do more to attract top calibre company management and to increase the incentives and motivation of existing executives and key personnel by linking their rewards to performance. I propose therefore that, subject to certain necessary limits and conditions, share options generally will be taken out of income tax, leaving any gain to be charged to capital gains tax on ultimate disposal of the shares. The new rules will

apply to options meeting the conditions which are granted from 6 April, ~~next~~.

119. I am sure that all these changes will be welcomed as measures to encourage the commitment of employees to the success of their companies and to improve the performance, competitiveness and profitability of British industry.

120. Before turning to North Sea taxation, I should like to remind the House of the Government's concern at the threat which the spread of unitary taxation in certain US states has posed to the US subsidiaries of British firms. With our European partners we are monitoring the situation closely, and await with keen interest the imminent report of a Working Group under my US counterpart. It is very important that a satisfactory solution be speedily implemented.

Omit ?

[121. ~~This issue isnot wholly irrelevant to the North Sea, for~~ US firms operating in the North Sea ~~there~~, or elsewhere in this country, are not of course taxed on a unitary basis, taking account of world-wide profits.]

122. Last year's North Sea tax changes were well received, and there has been encouraging progress in the number of development projects coming forward, as well as in exploration and appraisal. The Government is already committed to a study of the economics of investment in new projects within ~~incremental development in~~ existing fields. This is of increasing importance and in consultation with my rt hon friend the Secretary of State for Energy I

therefore propose to review this area with the industry, and to legislate as appropriate next year to improve the position. To prevent projects being deferred pending this review, ~~any~~ the changes will apply to all projects which receive development consent after today.

123. Meanwhile, I am taking two measures to prevent an unjustified loss of tax in the North Sea. First, in addition to the PRT measures on farmouts which I announced last September, I am limiting the potential Corporation Tax cost of such deals. Second, I propose to repeal the provision which allows Advance Corporation Tax to be repaid where Corporation Tax is reduced by PRT. I have concluded that this can no longer be justified. I have also reviewed the case for extending last year's future field concessions to the Southern Basin, but have concluded that additional incentives here are not needed.

124. I have just two further changes affecting business to propose, both of which will come into force on 1 October.

125. Ever since VAT was introduced in this country, we have treated imports differently from the ~~way in which they are treated by~~ way our main European Community competitors treat them. In a nutshell, they require VAT on imported goods to be paid in the same way as customs duties. We do not. Under our system an importer does not have to account for VAT on his

imports until he makes his normal VAT return, on average some 11 weeks later. During this time the importer enjoys free credit at the taxpayer's expense. This is an advan-
goods produced at home competing with
? tage not enjoyed by [the home-produced equivalent of the] imports, since businesses buying from UK suppliers have to pay VAT when they pay their suppliers.

126. The UK system does indeed have many advantages, which is why the European Commission has for some years now been seeking to get it adopted throughout the Community, with the full support of both my predecessor and myself. But the plain fact is that in all that time the Commission has made no progress whatever.

127. I must tell the House that I am not prepared to put British industry at a competitive disadvantage in the home market any longer. Should our European partners at any time undergo a Damascene conversion, and [redacted] agree that the Commission's proposal should be accepted after all, then of course we would gladly revert to the present system. But in the meantime I propose to move to the system used by our major competitors and charge VAT straight away on imports, providing the same facilities for deferring payment as apply to customs duties. That means that most importers will be able to defer payment of VAT by on average one month from the date of importation. But that is all.

128. As I have said, this change will apply from 1 October. By bringing forward VAT receipts, it will bring in an extra £1.2 billion in 1984-85, some of which will of course be borne ~~carried~~ by foreign producers and manufacturers. There will naturally be no increased revenue in subsequent years.

Radio

129. The second change I propose to make on 1 October concerns the National Insurance Surcharge. This tax on jobs once again, was a brainchild of the Labour Government - in particular Rt Hon member for Leeds East. Having introduced it in 1977 at the rate of 2 per cent, he then raised it in 1978 to 3½ per cent. During the last Parliament, ~~my predecessor~~ this Government ~~succeeded in~~ reduced it to 1 per cent, and we are pledged to abolish it during the lifetime of this Parliament.

130. Given the impact that this tax has, not only on industrial costs but also - at a time of high unemployment - on jobs, I have decided to take the opportunity of this my first Budget to fulfil that pledge. Abolition of the National Insurance Surcharge from October will reduce private sector employers' costs by almost £350 million in 1984-85, and over £850 million in a full year.

131. Thus my proposals offer British business the abolition of the tax on jobs and the reduction of the rate of taxation on profits. They also sweep away a number of out-dated reliefs, reduce distortions, and assist enterprise.

INDIRECT TAXES

131. Having announced major reforms of both the taxation of savings and investment and the taxation of business, I turn now to the third and final area in which I propose to make progress on tax reform. This is the taxation of personal income and spending.

check provision

132. The broad principle was clearly set out in the Manifesto on which we were first elected in 1979 and which emphasised the need for a switch from taxes on earnings to taxes on spending. My predecessor made an important move in this direction in <u>his</u> first budget, and the time has come to make a further move today. To reduce direct taxation by this means is important in two ways. It improves incentives and makes it more worthwhile to work, and it increases the freedom of choice of the individual.

133. I do not however see the excise duties - with certain exceptions - as an area for major change. I shall of course need to raise most of the duties broadly in line with inflation, so as to maintain their real value: not to do so would run counter to the philosophy I outlined a moment ago. But with inflation now as low as it is, the necessary increases are on the whole mercifully modest. Only for a few particular duties do I envisage steeper rises.

134. One significant exception is tobacco, where I believe it is right ~~convinced of the need~~ to raise the duty in real terms, ~~to help~~ given ~~cut smoking and thus reduce~~ the potential danger to health. I therefore propose an increase in the tobacco duty which, including VAT, will put 10p on the price of a packet of cigarettes, with corresponding increases for hand-rolling tobacco and cigars. This will do no more than restore the tax on tobacco to its 1965 level. I do not propose to increase the duty ~~in~~ on pipe tobacco at all, which is important for a great many pensioners. These changes will take effect from midnight on Thursday.

135. For the duties on petrol and derv I propose simply to raise them broadly ~~revalorisation, which~~ in line with prices. That means increases which, ~~again~~ also including VAT, will ~~increase~~ raise the price at the pumps by 4½p and 3½p a gallon respectively. I do not propose to increase the duty on heavy fuel oil, which is of particular importance to industrial costs. These changes will take effect for oil delivered from refineries and warehouses from six o'clock this evening.

136. There is one excise duty which I propose to do away with altogether. Many of those who find it hardest to make ends meet, including in particular many pensioners, use paraffin stoves to heat their homes, and it is with them in mind that I propose to abolish the duty on kerosene from six o'clock tonight. I am sure that this will be welcomed on all sides of the House.

137. The various rates of Vehicle Excise Duty will, once again, go up roughly in line with prices. Thus the duty for cars and light vans will be increased by £5, from £85 to £90 a year. However, given the further evidence my Rt Hon Friend the Secretary of State has now received on the wear and tear that various types of vehicle cause to the roads, there will be reductions in duty for the lightest lorries, offset by higher increases for some heavier lorries. All these changes in Vehicle Excise Duty will take effect from tomorrow.

138. However, I propose to exempt from Vehicle Excise Duty all recipients of the War Pensioners' Mobility Supplement.

139. And I have decided to widen the specific VAT reliefs for the disabled in the important area of transport. The existing VAT relief for motor vehicles designed or adapted for use by the handicapped will be extended, and matched by a new Car Tax relief. The effect will be that neither VAT nor car tax will apply to family cars designed for disabled people or substantially adapted for their use.

140. I now come to the most difficult decision I have to take in the excise duty field. As the House will be aware, the rules of the European Community, so far as alcoholic drinks are concerned, are designed to prevent a Member state from protecting its own domestic product by imposing a significantly higher duty on competing imports. In pursuit of this, the Commission has taken a number of countries to the European Court of Justice.

141. In our case, the Commission contended that we were protecting beer by under-taxing it in relation to wine. We fought the case, but lost; and I am now implementing the judgement handed down by the Court last year. Accordingly, I propose to increase the duty on beer, not by the 7p a pint which has been widely rumoured in the press, but by the minimum amount needed to comply with the judgement and maintain revenue: 2p on a typical pint of beer, including VAT. At the same time, the duty on table wine will be reduced by the equivalent of about 18p a bottle, again including VAT.

142. I cannot, however, ignore the fact that while we comply with the judgement of the European Court, one of our partners appears determined not to do so. ~~I refer to~~ Italy, ~~which~~ has been ordered by the Court to remove forthwith its discrimination against Scotch whisky, but as yet shows no sign whatever of complying. I have therefore decided to introduce a temporary duty surcharge on vermouth of some 20p a bottle on top of the basic increase, to which I shall come in a moment. This surcharge will come into operation on 1 September unless the Italian Government has - as I very much hope it will - implemented the Court's judgement by that date, and it will lapse as soon as I am satisfied that it has complied.

143. As for the rest of the alcoholic drinks, cider, which increasingly competes with beer but attracts a lower duty, will go up by 3p a pint. The duties on made-wine will be aligned with those on other wine. And I propose to increase the duty on sparkling wine, fortified wine and spirits by about 10p a

bottle, including VAT. All these changes, except the vermouth surcharge, will take effect from midnight tonight.

144. These changes in excise duties will, all told, bring in some £840 million in 1984-85, some £200m more than is required to keep pace with inflation. The addition is of course ~~largely~~ due to the increase in tobacco duty.

145. But much of the extra revenue I need to make a substantial switch this year from taxes on earnings to taxes on spending will come from VAT. I propose no change in the rate of VAT. Instead, I intend to broaden the base of the tax by extending the 15 per cent rate to two areas of expenditure that have hitherto been zero-rated.

146. First, alterations to buildings. At present repairs and maintenance are taxed, but alterations are not. The borderline between these two categories is the most confused in the whole field of VAT. I propose to end this confusion and illogicality by bringing all alterations into tax. However, to allow a reasonable time for existing commitments to be completed or adjusted, the change will be deferred until 1 June.

147. Secondly, food. Most food is zero-rated. But food served in restaurants is taxed, together with a miscellaneous range of items including ice-cream, confectionery, soft drinks and crisps, which were brought into tax by the Labour Government ~~Rt Hon Member for Leeds East.~~ Take-away food clearly competes with other

forms of catering, and I therefore intend to bring into tax hot take-away food and drinks, with effect from 1 May.

148. The total effect of the extensions of the VAT coverage which I have proposed will be to increase the yield of the tax by £375 million in 1984-85 and by almost £650 million in 1985-86.

149. The total impact effect on the Retail Price Index of the VAT changes and excise duty changes taken together will be less than three-quarters of one per cent. This has already been taken into account in the forecast which I have given to the House of a decline in inflation to 4½ per cent by the end of the year.

150. The extra revenue raised in this way will enable me within the overall framework of a neutral Budget to lighten the burden of income tax.

PERSONAL TAXATION

151. Since we took office in 1979, we have cut the basic rate of income tax from 33 per cent to 30 per cent and sharply reduced the confiscatory higher rates inherited from the last Labour Government. We have increased the main tax allowances not simply in line with prices but by around 8 per cent in real terms. It is a good record. But it is not enough. The burden of income tax is still too heavy.

152. During the lifetime of this Parliament, I intend to carry much further the progress we have already made. For the most part, this will have to wait for future Budgets, particularly since I have thought it right this year to concentrate on setting a new regime of business taxation for the lifetime of a Parliament - and beyond. But as a result of the changes to taxes on spending which I have just announced, I can make a start now.

153. I propose to make no change this year in the rates of income tax. So far as the allowances and thresholds are concerned, I must clearly increase these by the amounts set out in the statutory indexation formula, based on the 5.3 per cent increase in the Retail Price Index to December. The question is how much more I can do, and how to direct it.

154. I have decided that, this year, the right course is to use every penny I have in hand, within the framework of a revenue neutral Budget, to lift the level of the basic tax thresholds, for the married and single alike. It is fundamentally wrong that we collect income tax from people whose incomes are so low that they are entitled to social security benefits on grounds of need. Moreover low tax thresholds make the poverty and unemployment traps much worse, so that the financial incentive to find a job or a
better job ~~or even any job~~ may decline almost to zero. There is, alas, no quick or cheap solution to these problems. But that is all the more reason to make a start on solving them now.

155. I propose to increase most thresholds in line with the statutory requirement, and by no more. The first higher rate of 40 per cent will apply when taxable income reaches £15,400 a year and the top rate of 60 per cent to taxable income of £38,100 or more. The single age allowance will rise from £2,360 to £2,490 and the married age allowance from £3,755 to £3,955.

156. For the basic thresholds, statutory indexation would mean putting the single and married allowances up by £100 and £150 respectively. I am glad to say that I can do considerably better than that. I propose to increase the basic thresholds by well over double what is required by indexation. The single person's threshold will be increased by £220, from £1,785 to £2,005; and the married threshold by £360, from £2,795 to £3,155. ~~The special allowances for widows, and for single parents, will as a consequence go up by some 14 per cent.~~

157. This is an increase of around 12½ per cent, or some 7 per cent in real terms. It brings the married man's tax threshold for 1984-85 to its highest level in real terms since the war. It means that every tax-paying married couple in the land will enjoy an income tax cut of at least £2 a week. And it means that a large number of people, those with the smallest incomes of all, are taken out of income tax altogether. ~~And~~ Some 850,000 people - over 100,000 of them widows - ~~will not pay tax in 1984-85~~ who would have paid if thresholds had not been increased, will pay no tax in 1984-85. That is ~~And~~ 400,000 fewer than if the allowances had merely been indexed.

158. All these changes will take effect under PAYE on the first pay day after 10 May. Their cost is considerable: some £1.8 billion in 1984-85, of which roughly half represents the cost of indexation.

159. This is as far as I can go on income tax this year, within a broadly revenue-neutral Budget for 1984-85. But as I have already said, so long as we hold to our published planned levels of public spending, ~~there is an excellent prospect~~ and while we keep to the ~~consistent with the~~ necessary downward path of ~~public~~ government borrowing, there is an excellent prospect of further tax cuts in next year's Budget. These would be on top of the measures I have announced in this Budget which, as I have already told the House, will reduce taxation in 1985-86 by some £1¾ billion, with business taking the lion's share. So ~~for~~ th next year I ~~would~~ hope to ~~be~~ concentrate ~~ing~~ on further help to people, ~~individuals~~, and ~~principally~~ especially cutting income tax.

CONCLUSION

160. I have, Mr Deputy Speaker, completed the course I charted at the outset this afternoon. I have described the recovery, and how the Government plans to sustain it, by working for further reductions in inflation, by maintaining sound money and by curbing borrowing. I have described a three part reform strategy for a fairer, simpler tax system. And I have been able to propose substantial tax reductions over two years in a Budget that is revenue-neutral for 1984-85. It is a Budget for responsibility and reform; and I commend it to the House.

7.12

BUDGET SECRET

CH/EX REF. NO. B(84)558

FROM: MISS M O'MARA

DATE: 9 March 1984

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Mr Battishill (without attachment)
Mr Cassell
Mr Odling-Smee
Mr Ridley
Mr Lord
PS/IR

cc Mr Allen

MR MONGER

BUDGET SPEECH: TAX REFORM

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

MOM

MISS M O'MARA

TAX REFORM

58. I mentioned at the outset that this will be a radical, tax-reforming, Budget. It will also significantly reduce the overall burden of tax over the next two years taken together [- and indeed over the whole MTFS period -] and I hope to have scope for further reductions in tax in subsequent Budgets.

59. My proposals for reform are guided by two basic principles. First, the need to make changes that will improve our economic performance over the longer term. Second, the desire to make life a little simpler for the taxpayer.

60. But I am well aware that the tax reformer's path is a stony one. Any change in the system is bound, at least in the short term, to bring benefits to some and disadvantages to others. And, if I may borrow a phrase from the Rt Hon member for Leeds East, the howls of anguish from the latter group tend to be rather more audible than the murmurings of satisfaction from the former.

EST has pointed out that Mr Healey was pleased to create howls of anguish.

61. ~~Reform must succeed, but need not be, in this sense, a howling success. So~~ I have rejected the extreme suggestion, popular in some quarters, that I should scrap our income-based tax system and replace it with a brand new expenditure-based system. A reform of this kind would produce, in the real world, an upheaval of mind-boggling dimensions.

62. But I don't believe we can afford to opt for the quiet life and do nothing. So I have chosen the middle way: to work for improvements, some I believe very substantial, but within the framework of our existing income-based system. I shall also be proposing transitional arrangements where I believe it fair and appropriate to do so.

63. The changes I shall be proposing today fall into three broad categories. These are the taxation of savings and investment, business taxation, and the taxation of personal income and spending.

CONCLUSION

160. I have, Mr Deputy Speaker, completed the course I charted at the outset this afternoon. I have described the recovery, and how the Government plans to sustain it, by working for further reductions in inflation, by maintaining sound money and by curbing borrowing. I have described a three part reform strategy for a fairer, simpler tax system. And I have been able to propose substantial tax reductions over two years in a Budget that is revenue-neutral for 1984-85. It is a Budget for responsibility and reform; and I commend it to the House.

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CH/EX REF. NO. B 84 557

FROM: MISS M O'MARA

DATE: 9 March 1984

D

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Mr Folger (without attachment)
Mr Odling-Smee
Mr Ridley
Mr Lord
PS/IR

MR BATTISHILL (WITHOUT ATTACHMENT)

BUDGET SPEECH: INTRODUCTION

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by <u>lunch time today</u>.

MOM

MISS M O'MARA

Mr Battishill c Miss O'Mara

Some suggestions below. The first is important.

MJJ

9.3.84

INTRODUCTION

This Budget will set the Government's course for this Parliament. It is founded on the policies which we have consistently followed since 1979.

2. Consistency of purpose is the hallmark of this Government. It is the only way to improve economic performance and lay the foundations for future prosperity, more jobs and lower taxation. Above all, it is the only way to defeat inflation and achieve our ultimate objective of stable prices.

NB

"three" OR "nearly four"

3. The results of the Medium Term Financial Strategy introduced in 1980 can be seen in ~~four~~ years of falling inflation, down now to the lowest levels since the sixties. And that in turn has brought a steady recovery of output, rising living standards and, more recently, rising employment.

4. The facts speak for themselves. They are a tribute to the courage and foresight of the five Budgets presented from this Despatch Box by my distinguished predecessor, the present Foreign Secretary, whose duties sadly keep him in Brussels today.

5. Today's Budget has two themes: first, the further reduction of inflation, which will further improve the prospects

for jobs; and second, the reform and simplification of the tax system~~, which will make it fairer for all~~.

6. I shall begin by reviewing the economic background to the Budget. I shall then deal with the medium term financial strategy; with monetary policy and the monetary targets for next year; and with public borrowing and the appropriate PSBR for the coming year. I shall then turn to public expenditure, including the prospects for the longer term. Finally I shall deal with taxation, and the changes in the structure of taxation which will pave the way for cuts in taxes in subsequent years. Some of these cuts I shall announce today, for this is ~~in a sense~~ a Budget not just for the coming year but for 1985-86 and beyond, ~~for two years.~~ In a wider sense it is a tax reform Budget, setting out a tax strategy for this Parliament.

optional suggestion in interests of accuracy.

7. As usual, a number of press releases will be issued today, filling out the details of my tax proposals.

BUDGET SECRET

CH/EX REF. NO. B(84)559

FROM: MISS M O'MARA

DATE: 9 March 1984

cc Chief Secretary
Financial Secretary
Economic Secretary
Mr Battishill (without attachment)
Mr Cassell
Mr Lankester
Mr Odling-Smee
Mr Ridley
Mr Lord
PS/IR

cc Mr Allen

MR MONGER

BUDGET SPEECH: SAVINGS AND INVESTMENT

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

MOM

MISS M O'MARA

SAVINGS AND INVESTMENT

64. First, the taxation of savings and investment. The proposals I am about to make should improve both the direction and quality of both. And they will contribute further to the creation of a property-owning and share-owning democracy, in which more decisions are made by individuals rather than by intermediary institutions.

[avoid repetition of both].

I begin circle

65. First, stamp duty. This was doubled from its long-standing 1 per cent by the post-war Labour Government in 1947, reduced by the Macmillan Government in 1963, and once again doubled to 2 per cent in the first Budget presented by the Rt Hon member for Leeds East in 1974. At its present level it is an impediment to mobility and incompatible with the welcome movement to greater competition in the City, following the withdrawal of the Stock Exchange case from the Restrictive Practices Court.

[To avoid repetition of "first"].

66. I therefore propose to halve the rate of stamp duty to 1 per cent. [Transactions from today will benefit from the new rate, unless documents have to be stamped before 20 March, which is the earliest date on which the change will have legal effect.]

67. For the home buyer, the new flat rate 1 per cent stamp duty will start at (an increased threshold of) £30,000. Below this level no duty will in future be payable, and 90 per cent of first time home buyers will therefore not be liable for stamp duty at all.

[Delete: Investment through institutions also benefits].

68. Reducing the rate of duty on share transfers will remove an important disincentive to ~~direct~~ investment in equities and increase the international competitiveness of our stock market. It should also help British companies to raise equity finance.

69. In addition, I have three proposals to encourage the issue of corporate bonds. I shall go ahead with the new arrangements for deep discount stock and the reliefs for companies issuing Eurobonds and convertible loan stock which were announced but not enacted last year. And I propose to exempt from Capital Gains Tax certain corporate fixed interest securities provided they are held for more than a year. Since such securities are already exempt from stamp duty ~~- an exemption I can confirm also extends to certain convertible loan stocks -~~ this means that the tax concessions A[for Government borrowing in the gilt-edged market]A will now be virtually the same as B[for private sector borrowing in the corporate bond market]B.

Transpose A - A and B - B.

70. The reductions in stamp duty will cost £450 million in 1984-85, of which £160 million is the cost of the relief on share transfers, and £290 million the cost of the relief on transfers of houses and other real estate.

71. Next, life assurance. I have concluded that there is no longer any justification for Premium Relief on Life Assurance,

which is now only one of a number of savings channels for ordinary people. The main effect of the relief today is to encourage institutional rather than direct investment, and to spawn a multiplicity of well-advertised tax management schemes. I propose to withdraw the relief on all new contracts ~~(policies)~~ made after today. I stress that this change will apply only to new (or newly enhanced) policies, taken out or increased after today. Existing policies will not be affected ~~at all.~~ The change is estimated to yield £90 million in 1984-85.

[Revenue suggests "contracts" as a precise & legally defined term]

[Delete 'at all'; they will be affected if enhanced]

71A. Paragraph on friendly societies: EST minute of today.

72. We must also review unjustified penalties on direct personal investment. The Investment Income Surcharge is an unfair and anomalous tax on savings and on the rewards of successful enterprise. It hits the small businessman who reaches retirement without the cushion of a company pension scheme, and impedes the creation of farm tenancies. In the vast majority of cases it is a tax on savings made in the first place out of hard-earned and fully-taxed income. More than half of those who pay the investment income surcharge are over 65, and of these more than half would otherwise be liable to tax at only the basic rate.

73. I have therefore decided that the investment income surcharge should be abolished. The cost in 1984-85 will be some £25 million, and in a full year around £350 million.

74. Finally, I propose to draw more closely together the tax treatment of depositors in banks and building societies.

These institutions compete in the same market for personal deposits. I believe that they should be able to do so on more equal terms as far as tax is concerned.

of a rather different nature

75. One inequality has already been removed, with the recent change made on legal advice in the tax treatment of building societies' profits from gilt-edged securities. They are now treated in the same way as those of the banks have always been.

76. But the major inequality of treatment, against which the banks in particular have frequently complained, lies with the special arrangement for interest paid by building societies, under which the societies pay tax at a special rate - the "composite rate" - on the interest paid to the depositor who receives credit for income tax at the full basic rate.

77. This system, which has worked well for the past 90 years, has both an advantage and a disadvantage. The disadvantage is that a minority of depositors, whose incomes ~~who~~ are below the income tax threshold, still suffer ~~the deduction of~~ tax at the composite rate. ~~However, it is always open to such depositors to put their savings elsewhere, such as National Savings.~~ The advantage of the scheme is its extreme simplicity, particularly for the taxpayer; most taxpayers are spared the bother of paying tax on interest through PAYE or individual assessment, while the Revenue are spared the need to recruit up to ~~an additional~~ 2000 extra staff to collect the tax due on interest paid without deduction.

[Revenue suggestion: "Deduction" not exactly right, but will do if necessary].

(Revenue suggest "up to" because of uncertainty of figures).

HF prefer: "It has not however stopped many of them using Building Societies because of the competitive rates they have offered". They point out that National Savings are referred to in 79.

Not strictly accurate. There was a move to withdraw the Composite Rate before the war, which was stopped by the war. But this will do if necessary.

78. In common with my predecessors of all Parties over the past 90 years, I am satisfied that the advantage of the composite rate arrangement outweighs the disadvantage. It follows that equal treatment of building societies and banks should be achieved, not by removing the composite rate from the societies, but by extending it to the banks and other licensed deposit takers.

[Optional: seems to read better].

79. Non-taxpayers will ~~would~~ ~~of course~~ continue to be able to receive interest gross, should they wish to do so, by putting their money into appropriate National Savings facilities. But the purpose of the move is not, of course, (omit) to attract savings into Government hands: as I have already announced, next year's target for National Savings will be the same as this year's and last year's, and the total Government appetite for savings, which is measured by the size of the Public Sector Borrowing Requirement, is being significantly reduced. Moreover I have decided to reduce substantially the permitted maximum size of future holdings in the National Savings Investment Account and in Income Bonds.

[Suggestion by Mr Ridley].

80. The true purpose of the move are ~~is~~ simple: fairer competition and simplicity itself. The great majority of ~~Unless they are higher rate taxpayers~~, individual bank customers will, when it comes to tax, be able to forget about bank interest altogether, for all the tax due on it will have been ~~be deducted~~ already paid at source. The Inland Revenue will be able to make staff savings of up to an extra 1000 civil servants. Moreover, this figure takes no account of the extra numbers that would have

~~The gross~~

Necessary for accuracy.

Reference to deduction not strictly correct. But this will do if necessary.

been required to operate the present system as the trend towards the payment of interest on current accounts develops.

81. Accordingly, I propose to extend the composite rate arrangements to interest received by UK resident individuals from banks and other licensed deposit takers with effect from 1985-86. The composite rate will not apply either to non-residents or to the corporate sector. Arrangements will also be made to exclude from the scheme Certificates of Deposit and Time Deposits of £50,000 or more.

82. Taken together, the major proposals I have just announced on stamp duty, life assurance relief, the investment income surcharge and the composite rate, coupled with other minor proposals, will provide a simpler and more straightforward tax system for savings and investment. They will remove biases which have discouraged the individual saver from investing directly in industry. And they will reinforce the Government's policy of encouraging competition in the financial sector, as in the economy as a whole.

7.12

B(84) 1028

BUDGET SECRET

CH/EX REF. NO. B(84) 550

FROM: MISS M O'MARA

DATE: 9 March 1984

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Mr Battishill (without attachment)
Mr Evans
Mr Lavelle
Mr Botrill
Mr Shields
Mr Odling-Smee
Mr Ridley
Mr Lord

MR FOLGER (WITHOUT ATTACHMENT)

BUDGET SPEECH: THE ECONOMIC BACKGROUND

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

MOM

MISS M O'MARA

Miss O'Mara c Mr Shields

Some points below, as discussed with Mr Shields.

MJF

9.3.84

THE ECONOMIC BACKGROUND

8. But I start with the economic background, and the convincing evidence of recovery: a recovery that springs from the monetary and fiscal policies to which we shall hold.

Strongly advisable: the "calendar year on calendar year" figure never got above 18.4% & the 4½% is calendar on calendar.

9. Since 1980, inflation has fallen steadily from a peak of over 20 per cent. Last year the increase in prices over the preceding year it was down to about 4½ per cent, the lowest figure since the sixties. And with lower inflation have come lower interest rates.

10. The underlying strength of the recovery is clear. Whereas in some previous cycles recovery has come from a self-defeating stimulus to monetary demand, this time its roots are in our commitment to sound finance and honest money. Lower inflation and lower interest rates benefit industry, business, and consumer confidence. Falling inflation has made room for real growth, as we always said it would.

11. Across the economy, total money incomes grew in 1983 by about 8 per cent, of which 3 per cent represented real growth in output. Although there is still room for improvement, this ~~clearly~~ is a very much healthier division between inflation and real growth than the nation experienced in the 1970s. Output in the second half of 1983 is now reckoned to have exceeded the previous peak, before the world recession set in, and is still rising strongly.

12. Productivity too has continued to improve rapidly. Just as over the past year many have wrongly predicted an end to the recovery, so some have tried to dismiss the sharp rise in productivity as a flash in the pan. Yet during 1983 manufacturing productivity grew by 6 per cent with no sign of slowing down. Unit labour costs across the whole economy are likely to show the smallest annual increase since the 1960s. This has allowed a welcome and necessary recovery in real levels of profitability.

NB revised figure to be published 14 March make it essential to round down here (as in FSBR)

13. Higher profits lead to more jobs. The number of people in employment increased by about ~~85,000~~ 80,000 between March and September last year. The loss of jobs in manufacturing has slowed down sharply, while jobs in services increased by getting on for 200,000 in the first nine months of last year. This is encouraging news for the unemployed and those who will be leaving school this summer.

14. But further progress ~~on productivity~~ is needed: although our unit wage costs in manufacturing rose by under 3 per cent last year, such costs actually fell in the US, Japan and Germany, our three biggest competitors. The employment prospect would be significantly improved if a bigger contribution to improved ~~productivity~~ competitiveness were to come from lower pay rises. Good sense about pay remains vital.

15. Demand, output, profits and employment all rose last year. Home demand has played the major part in the recovery so far. Lower inflation reduced people's need to save and real

incomes rose. Personal consumption increased by over 3½ per cent compared with 1982. Fixed investment rose rather faster than consumption, with investment in housing and services particularly strong.

16. Imports rose a little faster than home demand last year, as the UK emerged from recession ahead of our main trading partners. Our rate of economic growth last year was the highest in the European Community. For much of 1983 our export performance reflected the weakness in many of our overseas markets. But by the end of last year world trade was clearly moving ahead again, and in the three months to January manufacturing exports increased very substantially. The balance of payments on current account last year is estimated to have been in surplus by about £2 billion.

17. Our critics have been confounded by the combination of recovery and low inflation. Even the pessimists have been forced to acknowledge the strength of the recovery. It is set to continue ~~throughout~~ this year at an annual rate of 3 per cent. Inflation is expected to remain low, edging back down to 4½ per cent by the end of this year. With rising incomes and low inflation, personal consumption will continue to grow. And the recovery is already becoming more broadly based. Encouraged by improved profitability and better long-term growth prospects, investment is expected to rise by 6 per cent this year.

NB
second half on first half is only 2.7% annual rate

18. Looking abroad, economic prospects are also more favourable than for some time. Output in the United States should continue to grow strongly this year. And recovery is spreading to the rest of the world.

(stylistic – para ends with same word)

19. Of course, there are inevitable risks [~~and uncertainties~~.] The size and continued growth of the United States budget deficit causes widespread concern, not least among Americans, and keeps American, and hence international, interest rates high. This acts as a brake on world recovery and worsens the problems of the debtor countries. Another consequence is a massive and still growing deficit in the US current balance of payments, financed by inflows of foreign capital, and leading to mounting pressures for protectionism within the United States, and sharp exchange rate movements. It is an unstable situation, creating worrying uncertainties.

20. A second potential risk is disruption in the oil market. The immediate prospects are less obviously volatile than they were a year ago. But uncertainties remain, and the United Kingdom, and indeed the world economy, inevitably remains vulnerable to any major disturbances.

21. But despite these risks there is a growing sense throughout the industrialised world that the recovery this time is not merely cyclical, but one which can be sustained. The essential requirement is the continued pursuit of prudent monetary and fiscal policies.

7.12

BUDGET SECRET

CH/EX REF. NO. BC(84)564.

FROM: MISS M O'MARA

DATE: 9 March 1984

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Mr Cassell
Mr Battishill (without attachment)
Mr Odling-Smee
Mr Ridley
Mr Lord
PS/IR

cc Mr Allen

MR MONGER

BUDGET SPEECH: PERSONAL TAXATION

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

MOM

MISS M O'MARA

PERSONAL TAXATION

151. Since we took office in 1979, we have cut the basic rate of income tax from 33 per cent to 30 per cent and sharply reduced the confiscatory higher rates inherited from the last Labour Government. We have increased the main tax allowances not simply in line with prices but by around 8 per cent in real terms. It is a good record. But it is not enough. The burden of income tax is still too heavy.

152. During the lifetime of this Parliament, I intend to carry much further the progress we have already made. For the most part, this will have to wait for future Budgets, particularly since I have thought it right this year to concentrate on setting a new regime of business taxation for the lifetime of a Parliament - and beyond. But as a result of the changes to taxes on spending which I have just announced, I can make a start now.

153. I propose to make no change this year in the rates of income tax. So far as the allowances and thresholds are concerned, I must clearly increase these by the amounts set out in the statutory indexation formula, based on the 5.3 per cent increase in the Retail Price Index to December. The question is how much more I can do, and how to direct it.

154. I have decided that, this year, the right course is to use every penny I have in hand, within the framework of a revenue neutral Budget, to lift the level of the basic tax thresholds, for the married and single alike. It is fundamentally wrong that we collect income tax from people whose incomes are so low that they are entitled to social security benefits on grounds of need. Moreover low tax thresholds make the poverty and unemployment traps much worse, so that the financial incentive to find a better job or even any job may decline almost to zero. There is, alas, no quick or cheap solution to these problems. But that is all the more reason to make a start on solving them now.

EST has commented that Sir G Howe made some moves in this direction.

155. I propose to increase most thresholds in line with the statutory requirement, and by no more. The first higher rate of 40 per cent will apply when taxable income reaches £15,400 a year and the top rate of 60 per cent to taxable income of £38,100 or more. The single age allowance will rise from £2,360 to £2,490 and the married age allowance from £3,755 to £3,955.

156. For the basic thresholds, statutory indexation would mean putting the single and married allowances up by £100 and £150 respectively. I am glad to say that I can do considerably better than that. I propose to increase the basic thresholds by well over double what is required by indexation. The single person's threshold will be increased by £220, from £1,785 to £2,005; and the married threshold by £360, from £2,795 to £3,155. ~~The special allowances for widows, and for single parents, will as a consequence go up by some 14 per cent.~~

[Optional: will keep to avoid repetition of threshold].

157. This is an increase of around 12½ per cent, or some 7 per cent in real terms. It brings the married man's tax allowance ~~threshold~~ for 1984-85 to its highest level in real terms since the war. It means that every tax-paying married couple of working age in the land will enjoy an income tax cut of at least £2 a week. And it means that a large number of people, those with the smallest incomes of all, are taken out of income tax altogether. ~~And~~ Some 850,000 people - over 100,000 of them widows - will not pay tax in 1984-85 who would have done so ~~[paid]~~ if thresholds had not been increased. And 400,000 fewer than if the allowances had merely been indexed.

[This seems necessary for accuracy. Pensioners may not get the £2 cut].

[Optional: makes slightly easier reading].

158. All these changes will take effect under PAYE on the first pay day after 10 May. Their cost is considerable: some £1.8 billion in 1984-85, of which roughly half represents the cost of indexation.

159. This is as far as I can go on income tax this year, within a broadly revenue-neutral Budget for 1984-85. But as I have already said, so long as we hold to our published planned levels of public spending, there is an excellent prospect consistent with the necessary downward path of public borrowing of further tax cuts in next year's Budget. These would be on top of the measures I have announced in this Budget which, as I have already told the House, will reduce taxation in 1985-86 by some £1¾ billion, with business taking the lion's share. So for next year I would hope to be concentrating on further help to individuals, and principally on income tax.

B(84) 606.

Arrived 6.40pm! We'll send back your own amended version as soon as it's ready. Mom.

FROM: F CASSELL
9 March 1984

MISS O'MARA

cc - Economic Secretary
Sir P Middleton
Sir T Burns
Mr Battishill
Mr Lankester
Mrs Lomax
Mr Ridley
Mr Lord

BUDGET SPEECH: MONETARY POLICY

I have shown the section on monetary policy that you circulated this morning to Eddie George.

His reactions were very much on the same points as were commented on in Tim Lankester's note to you. But he had quite a neat reformulation of paragraph 31, which the Chancellor might like to consider, and some additional suggestions on paragraphs 33, 36 and 37.

Paragraph 31. Replace last two sentences by:-

> "But a large proportion of this money is in reality a form of savings, invested for the interest it can earn. In defining policy it is helpful also to make specific reference to measures of money which relate more narrowly to balances held for current spending."

Paragraph 33, last sentence. Since we say in the MTFS we are in fact going to make use of M2 in interpreting MO the phrase "may in time prove" may look odd. He would prefer:-

> "... of transactions balances. This may also be a useful guide but, being new, still needs to be interpreted with particular care."

Paragraph 36, third line. Add after PSL2 ", which include building society liabilities,".

Paragraph 37. There is no mention of (or for) gilts, only of National Savings. The message that the market wants to have is that we will be making less demands on it. This message could be conveyed by extending the opening of the paragraph:-

> "So far as funding is concerned, the public sector's borrowing requirement, as I shall shortly explain, will be significantly lower in the coming year. In financing it, the role of ~~the~~ National Savings ~~movement~~ ..."

I think all these suggestions are helpful. I slightly prefer the George version of paragraph 31 to the Lankester; the important point, however, is that either is preferable to the existing version.

F CASSELL

7.12'

B(84) 1020.

391/84

BUDGET SECRET

cc Miss O'Mara

CH/EX REF. NO. B(84) 565

FROM: MISS M O'MARA

DATE: 9 March 1984

D

cc Chief Secretary
Financial Secretary
Mr Cassell
Mr Lovell
Mr Odling-Smee
Mr Ridley
Mr Lord
PS/IR

Mr Monck.

Some comments. First an important general point. Is it clear enough that the changes in allowances & stock relief apply to all enterprises not just companies. §86 & 87 could easily be construed to imply the latter only. This could in turn
(a) provoke much anxious questioning from the unincorporated;
(b) provoke further dismay & possibly even accusations of deviousness when we give the answer that the changes are universal.

§88 understates a good argument. I like the rhetoric of the last sentence; but "market assessments" is not quite right. tho I can't find a better phrase yet.

MR MONCK

§127 needs a disclaimer, to reassure people that VAT on imports will not create frontier congestion!

BUDGET SPEECH: BUSINESS TAXATION

AR 9/3

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

89

MOM

MISS M O'MARA

BUSINESS TAXATION

83. I now turn to company taxation.

84. In this area, Government has two responsibilities towards British business and industry. The first is to ensure that they do not have to bear an excessive burden of taxation. The second is to ensure that, given a particular burden, it is structured in the way that does least damage to the nation's economic performance.

85. The measures I am announcing today will, taking the next two years together, result in a [redacted] substantial reduction in the burden of taxation on British industry. And in addition I shall be proposing a far-reaching reform of the structure of company & business taxation.

??
necessary to worry unincorporated?

86. The current rates of Corporation Tax are far too high, penalising profit and success, and blunting the cutting edge of enterprise. They are the product of too many special reliefs, indiscriminately applied and of diminishing relevance to the conditions of today. Some of these reliefs reflect economic priorities or circumstances which have long vanished, and now serve only to distort investment decisions and choices about finance. Others were introduced to meet short-term pressures, notably the upward surge of inflation. With inflation down to 5 per cent and set to go lower, this is clearly the time to take a fresh look. And with unemployment as high as it is today, it is particularly difficult to justify

a tax system which encourages low-yielding or even unprofitable investment at the expense of jobs.

87. My purpose therefore is to phase out some unnecessary reliefs, in order to bring about, over time, a markedly lower rate of tax on company profits.

88. First, capital allowances. Over virtually the whole of the post-war period there have been incentives for investment in both plant and machinery and industrial (though not commercial) buildings. But there is little evidence that these incentives have strengthened the economy or improved the quality of investment. Quite the contrary: the evidence suggests that businesses have invested substantially in assets yielding a lower rate of return than the investments made by our principal competitors. Too much of British investment has been made because the tax allowances make it look profitable, rather than because it would be truly productive.

But higher investment will only bring proper returns to the nation when

89. The nation needs more investment, and the 6 per cent increase forecast for this year is encouraging. ~~But the greatest benefits flow from investment decisions~~ based on analysis of future market assessments, not future tax assessments.

?

90. I propose to restructure the capital allowances in three annual stages. In the case of plant and machinery, and assets whose allowances are linked with them, the first

next three years.

94. After consulting my Rt Hon Friend the Secretary of State for Trade and Industry, I have decided to make transitional tax arrangements for certain investment projects in the regions. Existing capital allowances will continue to apply to expenditure on projects in Development Areas and special Development Areas for which regional development grants are available and offers of selective assistance have already been made between 1 April 1980 and today. Similar arrangements were announced for regional development grants in my Rt Hon Friend's White Paper on Regional Industrial Development last December.

95. Over the same period to 31 March 1986 most other capital allowances will be brought into line with the main changes I have announced. The Inland Revenue will be issuing a press notice tonight giving full details of these proposals.

96. Next, stock relief. As the House will recall, this was introduced by the last Labour Government as a rough and ready form of emergency help to businesses facing the ravages of high inflation. These days are past; and therefore the relief is no longer justified ~~necessary~~; for company liquidity has improved and, above all, inflation has fallen sharply. ~~and will be falling further during this Parliament.~~ Accordingly, I propose to abolish stock relief from this month.

(many will still claim it after all is still needed, or beneficial!)

97. The changes I have just announced, in capital allowances and stock relief, enable me to embark on a major programme of progressive reductions in the main rate of Corporation Tax. For profits earned in the year just ending, on which tax is generally payable in 1984-85, the rate will be cut from 52 per cent to 50 per cent. For profits earned in 1984-85 the rate will be further cut to 45 per cent. Looking further ahead, to profits earned in 1985-86, the rate will go down to 40 per cent; and for profits earned in 1986-87 the main rate of Corporation Tax will be 35 per cent.

That will mean a cut of no less than 17 pts overall over 3 years

98. All these rates for the years ahead will be included in this year's Finance Bill.

99. And they will bring a further benefit. Responses to the Corporation Tax Green Paper published in 1982 revealed a strong and general desire to retain our imputation system of Corporation Tax. This allows a company to offset in full all interest paid. But only a partial deduction for dividends is allowed. Companies thus have an unhealthy incentive to finance themselves through borrowing, in particular bank borrowing, rather than by raising equity capital. The closer the Corporation Tax rate comes to the basic rate of income tax, the smaller this undesirable distortion becomes.

100. Of course, the majority of companies are not liable to pay the main rate of Corporation Tax at all. For them it is the small companies' rate, at present 38 per cent, which applies.

I propose to reduce this rate forthwith to 30 per cent, for profits earned in 1983-84 and thereafter.

101. The Corporation Tax measures I have just announced will cost £280 million in 1984-85. In 1985-86 the cost will be £600 million - made up of £1,150 million by way of reductions in the rates, only partially offset by a £550 million reduction in the value of the reliefs. The estimated costs for later years, which have been provided for in the MTFS figures contained in the Budget Red Book, have been drawn up on a cautious basis. Thus business and industry can go ahead confidently on the basis of the Corporation Tax rates I have announced today, and which set the framework of company taxation for the rest of this Parliament.

102. I expect these changes to have both a somewhat different impact in the short and long term. In the short term, some
brought investment should be forward over the next two years, to take advantage of high first year capital allowances while they last - a prospect made all the more alluring for business by virtue of the fact that profits earned will be taxed at the
long-term new lower, rates. But the more important and durable effect will be to encourage the search for investment projects with a genuinely worthwhile return, and to discourage uneconomic investment.

103. It is doubtful if it was ever really sensible to subsidise capital irrespective of the true rate of return. Certainly,

except as a temporary emergency measure

with over three million unemployed it cannot make sense to do so.

104. These changes hold out an exciting opportunity for British industry as a whole: an opportunity further to improve its profitability, and to expand, building on the recovery that is already well under way. Higher net profits should encourage and reward enterprise and stimulate [higher current expenditure and] innovation in all its forms - research and development and work on new products, processes and markets. They are the centre-piece, for business, of this Budget and the tax strategy for this Parliament.

105. But I have further measures to announce that are relevant to business.

106. First, the Business Expansion Scheme, introduced last year as a successor to the Business Start Up Scheme, has been widely welcomed as a highly imaginative scheme for encouraging individuals to invest in small companies. It is already proving a considerable success. It now needs time to settle down, and I have only one change to propose this year.

107. The scheme was designed to offer generous incentives for investment in high risk areas by new or expanding companies. Farming is clearly not an area which falls within this category, and I therefore propose that from today farming should cease to be treated as a qualifying trade under the scheme. I am

also ready to consider tightening the scheme further, if it becomes clear at any time in the future that it is being used for purposes for which it was clearly not designed.

108. Secondly, as a measure of help to small firms, I propose to raise the VAT registration threshold with effect from midnight tonight from £18,000 to £18,700.

109. Thirdly, in keeping with what I have said about removing distortions, I propose to abolish two reliefs in the personal tax field which were introduced at a time when this country suffered from excessively high rates of income tax. As we have reduced those rates, the reliefs are no longer justified.

110. The first distortion is the 50 per cent tax deduction (falling after 9 years to 25 per cent) ~~given from~~ applied to the emoluments of foreign employees working here for foreign employers. Foreign employees are often paying much less tax here than they would either at home or in most other European countries. At present income tax rates, the need for the relief has clearly disappeared. Moreover it is open to widespread abuse. It is, for example, possible for the son of an immigrant, working here for a foreign company, to pay tax on only 75 per cent of his salary, even if he himself has lived in this country all his life. I therefore propose to withdraw the relief entirely for all new cases from today, and to withdraw the 25 per cent deduction from existing beneficiaries from 6 April next. The 50 per cent deduction will be phased out over the

Despite the increases over recent years, the levels still fall short of any realistic measure of the true benefit. I am accordingly proposing an increase of 10 per cent in both the car and car fuel scales with effect from April 1985.

114. Unnecessarily high rates of tax discourage enterprise and risk taking. This is true of the capital taxes, just as it is of the corporation and income taxes. It is a matter of particular concern to those involved in running unquoted family businesses. The highest rates of capital transfer tax are way out of line with comparable rates abroad, and with the top rates of other taxes in this country. I propose therefore to reduce the highest rate of capital transfer tax from 75 per cent to 60 per cent and to raise the exemption threshold to £64,000 in line with indexation. [For lifetime gifts I further propose to make the rate one-half of that on death over the whole scale.]

misleading

115. For capital gains tax I will, as promised, bring forward in the Finance Bill proposals to double the limit for retirement relief to a figure of £100,000, backdated to April 1983. A consultative document on other possible changes in this relief is being issued next week. I am proposing no other changes this year in capital gains tax beyond the statutory indexation of the exempt amount from £5,300 to £5,600. However, the tax continues to attract criticism - not least for its complexity - and that is a matter to which I hope to return in a later year.

116. We have done much to improve the Development Land Tax. Early in the last Parliament, my predecessor increased the threshold from £10,000 to £50,000. I now propose a further
of cases increase to £75,000, which will reduce the number~~s~~ affected by the tax by more than one-third.

117. Next share options. The measures introduced in the last Parliament to improve employee involvement through profit sharing and savings related share option schemes have been a notable success. The numbers of all these employee
Right! schemes have increased from about 30 in 1979 to over 670
covering now, benefiting some half a million employees. To maintain and build on this progress I propose to increase the monthly limit on contributions to savings related share option schemes from £50 to £100. I have also authorised the Inland Revenue to double the tax-free limits under the concession on long
without those limits service awards and to include the gift of shares in the employee's company.

118. But beyond this, I am convinced that we need to do more to attract top calibre company management and to increase the incentives and motivation of existing executives and key personnel by linking their rewards to performance. I propose therefore that, subject to certain necessary limits and conditions, share options generally will be taken out of income tax, leaving any gain to be charged to capital gains tax on ultimate disposal of the shares. The new rules will

apply to options meeting the conditions which are granted from 6 April, [redacted].

119. I am sure that all these changes will be welcomed as measures to encourage the commitment of employees to the success of their companies and to improve the performance, competitiveness and profitability of British industry.

120. Before turning to North Sea taxation, I should like to remind the House of the Government's concern at the threat which the spread of unitary taxation in certain US states has posed to the US subsidiaries of British firms. With our European partners we are monitoring the situation closely, and await with keen interest the imminent report of a Working Group under my US counterpart. It is very important that a satisfactory solution be speedily implemented.

121. This issue isnot wholly irrelevant to the North Sea, for US firms operating there, or elsewhere in this country, are not of course taxed on a unitary basis, taking account of world-wide profits.

122. Last year's North Sea tax changes were well received, and there has been encouraging progress in the number of development projects coming forward, as well as in exploration and appraisal. The Government is already committed to a study of the economics of investment in incremental development in existing fields. This is of increasing importance and in consultation with my rt hon friend the Secretary of State for Energy I

imports until he makes his normal VAT return, on average some 11 weeks later. During this time the importer enjoys free credit at the taxpayer's expense. This is an advantage not enjoyed by the home-produced equivalent of the import, since businesses buying from UK suppliers have to pay VAT when they pay their suppliers.

126. The UK system does indeed have many advantages, which is why the European Commission has for some years now been seeking to get it adopted throughout the Community, with the full support of both my predecessor and myself. But the plain fact is that in all that time the Commission has made no progress whatever.

127. I must tell the House that I am not prepared to put British industry at a competitive disadvantage in the home market any longer. Should our European partners at any time undergo a Damascene conversion, and agree that the Commission's proposal should be accepted after all, then of course we would gladly revert to the present system. But in the meantime I propose to move to the system used by our major competitors and charge VAT straight away on imports, providing the same facilities for deferring payment as apply to customs duties. That means that most importers will be able to defer payment of VAT by on average one month from the date of importation. But that is all.

Surely a reference here is needed to tell people this will not create disruption at ports & frontiers

128. As I have said, this change will apply from 1 October. By bringing forward VAT receipts, it will bring in an extra £1.2 billion in 1984-85, some of which will of course be borne ~~carried~~ by foreign producers and manufacturers. There will naturally be no increased revenue in subsequent years.

129. The second change I propose to make on 1 October concerns the National Insurance Surcharge. This, once again, was a brainchild of the Rt Hon member for Leeds East. Having introduced it in 1977 at the rate of 2 per cent, he then raised it in 1978 to 3½ per cent. During the last Parliament, my predecessor succeeded in reducing it to 1 per cent, and we are pledged to abolish it during the lifetime of this Parliament.

130. Given the impact that this tax has, not only on industrial costs but also - at a time of high unemployment - on jobs, I have decided to take the opportunity of this my first Budget to fulfil that pledge. Abolition of the National Insurance Surcharge from October will reduce private sector employers' costs by almost £350 million in 1984-85, and over £850 million in a full year.

131. Thus my proposals offer British business the abolition of the tax on jobs and the reduction of the rate of taxation on profits. They also sweep away a number of out-dated reliefs, reduce distortions, and assist enterprise.