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PART F

1987 FINANCE BILL

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25

MR A J WALKER/IR

FROM: NIGEL WILLIAMS

DATE: 2 July 1987

cc PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Scholar
Mr Evans
Miss Evans
PS/IR

SUMMER FINANCE BILL: GENERAL INLAND REVENUE PRESS RELEASE

The Financial Secretary was grateful for your minute of 1 July.

2. This is to confirm that he was content with the press release attached to your minute subject to the change suggested by the Economic Secretary (as further amended).

NIGEL WILLIAMS
(Assistant Private Secretary)



Inland Revenue

Policy Division
Somerset House

28

From: J B SHEPHERD
Ext: 7019
Date: 2 July 1987

PS/EST (MR BARNES)

SUMMER FINANCE BILL 1987: BANKS - TAX CREDIT RELIEF

You telephoned me 2 July to say that the Economic Secretary had suggested that he might write to the British Bankers' Association on Finance Bill publication day, introducing the changes to Clauses 67 and 68 compared with the clauses as originally introduced. You cited the analogy of the oil clauses (minute Miss Hill to Economic Secretary 1 July 1987 enclosing a draft letter Economic Secretary to the Director General UKOOA).

We agree that a similar letter in the case of the banks would be appropriate and I attach a draft for the Economic Secretary's approval.

J B SHEPHERD

cc PS/Chancellor
PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
Mr Haigh
Mr Graham (OPC)

Mr Painter
Mr Taylor Thompson
Mr Beighton
Mr Cleave
Mr Shepherd
Mr Spence
Mr Hunter
Mr J F Hall
Mr Skinner
Mr Sharp
PS/IR

DRAFT PUBLICATION DAY LETTER

ECONOMIC SECRETARY TO -

Mr D M Child CBE
Chairman, Executive Committee
British Bankers' Association
10 Lombard Street
LONDON EC3

BANKS: TAX CREDIT RELIEF

The Finance Bill, published today, contains two clauses (67 and 68) which reintroduce the provisions of the original 1987 Bill (where they were Clauses 52 and 53).

Your members may like to note that Clause 67 contains two changes from the earlier version. The first is a technical amendment to Section (5A) to correct an oversight in the previous draft. The amendment provides that in computing the net profits on each loan it will be permissible to take into account charges (deductible against total profits) as well as expenses (which are deductible in computing those profits of the lender which are brought into charge to income tax or corporation tax). It was always the intention that both kinds of expenditure should be taken into account.

The second and more significant change alters the effective date of the new rules for loans already in existence on 1 April 1987. Having looked carefully at the representations which have been made by your association we have concluded that the transitional period of grace should be doubled to two years.

I know that the banks have had certain reservations about the practicability of the proposals and I endorse what my predecessor said to you in April about the Government's sharing your concern that the system

should be workable. In that connection I have had a full report of your Committee's meeting on 30 June with the Inland Revenue which focussed upon the scope and detail of the proposed supporting regulations. I should like to thank the Association for the amount of time and constructive effort that they have contributed to their detailed discussions about the proposed legislation with the Inland Revenue.

RESTRICTED



28

FROM: N WILLIAMS

DATE: 2 July 1987

DEPUTY PARLIAMENTARY CLERK

cc: PPS

PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Miss CEC Sinclair - FP
Mr K Bradley - CA
PS/IR
PS/HMCE

FINANCE BILL 1987/8: NOTES ON CLAUSES

The Financial Secretary was grateful for your minute of 29 June.

2. This is to confirm that he was content for the Parliamentary Question as set out in your note to be tabled today (Thursday) for answer tomorrow.

A handwritten signature in dark ink, appearing to read "N Williams", with a long horizontal stroke extending to the right.

NIGEL WILLIAMS
(Assistant Private Secretary)

pur



FROM: ANTHONY DIGHT

DATE: 3 July 1987

PS/CHANCELLOR/2

CC:

Mr N Williams

Miss J Long

Mrs J Daly

Mr N Dawson

Mr Culpin

Mr Dyer

Mr P Wales

Mr N Forman MP

Mr T Favell MP

Mr D Heathcoat-Amory MP

Mr M Stern MP

**2ND READING OF THE FINANCE BILL DEBATE:
MINISTERIAL BENCH DUTY ROTA - WEDNESDAY 8 JULY**

I have set out below the Ministerial Duty Rota which has been agreed:

CST to open debate	3.30pm approx.	(All members should to be present)
Financial Secretary	5.30pm - 6.30pm	
Paymaster General	6.30pm - 7.30pm	
Economic Secretary	7.30pm - 9.00pm	
Financial Secretary	9.00pm - 10.00pm	(To close debate)

A handwritten signature in blue ink that reads "Anthony Dight".

ANTHONY DIGHT
Diary Secretary



FROM: ANTHONY DIGHT

DATE: 6 July 1987

MR C HUTSON

CC:

PS/Chancellor /2
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary
Miss O'Mara
Ms C Evans
Mr Patterson
Mr Haigh
Mr Romanski
Mr P Cropper
Mr A Tyrie
Mr A Hudson

Mr Walker - IR
Mr D Shaw - IR
Mr Munroe - IR
Mr Spence - IR
Mr Bolton - IR

PS/Customs & Excise

SECOND READING OF THE FINANCE BILL: WEDNESDAY 8 JULY

... Could you please let the House Authority know that the officials on the attached list will be occupying the official box at various times during the Second Reading of the Finance Bill Debate on Wednesday 8 July.

ANTHONY DIGHT

Diary Secretary

Inland Revenue

Mr Walker
Mr D Shaw
Mr Moore
Mr Spence
Mr Bolton

FP

Ms Evans
Mr Haigh
Mr Romanski

EB

Miss O'Mara
Mr Patterson

Special Advisers

Mr Cropper
Mr Tyrie
Mr A Hudson



INLAND REVENUE
CENTRAL DIVISION
SOMERSET HOUSE

18

FROM: D SHAW
DATE: 7 JULY 1987

PS/FINANCIAL SECRETARY

SUMMER FINANCE BILL

As requested in your note of 29 June to Mr Walker, I attach a note commenting on the points made in the Institute of Directors' representations.

D. Shaw

D SHAW

PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Scholar
Mr Walters

Mr Isaac
Mr Painter
Mr Beighton
Policy Directors
Mr Johns
Mr Walker
Mr Shaw - CD
PS/IR

ITEMS FROM FINANCE ACT 1987

Income tax rates

Representation

The IOD propose that the higher rates of income tax should be reduced immediately (ie in the current Finance Bill).

Comment

The Chancellor told the Financial Times (5 January) that "we may well need to bring our top rate down further" in the next Parliament. All income tax rates need to come down if we are to remain competitive with those countries which are currently making substantial changes in income tax, including reductions in their top rates. But it would be wrong to change now the fiscal stance for 1987-88 which the Chancellor set out in his Budget Statement. Whatever the longer term effects of cutting tax rates in stimulating additional revenue in the short term cutting the top rate of income tax to 50% for the current year would lead to a loss of revenue in 1987-88 of about £1/4 billion.

Additional rate for trusts

Representation

The IOD suggest that the additional rate for trusts should be abolished or, failing that, reduced significantly.

Comment

Trusts provide an opportunity for sheltering income from higher rates of tax. Generally accepted that not right to tax trust income at only basic rate and so provide opportunity for avoidance by all higher rate taxpayers.

Although introduced at the same time as investment income surcharge, aim was to pitch charge at a level somewhere along the progressive scale of tax for individuals. Seen as a flat rate substitute in the trust field for the graduated higher rates of tax imposed on individuals and still represents a considerable tax saving for those taxpayers liable to tax at rates above 45 per cent.

Payments of trust income to beneficiaries carry credit of 45 per cent; where beneficiary is liable at less than this rate, or is not liable to pay tax, he can reclaim from Inland Revenue part or all of tax suffered by trustees.

Corporation tax payment date

Representation

The IOD consider that it is unjust to accelerate CT payment dates and that this will result in companies being charged to tax over more accounting periods than there would be in the life of the company. They suggest that some profits should be allowed to drop out of charge to tax when the payment date is brought forward.

Comment

Although this change does prevent abuse of the CT payment rules this was not its main purpose. Ministers decided that the time was right to standardise the payment rules for all companies (and building societies) and so put them on an equal footing.

This will mean that some companies will have their CT payments accelerated over the transitional period. But these companies will typically have obtained a considerable benefit in the period since 1965. Each year, such a company's tax liability will have been based on profits of an earlier period than those being taxed in the case of a company with a nine months payment interval. Since profits have tended to rise over time, partly as a result of inflation, a company with a long payment interval has therefore received a continuing advantage. Of course, the value of this depends upon the particular circumstances of a particular company. But, for many companies the value could be at least as great as the cost to the company of having its payment interval reduced to nine months.

This change in payment dates does not cause a company to pay more tax over its life - it merely accelerates payment. So Ministers decided against allowing any profits to drop out of charge to tax. They concluded that the only relief which should be given was to phase in the change so as to ease any cash flow difficulties.

Carry-back of BES relief

Representation

The IOD consider that the maximum amount of relief of £5,000 which can be carried back is far too low to be worthwhile, and suggest a figure of £20,000, being one half of the maximum relief available.

Comment

The aim is that the carry-back should encourage investment in the early part of the year, but not to the extent that it is so attractive for investors that it leads to the peak of investment moving from the last quarter of the tax year to the second quarter of the next tax year. Without some restriction there is a real danger that this would happen. The £5,000 limit was based on the amounts of BES relief claimed in 1984-85, which is

the last year for which we have full information.

We shall not know what will happen in practice until the new relief has been running for a couple of year (1987-88 will not provide much of a guide because most people will have made their BES investments for 1986-87 before they know that they would be able to carry-back relief on investments made in the first half of 1987-88). We shall then be able to consider the case for changing the £5,000 limit.

ITEMS DROPPED FROM FINANCE BILL 1987

Occupational Pension Schemes

Representation

The IOD criticise the anti-exploitation legislation on two points:

1. the more restrictive rules for accelerated accrual of pension and lump sum benefits and the £150,000 limit on lump sums will inhibit job mobility because people will not leave their existing pension schemes.
2. the new legislation was not fore-shadowed in "Improving the Pensions Choice" or any other consultative document.

Comment

The first point covers well-trodden ground. Ministers are aware of the point but - as the Financial Secretary said during the pre-Election Committee Stage debates - the overall effect of the pensions reform package will encourage mobility (Standing Committee B, 7 May 1987, col 115).

The second point is misconceived. It has never been the policy to give prior warning of measures against exploitation. To do so would simply invite forestalling.

Retrospective overruling of cases

Representation

The IOD urge that any legislative overruling of court decisions both in the case of Padmore v IRC and the recent Special Commissioners decision on roll-over of oil licence gains should be retrospective only to the date the proposal was announced.

Comment

Clause 62 of the Summer Bill ensures that a UK resident member of an overseas partnership is chargeable to tax in the UK, notwithstanding the provisions of any double taxation agreement, on his share of any income arising, or capital gains accruing, to the partnership. Subject to an exception relating to decisions of the Commissioners and courts made before 17 March 1987 the clause applies retrospectively (that is it prevents claims being made for six years back). The legislation on the roll-over of oil licence gains (clause 80 of the Summer Bill) makes clear that oil licences are not a qualifying asset for roll-over relief purposes. Potential claims totalling some £150 million in respect of past gains are thus forestalled.

Ministers accept that retrospection is open to objection where a taxpayer has arranged his affairs on the basis of existing law as generally understood and the law is then changed with retrospective effect so that he finds himself faced with unexpected - and unprovided for - liability for past years. The legislation on foreign partnerships and the roll-over of oil licence gains is quite different, as Ministers have accepted. As a result of the Padmore case as it stands, a partner in an overseas partnership who has paid UK tax on the partnership profits in the normal way would be able to obtain an entirely unexpected benefit in the form of recovery of the tax for the past six years. Equally the Special Commissioners' decision on roll-over relief could have meant an uncovenanted benefit for certain oil companies in respect of farm out gains made up to 6 years ago. The purpose of retrospection in both these cases is thus to prevent taxpayers obtaining such a windfall advantage, not to inflict an unexpected tax charge on the unwary.

Dual Resident Companies

It is not true to say, as the IOD do, that the proposals in the Bill incorporate only a few minor changes from the draft legislation in the consultative document of 5 December 1986. The two main representations made in response to that document have been dealt with: the definition of investing company (it is now clearer that the relevant clause does not apply to a genuine trading company which needs to have investments for its trade such as an insurance company) and an element of retrospection (the provisions do not apply to forestalling arrangements made before the date of the consultative document).

The IOD ask:

(a) Why the UK needs legislation when the US has already legislated: the answer to this is that it is likely that the UK without legislation would be left bearing most of the cost of giving relief. In any event the US legislation does not meet all our concerns (eg there are no anti-avoidance provisions) and cannot cover UK/third country DRCs.

(b) Why the UK legislation needs to deny any relief for loss-making DRCs: the answer to this is that DRCs are in general set up to exploit tax provisions and there is no justification for encouraging their perpetuation.

(c) Why the UK legislation needs to come into force before the US regulations have been published: the answer to this is that it may be a long time before the new regulations are published and it is unreasonable that the UK should continue to give relief while the US is denying relief (even though the regulations have not yet been published).

For the above reasons the Government is acting solely on the basis of what is in the UK's interest (as opposed to the US's interest). The UK was considering action (1984 consultative document) before the US.

The IOD argue that if there is justification for the UK legislation, companies should be able to elect in which country to have the relief. As Ministers know, we explored in some detail with the US the possibility of an election but it did not prove possible to devise a suitable arrangement: it would be necessary to harmonise relevant provisions of several countries exactly and even then DRCs might be able to get some alternative form of overseas relief, thus side-stepping the DRC legislation.

Technical points (in Annex):

- (i) "Tax" means tax on profits (cf Section 84(1) FA 1984).
- (ii) Local and state taxes not to be taken into account and territory refers to sovereign states.
- (iii) "Place of management" and "residence" to be interpreted according to tests well established and used in double taxation agreements for many years.
- (iv) The DRC would be within the "charge to tax" in a foreign territory but subject to any double tax treaty.
- (v)/(vi) "The main function or one of its main functions" was intended to distinguish the main function of a company from subsidiary functions. For example, the only main function of an ordinary insurance company is the business of insurance. Assets are required and held as an incident in the course of the company's insurance business but not as a main function. The clauses amended prevent avoidance by a company carrying on a distinct trade while simultaneously carrying on other significant activities mentioned in the clause.
- (vii) No justification for legislation which bites only when double relief is in point because no justification for non-trading DRCs. No company has indicated that it has a current problem.
- (viii) Our Section 482 Unit has given every assistance to companies wishing to restructure.

Lloyd's Underwriters

Comment

The IOD have lined themselves up with Lloyd's arguments about the provisioning approach. Their line is, in fact, simply a rehearsal of the arguments Lloyds have put forward. It can be expected they will take their cue from Lloyds in their response (favourable or otherwise) to the revised clause in the Bill.

Rate of tax on chargeable gains

Representation

The IOD suggest that it is wrong in principle to charge corporate gains at rates applicable to income.

Comment

With the main CT rate reduced (from 52% in 1979) to 35%, the case for a differential lower rate on gains is now much weaker. For small companies the rate of tax on gains is reduced from 30% to 27%. For larger companies the rate is increased to 35% but these companies are more likely to benefit from ACT set-off. Most other countries charge corporate gains at income rates.

ACT Imputation on Companies' Gains

Representation

The IOD urged the reintroduction of this measure in the Summer Bill.

Comment

This measure has been reintroduced.

Personal Pension Schemes

Representation

The IOD argue that the legislation should be amended to include profit-related pay as "relevant earnings".

Comment

There is no need: the present definition achieves this result.

Representation

The IOD asked for confirmation that the death benefit will be excluded from the IHT charge on death and can be nominated to specific beneficiaries as with death benefit under RAP schemes.

Comment

It will be possible, as it is now, for death benefits under clauses 25 and 26 of the Summer Bill to be excluded from the IHT charge.

Representation

The IOD asked what would happen to the surplus if the lump sum permissible under clause 26(2) was less than the full value of the of the fund on death.

Comment

We do not think it is possible for a surplus to arise under clause 26(2).

Representation

The IOD suggest that clause 29(1)(a) needs amendment to reflect the decision to allow an individual to have more than one personal pension scheme.

Comment

Clause 29(1)(a) has been amended to meet this point.

Representation

The IOD suggest that provision should be made for the individual whose scheme's approval has been withdrawn by the Inland Revenue to transfer his investments to another approved scheme.

Comment

Schemes will be required, as a condition of approval, to include in their rules provision for an individual's investments to be transferred if approval is withdrawn.

Inheritance Tax - Interests in Possession

Representation

The IOD urged the reintroduction of these provisions in the Summer Bill.

Comment

These measures have been reintroduced.

Profit-Related Pay

Representation

Where an employee is a member of more than one registered PRP scheme, he should be able to choose the scheme for which he will get relief.

Comment

Clause 4(1), (formerly 110(1)), provides that an employee cannot receive tax-exempt PRP in respect of more than one simultaneous employment. There are no provisions concerning how this is to be brought about, and there is therefore no bar on an employee's negotiating with his employer(s) about which scheme participation is to attract the tax relief. This is solely a matter for employers and employees.

Representation

The time allowed for submission of a joint notification of a change of scheme employer should be six months, not one month.

Comment

Clause 9 (formerly 115) seeks to ensure continuity of a scheme where the only change is of the scheme employer. It allows the two employers to make a joint application within one month of the succession and that results in re-registration in the new employer's name.

A brief time limit is needed here - for example, to ensure that no substantial gap exists where interim payments are in force. Six months destroys the intent of the provision - to provide a rapid replacement without affecting the scheme.

A change of employer will not normally come as a shock to the outgoing employer: there will doubtless have been negotiations (on a wide range of matters, including the effects on employers) beforehand, effectively lengthening the one month period terms of consideration of what action is needed.

Representation

An annual return for PRP purposes is required (under Clause 12, formerly 118) earlier than it is required for corporation tax purposes (under Clause 82 (formerly 123)).

Comment

The longer period permitted under Clause 82 reflects the greater amount of work required in completing the return. A corporation tax return requires full computations of tax due, including capital allowances claims. A PRP return will be accompanied by the profit and loss account which in the case of an employment unit which is an incorporated enterprise must be submitted within the same time limits to the Registrar of Companies (the PRP account will be modified only in minor ways - for example, to reflect the adjustments permitted by paragraph 19(6) of the schedule). The computation of the PRP pool must be regarded as a much simpler exercise and the computation of corporation tax due.

Further, any greater delay in the completion of the PRP account will probably have the undesirable consequences, in a number of cases, of delaying distribution of PRP to employees.

Taxes Management Provisions

Representation

The Revenue should not be given broad powers to prescribe the information, accounts, statements and reports to be supplied with companies' tax returns.

Comment

The relevant clause has been redrafted for inclusion in the Summer Finance Bill to meet these criticisms. We have removed the power allowing the Revenue to use regulations to expand upon the questions in the return. We have restricted the accounts which can be required from companies resident in the UK to the ones they prepare under the Companies Act. There will be continuing consultations with the representative bodies on the contents of the new returns to ensure that, whilst meeting the needs of the Revenue, they do not place an excessive burden on businesses.

Representation

Interest rates under the new penalty regime should be the same for over- and under-payments.

Comment

Interest rates will be crucial to the success of Pay and File. The term "mirror-image interest" was used to mean that interest would run for the same period in either direction. It was never meant to mean that interest rates would necessarily be the same in either direction. There will be further consultations with the representative bodies before any decision is taken on how interest rates should be set. In the meantime, the provision does no more than to preserve the present arrangements for setting interest rates.

Representation

Where a company makes an over-payment of tax before the due date it should not have to wait until after the "material date" to obtain a refund.

Comment

This is based on a misunderstanding. The company will be entitled to a refund before the material date and no special provision is needed for this in the legislation.



Inland Revenue

Policy Division
Somerset House

Handwritten initials

FROM: N C MUNRO

7 July 1987

PS/Financial Secretary

PENSIONS: SECOND READING

As requested, I attach short speaking notes on various pensions matters which may crop up during the debate.

N C Munro

N C MUNRO

cc PPs
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Scholar
Miss Evans
Mr Cropper
Mr Tyrie

Mr Isaac
Mr Beighton
Mr Corlett
Mr Munro
Mr Walker
Mr Hinton
PS/IR

Anti-exploitation provisions will inhibit job mobility

This overlooks the fact that, if an individual qualifies for maximum benefits after as little as ten years service, any 'retained benefits' from earlier employments, must be taken into account. And it ignores the effect of the overall reforms package on this problem. In particular, the introduction of personal pensions and free-standing additional voluntary contributions and the lifting of the restrictions on transferability (together with the DHSS changes on the revaluation of deferred pension rights) will greatly ease the present pensions barriers to labour mobility.

Pension considerations only one factor in decision to change job.

AVC benefit limits: impossible to police

Members of occupational schemes will have a right (under Social Security legislation) to know how much their pension rights are worth and, therefore, what scope there is within the overall benefit limits to pay AVCs. This is a calculation which the scheme managers should carry out under present rules, with 'in-scheme' AVCs, in order to guard against excessive contributions. For free-standing AVCs they will have to make the same calculation, and this information will be conveyed by the scheme member to the AVC provider.

When benefits are payable, the scheme member will have to inform his employer's scheme of any AVC benefits, so that his overall entitlement from all schemes can be determined, and any necessary adjustments made to main scheme benefit.

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PRESSED

[If, on the other hand, the benefit limits were disapplied, it would be possible for someone in a non-contributory occupational scheme to invest up to 15 per cent of salary in a free-standing AVC scheme and increase his total pension benefits way beyond the two-thirds final salary maximum under existing rules. This would increase enormously the cost of the already very generous tax reliefs for pensions, and the scope for abuse. The pensions tax reliefs were never intended simply to provide a tax shelter for investment generally.

Important to remember that free-standing AVCs are integral part of benefits, provided for member of occupational pension scheme. They are not personal pensions under another name.]

Sir Brandon Rhys Williams' proposals: force pension schemes to provide better benefits for early leavers and pensioners

Understand hon Friend's continuing concern about this point. He will be well aware that recent Social Security legislation has done much to improve the position for early leavers - greater transferability, revaluation of preserved benefits etc. Our proposals for personal pensions and free-standing AVCs take this further. Do not think it would be right to compel pension schemes to provide benefits at a particular level.

Even if we were persuaded such a sanction would be appropriate, far from clear that it would be proper to impose it through the tax system.

[In general, the purpose of the tax rules is to contain the cost of the special reliefs for pensions, and to safeguard eg maximum contributions and maximum benefits. My Hon Friend's proposals would, if implemented through the tax regime, introduce a new condition for approval

FOR USE IF
PRESSED

based on minimum levels of benefit. This new condition would have no relevance to the control of the cost of the tax reliefs or the prevention of abuse.]

No consistent Government policy on pensions: Revenue and DHSS policies conflict

Do not accept this. Government's policy is to ensure that people can enjoy an adequate income in retirement. Revenue limits on pension benefits simply intended to control cost of tax reliefs for pensions and to ensure that relief is given only for genuine retirement provision.

Reforms do not go far enough: missed opportunity to harmonise occupational and personal pensions tax regimes

This is attractive in principle - but difficult to see how such harmonisation could be achieved. The tax regime for occupational pensions is defined benefit (with no overall direct limit on contributions); the tax regime for personal pensions is defined contribution (with on limit on total benefits).

It would be easy to harmonise these two fundamentally different regimes if the benefit limits were abandoned (but that would be very costly and would tend to turn the relief into one for saving and investment generally) or if rigid contribution limits applied to everyone (but the pensions industry would not welcome that).

Andrew

FROM: MISS C EVANS
DATE: 2 July 1987

FINANCIAL SECRETARY

cc **Chancellor**
Chief Secretary
Paymaster General
Economic Secretary
Sir Peter Middleton
Mr Scholar
Miss Sinclair
Miss O'Mara
Mr Hudson
Mr Cropper
Mr Tyrie
Mr Guy (ministry/only)
Mr Walker - IR

SECOND READING: WIND-UP SPEECH

As requested I attach material on

- i. PRP
- ii. Keith
- iii. inheritance tax
- iv. pensions
- v. tax reform

2. The material on Keith supersedes paragraphs 50-56 of the draft opening speech - the Chief Secretary has agreed to omit these.

C.

You may like to glance at:
-PRP

CE

MISS EVANS

1. As my right honourable Friend explained in his opening Speech, profit related pay can make a major contribution to the further strengthening of the economy. There are major weaknesses in the operation of our labour market that must be tackled.
2. We must get away from the delusion that employees should be rewarded without any regard to the commercial success of what they produce. We need pay systems which acknowledge the basic and self-evident truth that a business can only pay wages out of money which it gets in. If it isn't getting in enough - if its profits aren't doing well - then the sooner that pay levels respond to the realities of the situation, the better for all concerned.
3. We need much less of the going rate for the job approach to pay. The idea of a rate for the job which takes no account of what rate can be afforded, and what it will mean for jobs and for business growth, is a recipe for disaster. Because what we get then is not a rate for the job but a rate for fewer jobs.
4. What we need instead is pay systems which can respond and adapt to the changing circumstances of businesses. That means also that when a business is successful, the employees share in that success. But the rule has to be - earn it first, spend it later. That is the only way to the high performance/high pay economy that we all want to see. What we do not want is more of what ~~we already see~~ ^{there is still} too much of - the low performance/high pay syndrome which comes from systems which lead with high pay in the hope that performance will follow. Because if it doesn't and the product is therefore not competitive, markets are lost, output cannot be sustained and jobs are lost.
5. Greater adoption of profit-related pay, in which a part - not all, but a part - of employees' pay is linked to the profits of the business they work in, offers a way forward. Employees will then get tangible signals through the pay packet about how their business is really doing. They have a direct share in its success, and a strong incentive to contribute to that success. They see that the survival of the business, and their jobs in it, is that much more secure if conditions are difficult. Industrial relations and pay determination becomes less adversarial. And at the end of the day, there can be more investment, more output, more jobs, more profits and higher standards of living throughout the whole economy, not least for those who are now unemployed.

6. Whether we can move forward in this way is in the hands of employers and employees. For us to use coercion would be counterproductive. It would just lead to more rigidity.

7. But there is something which this ~~hence~~ ^{House} can do to assist the process of change. That is to support the proposals in the Finance Bill for an income tax relief for employees in PRP schemes. That would I believe help more PRP schemes to get off the ground. And that would be a great step towards securing an efficient and effective labour market, and strengthen the economy as we encounter new challenges and new opportunities in the fast moving markets of the world. I hope therefore that our PRP proposal will recieve the full support of this House, and that the new tax relief can soon take its place in the array of measures which we are promoting to improve the supply side of our economy.

KEITH/PAY AND FILE

In this Bill we have taken further important steps to streamline tax administration.

2. Clauses 82 to 91, 95 and Schedule 6 reintroduce the new system of accounting for and paying corporation ~~tax~~ known as Pay and File. This is a further important step in our programme of improvements to the system of corporation tax. In 1984 we initiated radical changes to the structure of the tax, with a phased withdrawal of outdated tax reliefs linked with a staged reduction of tax rates. The new Pay and File system, which follows on from recommendations of the Keith Committee will add an efficient and modern administrative system for collecting the tax. It does away with the present antiquated rules and the inefficient practices which have developed out of them. It replaces those rules with a proper legal framework under which taxpayers will have clear rights and responsibilities. We have consulted widely with the business community which has generally welcomed the new system.

3. Pay and File will mean major changes for the Revenue, the taxpayers and for tax practitioners. It cannot be introduced until 1992, but we are legislating now to allow sufficient time for all those affected - both inside and outside Government - to make the necessary changes to their operating and computer systems.

4. But other parts of the tax system are also in need of modernisation and we shall be looking in future at the scope for this. One of the things we shall be examining is whether the concept of pay and file could be extended in due course to cover individuals, particularly those who are in business. This would not be straightforward, but progress on this front will be helped by the experience gained from introducing pay and file first for companies and corporation tax, and by the Inland Revenue's major programme to install a comprehensive on-line computer system linking all their local offices.

5. The Bill also contains provisions which make a start on modernising the rules relating to the payment over to the Revenue of PAYE tax deducted by employers. Here again we have followed the general route pointed to by the Keith Committee, by introducing an interest charge

in certain special cases where there has been serious delay. And again we shall be considering whether, as the Revenue's computerisation programme progresses, further improvements can be made.

6. At the end of last year the Inland Revenue issued a consultative document on a wide range of other recommendations made by the Keith Committee on ways in which tax administration could be improved. Views on these matters have been invited by the end of October, and we shall be considering them very carefully in the context of our continuing policy of achieving a simpler, more efficient and fairer tax system.

INHERITANCE TAX

Interest in possession trusts

In 1986 we replaced capital transfer tax (CTT) by inheritance tax, and removed an obstacle to lifetime giving of assets by abolishing the immediate tax charge on outright gifts between individuals. These reforms had particularly in mind the transfer of family businesses and family farms, and they were warmly welcomed by the business community.

Last year we concentrated on encouragement of outright giving. We are now extending the same freedom as for outright gifts to gifts between individuals involving interest in possession trusts, while providing due protection for the continuing charge on discretionary trusts. This further increases individual freedom of choice, and like last year's change, this further measure removes a disincentive to the transmission of family businesses and farms, which are often held in trust in the interests of efficient control and management, and orderly succession. It also meets representations received from a wide spectrum of representative interests, professional bodies and individual taxpayers.

Decisions concerning disposal of assets may now be taken with much less need for them to be distorted by fiscal considerations.

Acceptance in lieu of tax

We are also building on various measures introduced in recent years to assist the national heritage by changing the rules relating to acceptance of property in lieu of tax. In future, an offeror will have the choice of either staying with the present system and having the amount of tax satisfied by acceptance in lieu calculated from the value of the item at the time it is accepted with the outstanding tax bearing interest up to that date, or basing the acceptance on the value of the item at an earlier date with interest ceasing to run on that date.

[The Bill fulfills our undertaking to extend to pre-1985 capital transfer tax and estate duty the provision included in the pre-election Finance Act for post-1984 capital transfer tax and inheritance tax.]

omit if some
shortening
required.

This change is designed to encourage acceptances in lieu where owners decide to dispose of heritage property. It meets representations from a number of heritage organisations that the former rules acted as a disincentive because of the mandatory accrual of interest while the purchase negotiations continued. The acceptance in lieu system is a valuable tool in preserving our heritage - Hon. Members will recall that it recently enabled us to acquire Constable's "Stratford Mill" - and we hope that the new optional arrangements will provide further encouragement for the continued future use of the facility.

Sir Brandon Rhys Williams' proposals: force pension schemes to provide better benefits for early leavers and pensioners

Understand hon Friend's continuing concern about this point. He will be well aware that recent Social Security legislation has done much to improve the position for early leavers - greater transferability, revaluation of preserved benefits etc. Our proposals for personal pensions and free-standing AVCs take this further. Do not think it would be right to compel pension schemes to provide benefits at a particular level.

Even if we were persuaded such a sanction would be appropriate, far from clear that it would be proper to impose it through the tax system.

In general, the purpose of the tax rules is to contain the cost of the special reliefs for pensions, and to safeguard against abuse. This is why the rules provide for limits on eg maximum contributions and maximum benefits. Mr hon Friend's proposals would, if implemented through the tax regime, introduce a new condition for approval based on minimum levels of benefit. This new condition would have no relevance to the control of the cost of the tax reliefs or the prevention of abuse.

AVC benefit limits: impossible to police

1. Members of occupational schemes will have a right (under Social Security legislation) to know how much their pension rights are worth and, therefore, what scope there is within the overall benefit limits to pay AVCs. This is a calculation which the scheme managers should carry out under present rules, with 'in-scheme' AVCs, in order to guard against excessive contributions. For free-standing AVCs they will have to make the same calculation, and this information will be conveyed by the scheme member to the AVC provider. When benefits are payable, the scheme member will have to inform his employer's scheme of any AVC benefits, so that his overall entitlement from all schemes can be determined, and any necessary adjustments made to main scheme benefits.

2. If, on the other hand, the benefit limits were disapplied, it would be possible for someone in a non-contributory occupational scheme to invest up to 15 per cent of salary in a free-standing AVC scheme and increase his total pension benefits way beyond the two-thirds final salary maximum under existing rules. This would increase enormously the cost of the already very generous tax reliefs for pensions, and the scope for abuse. The pensions tax reliefs were never intended simply to provide a tax shelter for investment generally.

TAX REFORM AND THE FINANCE BILL

With this Bill we are pressing ahead with the programme of tax reform which we have followed consistently since 1979. The importance of tax reform and tax reduction to the health and vigour of the economy is now a matter of international consensus. Lower rates of tax sharpen incentives and stimulate enterprise: ~~the~~ the only route to better economic performance. Lower tax rates are part and parcel of the kind of society we want to see where individuals are allowed to keep more of their own money, to spend or save as they wish with the responsibilities that came with that freedom.

The record is clear. Personal tax rates are down: the basic rate from 33 per cent to 27 per cent and top rates from the absurd level of 98 per cent to 60 per cent. Thresholds are up by 22 per cent in real terms, so that almost 1½ million people pay no tax who would otherwise have had to. Four damaging taxes have been abolished completely. The burden of capital taxes has been reduced, particularly inheritance tax on the smaller estates where the family home is the principle asset. Stamp duty on shares has been cut twice. But taxes are still too high. There is no room for complacency about the level of tax paid by the less well off. We cannot be satisfied that a nurse earning £170 per week pays nearly 27 per cent in tax and NICs. That is why we are determined to cut the basic rate still further as soon as we can prudently do so.

Our business tax reforms have lead a world-wide trend to cut rates and reduce tax induced distortions, reducing the corporation tax rate to what is still, at 35 per cent, one of the very lowest in the industrialised world. We have cut the small companies' rate from 38 per cent to 27 per cent. The changes we have made are helping to bring about a radical change in the environment in which companies operate. We now have a system which rewards enterprise by allowing companies to retain more of the profits they have made to spend as they wish; rather than the self-defeating system we replaced, which gave tax subsidies

to encourage investment but then taxed away the incentive to invest profitably.

We have not just reduced the rate of most direct taxes. We have taken steps to reform and simplify the tax system, reducing the cost of compliance. The Finance Act passed immediately before the election introduced an important package of measures designed to reduce the burden on small businesses of administering VAT.

The measures in this Bill keep up this momentum of reform. For businesses a valuable set of measures to streamline and simplify the system of tax collection, lighten the administrative burden and promote fair competition, as well as the opportunity to participate in the new profit-related pay scheme. For individuals an innovative personal pensions scheme which will offer new freedom of choice and flexibility to all employees and self-employed people in this country. We have introduced this Bill quickly because we are anxious to see these vital measures on the Statute Book as soon as possible.

FROM: MISS C EVANS
DATE: 3 July 1987

MISS RUTTER

cc **Chancellor**
Financial Secretary
Paymaster General
Economic Secretary
Sir Peter Middleton
Mr Scholar
Miss Sinclair
Mr Cropper
Mr Tyrie

Mr Spence - IR
Mr Walker

Ms French - C&E

FINANCE BILL SECOND READING

Mr Bradley - page 4 only.

I attach a revised contribution to the ^{opening} speech covering the non PRP and pensions clauses. The section on Lloyd's is being submitted separately. As requested I have grouped these as follows:

- i) unchanged clauses
- ii) amendments to the pre Election Bill (this section also includes the amendments to the 1987 Act)
- iii) new measures

2. As discussed I also attach a revise of the section on PRP.

- 1. *Tony*
- 2. *C*

*You may like to look at: the
- CGT streamlining (p 2)*

CE

MISS C EVANS

UNCHANGED CLAUSES

Most of the remaining clauses re-enact the same measures as those in the pre Election Bill. I will mention only briefly the points which are unchanged and then outline the amendments we have made. The largest remaining group of clauses deals with the new Pay and File system. This will put in place efficient, modern arrangements for collecting corporation tax which will, after the introductory period, reduce significantly the administrative burden on companies. This is a further important step in our programme to simplify and rationalise the system of corporation tax. It has been generally welcomed by the business community. Pay and File will mean some quite major changes, but it will not start in full before 1992. The purpose of legislating now is to give all concerned time to make the necessary changes to their operating and computer systems.

Clauses 74 to 81 provide for companies' capital gains to be taxed at normal corporation tax rates thus removing the complicated adjustment needed under present arrangements. This will have the effect of reducing the rate of tax on gains for small companies from 30 to 27 per cent. The Bill also reintroduces the group of measures designed to remove unintended or unjustified tax reliefs and thus ensure that businesses compete on more equal terms. There are two broadly unchanged clauses on inheritance tax which round off the changes already enacted and include the measure to exempt lifetime transfers by individuals into and out of interest in possession trusts.

CHANGES FROM THE PRE-ELECTION BILL

The House will be particularly interested in the changes to the remaining clauses which we have made in response to representations received about the pre-Election Bill. The most important is contained in Clause 70, which deals with Lloyd's reinsurance to close provisions.

Lloyd's

[Mr Spence to provide.]

Capital gains streamlining

We ^{have} also introduced an important modification to the Bill's provisions on the taxation of companies' capital gains. We ~~have~~ received a number of representations from inside and outside this House about the impact of this change on the life assurance industry. We considered these very carefully and concluded that the time has come to take a general look at the tax arrangements for life assurance as they have now developed. There will be a full opportunity for the life assurance industry and other interested parties to contribute to the review. In the meantime we have decided that the tax rate on gains earned for policy holders should remain at 30 per cent, pending the outcome of the review.

Other amendments in response to representations

I shall now outline briefly the remaining amendments we have made in response to representations about the pre Election Bill. We have made a number of improvements to the Pay and File provisions, for example, to ensure that the accounts which companies have to provide to the Revenue are no more detailed than those which they already prepare under the Companies Act. We received a number of representations from the banks about Clauses 67 and 68 concerning double taxation relief on interest on certain overseas loans. In the light of these we have decided to double the length of the transitional period before the new provision takes effect for loans which were already in existence on 1 April this year.

Technical amendments to 1987 Finance Act

The remaining changes to the Bill are mainly technical amendments to the Finance Act passed before the Election, as well as a few new measures. First, I shall mention briefly the amendments to the Finance Act. Clause 97 fulfills our undertaking to extend the inheritance tax interest waiver facility created by Section 60 of the Act to estate duty and pre-1985 capital transfer tax. Clause 101 and Schedule 8 make technical amendments to the oil taxation provisions in Sections 61-63 of the Finance Act. They include a measure to counter arrangements to circumvent the petroleum revenue tax nomination scheme. This will take effect only when brought in by Treasury order if evidence of actual abuse becomes apparent. Clause 59, dealing with employee share schemes, will clarify the 1987 Act to prevent an unintended capital gains tax liability arising when options in a company subject to takeover are exchanged for options in the new company. Clauses 99 and 100 make minor changes to the stamp duty clauses in the Act: Clause 99 deals with exemptions for options in respect of gilts and other exempt securities and Clause 100 introduces the special rules for public issues which we announced on 8 May.

NEW MEASURES .

Finally there are four new measures which I should mention to the House. Clause 71 is designed to prevent a possible loophole in relation to capital losses on Building Society share accounts.

Clause 80, which deals with oil taxation, gives effect to the undertaking we gave shortly before the Election to introduce legislation to make it clear that capital gains 'rollover relief' is not available for gains on the disposal of interests in oil licences.

Clause 103 will provide a new relief which will benefit factory ships processing fish in UK ports. It will allow goods such as food and fuel oil, imported as stores for ships engaged on international voyages to be relieved from duty when used in port. Without this relief there is a risk that these ships which provide a significant market for UK and Scottish Fishermen, would stop using British ports. Clause 102 clarifies and supports existing legislation in relation to fees and charges ~~to~~^{for} services and facilities provided by Government Departments. It enables Ministers to extend by Order the range of functions and costs which they may take into account in setting such charges and enables them to specify the costs to be recovered.

PROFIT RELATED PAY

Clauses 1 to 17 introduce the scheme for tax relief for profit related pay. I believe that this scheme offers a major opportunity to British industry. It forms a new and imaginative element in our strategy to improve the supply-side of the economy, by helping the labour market to work better.

PRP builds on success. A number of firms already have cash based profit sharing schemes, and find them valuable. For the employer it can mean a more committed workforce, with better incentives to profitability and productivity. It can mean that if times are difficult, and profits fall, part of the strain can be taken by a temporary fall in pay, perhaps instead of redundancies. That extra flexibility can help to make output more secure, which in turn can mean more certainty and less caution about hiring extra labour to increase output when prospects look good.

For the employee, it means a direct stake in the business's success, higher pay if that has been earned by higher profits, and greater job security if business conditions are difficult. And of course a very valuable tax relief.

For the whole economy, a broad spread of PRP schemes could mean higher productivity, output and employment from which everyone stands to gain, not least those who are at present unemployed.

For the tax relief to be given it will be necessary for schemes to meet certain basic statutory requirements and to be registered with the Inland Revenue before the start of their first profit period. We have aimed to keep the criteria for registration as simple and flexible as possible. We have taken full account of responses to the Green Paper we published a year ago and technical discussions with employers and other interested bodies.

The provisions on profit related pay follow very closely those in the earlier Bill. But we have incorporated in this Bill the Government Amendments which were put down on this subject for the last Bill, and we have also made other minor detailed changes

and improvements in response to representations.

These clauses thus represent over a year's detailed consultations with practioners of all sorts, as well as reflecting representations from academics and members of the general public. We believe we have struck the right balance between the regulation which is necessary with any tax relief, and flexibility for employers to tailor schemes to the particular circumstances of their businesses. And keeping registration arrangements simple should help, in particular unincorporated businesses, who will be able to benefit from PRP in ^athe way that they cannot benefit from share schemes.

I hope it will be widely appreciated how very valuable the income tax relief will be. For a man on average earnings with 20 per cent of his pay as PRP, the maximum eligible for tax relief, it would be equivalent to 4 pence off the basic rate of income tax. These provisions will thus give employers a very useful and practical tool to help them introduce PRP.

PRP is a very important strand in our policies to improve the ways in which the labour market works. It is also part of a successful approach to management. I hope that all managers will give it very serious consideration. It is not too soon now to be thinking about how to introduce a scheme which will qualify for the tax relief.

That is why I am so encouraged that already over [20,000] employers have contacted the Inland Revenue to establish their interest in the details of these proposals, and to order copies of the Guidance Notes which will be published later this year. And that is why I hope the whole House will want to see this measure on the Statute Book as soon as possible.



Inland Revenue

Policy Division
Somerset House

Andrew

FROM: N C MUNRO

6 July 1987

Chief Secretary

FINANCE BILL SECOND READING DEBATE: PENSIONS

1. I attach a revised draft of your speech on pensions, in the light of this afternoon's meeting, together with a few defensive notes.
2. In an effort to shorten it and to improve the flow I have removed the reference to the Chancellor's 1985 'promise' and simplified the passage on personal pension contributions.
3. I also attach the factual briefing notes you requested on the benefit limits and lump sums.

Rem.

N C MUNRO

cc **Chancellor of the Exchequer**
Financial Secretary
Paymaster General
Economic Secretary
Mr Cassell
Miss O'Mara
Mr Culpin
Mr Hudson
Miss Evans
Mr Cropper
Mr Tyrie

Mr Isaac
Mr Beighton
Mr Corlett
Mr Johns
Mr Munro
Mr Walker
PS/IR

PENSIONS

I should like to turn now to the largest group of clauses in the Bill clauses 18 to 57 - which contain important and far-reaching changes for private pensions. Again the legislation is substantially the same as that proposed in April although it has in some places been amended to repair certain technical faults. Our proposals have two main objectives: firstly to widen individual choice and to encourage job mobility and, secondly, to ensure a fairer deal for the taxpayer.

Widening the pension choice

I suspect there will be general agreement that it is desirable to widen the coverage of private pension provision. Much has already been done. Many employers have established occupational pension schemes for their staff, with the help of generous tax reliefs. At present, over 10 million people are currently members of occupational schemes of which all but about a million are contracted-out of the Additional Component of the State Scheme. Moreover, to make entirely clear the scale of private pension provision, I should add that an increasing number of people - currently 5 million - are already receiving pensions from occupational schemes. And, as the FES revealed vividly recently, there has been a steady improvement in the average real income of pensioner households over recent years.

But more can be done. There are still some 10 million employees who are not in an occupational scheme and who make no private provision for retirement. A central feature of our strategy is to bring private pensions within the reach of these employees for two reasons: to provide them with a pension of their own and to increase their independence of the State.

Personal pension schemes

We propose to do this through the new personal pensions which will be available to all employees who are not in an occupational

scheme; to the minority of employees who choose to opt out of their occupational scheme; and to the self-employed.

Clauses 18 to 57, and Schedule 2, of the Bill introduce the tax regime for these schemes, which will be available from next January. The legislation has no novel ingredients but is based on the present, broadly similar, retirement annuities provisions enacted over thirty years ago. In addition to being brought up to date, the new measures also incorporate a number of new features which have been widely welcomed. The 1986 Social Security Act enables employees to contract-out of the Additional Component of the State Scheme through a personal pensions. Clause 42 provides the necessary tax procedures to achieve this result.

We propose other improvements in the rules, in order to make personal pensions more attractive. In particular, we shall allow people to have more than one personal pension plan, which will enable risks to be spread, and choice to be greater. The amount of contributions will be limited, but there will be no limit on the benefits which such schemes can provide.

Wider range of providers

In addition, Clause 20 enables a much wider range of pension providers to establish personal pension schemes. As well as insurance companies and certain friendly societies, at present, the field will be open to banks, building societies and unit trusts. And, in response to representations, all registered friendly societies - not just those with income above a certain level - will be able to offer such schemes.

Additional voluntary contributions

The House will also be aware that the Bill also contains provision to allow members of occupational schemes to make additional voluntary contributions to a pension plan completely separate from their employer's scheme, up to the tax approval limits on contributions and benefits. This development has been widely

welcomed and, taken together with the other changes, will dramatically increase the choice of how to provide for retirement.

Job Mobility

A further purpose of our reforms is to remove - as far as possible - the pension obstacles to job mobility. The House will be well aware of the 'early leaver' problem: the person who changes jobs in mid-career and whose pension expectations are in consequence much reduced. There is no quick and easy solution to this problem. But the very existence of the new pension opportunities I have just described will have the additional advantage of greatly reducing its worst impact. Personal pensions and 'free-standing AVCs' schemes - together with much greater transferability of pension rights - will mean that, when someone changes his job, he will be able to take some or all of his pension with him.

The changes we have proposed do not increase the already generous tax regime for retirement provision, but simply extend it potentially to every employee. I believe these reforms will greatly improve the pension position and the freedom of choice of all employed and self-employed people in this country.

Exploitation of tax reliefs for pensions

But the improvements we propose can be justified only if the tax reliefs for pensions are not abused. We have felt it necessary to impose some limited restrictions, to guard against misuse of the tax reliefs - particularly by a small number of very high earners. The legislation is contained in Schedule 3. The tax rules for pensions were never intended simply as a tax-sheltered medium for investment generally - with scope for the postponement (and for lump sums, complete elimination) for a tax liability.

These restrictions will have no impact whatever on the vast majority of pension scheme members: for ordinary working people the scope for abuse has never been available. But for a few

highly paid people, the new rules will ensure that the tax reliefs are used only for their originally intended purpose.

I have seen suggestions that these changes will restrict job mobility, particularly among senior executives. I understand the argument, although this would generally be only one of the many factors which influence the decision to move.

In response to representations, however, we have amended our proposals in one important respect. We originally proposed that new members of occupational schemes should be permitted to have maximum lump sum benefits after as little as twenty years only if they obtained maximum pension benefits after the same period. In all other cases, maximum lump sums could only be obtained after 40 years.

It was put to us that this was somewhat harsh on an individual with less than 40 years service whose pension was boosted, but not completely up to the maximum possible. In such cases, it was argued, it should be possible for the lump sum to be boosted to the same extent. We accepted this point, and the legislation in Schedule 3 has been amended accordingly.

The measures I have outlined comprise some of the main changes in a continuing process of pensions reform which was initiated by my Rt Hon Friend, the previous Secretary of State for Social Services over three years ago. The proposals in this current Finance Bill build on, and extend, the changes made in recent Social Security legislation, and provide a better pensions deal for millions of employees - and the self-employed - in this country.

DEFENSIVE NOTE

AVC benefit limits: impossible to police

Members of occupational schemes will have a right (under Social Security legislation) to know how much their pension rights are worth and, therefore, what scope there is within the overall benefit limits to pay AVCs. This is a calculation which the scheme managers should carry out under present rules, with 'in-scheme' AVCs, in order to guard against excessive contributions. For free-standing AVCs they will have to make the same calculation, and this information will be conveyed by the scheme member to the AVC provider.

When benefits are payable, the scheme member will have to inform his employer's scheme of any AVC benefits, so that his overall entitlement from all schemes can be determined, and any necessary adjustments made to main scheme benefit.

FOR [If, on the other hand, the benefit limits were disapplied, it
USE would be possible for someone in a non-contributory occupational
IF scheme to invest up to 15 per cent of salary in a free-standing
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reliefs were never intended simply to provide a tax shelter for
investment generally.]

DEFENSIVE NOTE

Sir Brandon Rhys Williams' proposals: force pension schemes to provide better benefits for early leavers and pensioners

Understand hon Friend's continuing concern about this point. He will be well aware that recent Social Security legislation has done much to improve the position for early leavers - greater transferability, revaluation of preserved benefits etc. Our proposals for personal pensions and free-standing AVCs take this further. Do not think it would be right to compel pension schemes to provide benefits at a particular level.

Even if we were persuaded such a sanction would be appropriate, far from clear that it would be proper to impose it through the tax system.

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condition for approval based on minimum levels of benefit. This
new condition would have no relevance to the control of the cost
of the tax reliefs or the prevention of abuse.]

DEFENSIVE NOTE

Anti-exploitation provisions will inhibit job mobility

This overlooks the fact that, if an individual qualifies for maximum benefits after as little as ten years service, any 'retained benefits' from earlier employments must be taken into account. And ~~they~~^{it} ignores the effect of the overall reforms package on this problem. In particular, the introduction of personal pensions and free-standing additional voluntary contributions and the lifting of the restrictions on transferability (together with the DHSS changes on the revaluation of deferred pension rights) will greatly ease the present pensions barriers to labour mobility.

TAX TREATMENT OF PROVISION FOR RETIREMENT

Present position

Two types of pension provision:

- a. occupational pension schemes
- b. retirement annuities.

Occupational pension schemes

Established by employer. Tax rules in 1970 Finance Act - minimum of statutory rules, with extensive Revenue discretionary powers to approve schemes.

Benefits limited by reference to final salary (even if scheme provides money purchase benefits):

- total pension benefit may not normally exceed $\frac{1}{60}$ final salary for each year of service up to 40 (hence 'two thirds' final salary limit)
- lump sum (usually by commutation of pension) may not exceed $\frac{3}{80}$ final salary for each year of service up to 40 (hence 1.5 final salary limit)

But accelerated accrual (or 'uplift') permits:

- 'two thirds' final salary pension after 10 years service to retirement
- 1.5 final salary lump sum after 20 years service to retirement

Contributions limited:

- employee contributions (if paid) may not exceed 15 per cent salary. Average level of basic contributions required ~~but by~~ schemes generally 4-5 per cent. Additional voluntary contributions (AVCs) may be paid on top of basic: but cannot breach 15 per cent and should not result in excessive benefits.
- employer contributions: ~~not~~ fixed limit, but should not produce excessive benefits.

Retirement annuities

Taken out by individual (self-employed or unpensioned employee).
Tax rules in Section 226 et seq 1970 Taxes Act.

Benefits not limited: based on money purchase. But lump sum cannot exceed three times residual annuity.

Contributions limited:

- 17.5 per cent income if born after 1933
- higher limits (up to 24 per cent) ^{FN}older.

Personal pension schemes

Based on retirement annuities, but with improvements:

- scope for employer contributions (within overall limits)
- for employees, can be contracted-out of SERPS
- for employees, tax relief at source on contributions
- wider range of providers
- different lump sum rule (25 per cent of the individual's fund)

PENSIONS PACKAGE: ANTI-EXPLOITATION MEASURES

The problem

Tax reliefs for pensions exploited in number of ways (in particular, by high earners):

i. Accelerated accrual of total benefits

Provision of maximum 'two thirds' final salary pension after as little as ten years service very costly (often requiring annual employer contributions of 150 per cent payroll). Such contributions ~~tax-deductible~~.

ii. Accelerated accrual of lump sums

Maximum lump sum by commutation after 20 years possible even if pension benefit only at basic level: scope for maximising tax-free lump sum at expense of taxable pension.

iii. Final remuneration

Amount of final salary for calculation under i. and/or ii. could be inflated with eg very large share option payment.

iv. Lump sums

The maximum lump sum of 1.5 final salary is over-generous given the level of salaries now being paid eg in the City.

This year's proposals

In order to deal with these problems:

- i. The accelerated accrual rules are to be changed to permit maximum pension benefits only after twenty years service.
- ii. Accelerated accrual for lump sums only possible if (and to the extent that) accelerated accrual applies for total pension benefits.
- iii. 'Final remuneration' redefined to exclude payments from share options; and tighter definition for higher (+ £100,000) earners.
- iv. Lump sum limit of £150,000.

Changes at i., ii., and iv. apply only to new pension schemes set up on or after 17 March 1987 or new members joining existing schemes after that date. Change in 'final remuneration' does not catch share option arrangements entered into before that date.

Additional voluntary contributions (AVCs)

With effect from 7 April 1987, benefits secured by AVCs - whether 'in-scheme' or 'free-standing'-not commutable. People affected, even if rate of AVCs subsequently increased.

already paying
AVCs not

TGS
Andrew

FROM: P R C GRAY

DATE: 6 JULY 1987

CHIEF SECRETARY

cc Chancellor
FST
PMG
EST
Sir P Middleton
Mr Monck
Mr Scholar
Miss C Evans
Mr Guy
Mr Farmer - IR

FINANCE BILL SECOND READING - PRP

Following our talk earlier this afternoon, I attach a re-casting of the material on PRP for your speech.

2. I have been somewhat less forthcoming than you were envisaging about the rate at which the number of firms operating PRP schemes has been growing the recent past. We don't at present have data on PRP schemes, so we have no firm basis on which to base any assertions.

3. We are checking overnight with the PRP Office on the latest number of enquiries from employers, and will advise you in the morning if there is any advance on "over 20,000".

RCC

P R C GRAY

The Bill before us this afternoon contains a number of important matters, to which I turn without delay.

Clauses 1 to 17 introduce our proposals for tax relief for profit related pay. The detailed provisions follow very closely those in the earlier Bill. But we have incorporated the Government Amendments which were put down on this subject before the Election, and we have also made other minor detailed changes and improvements in response to representations.

These PRP proposals represent a major initiative. They form an important and imaginative element in the Government's overall strategy to improve the supply performance of the economy. The working of the labour market is one of the areas of greatest remaining weakness in this country. Its rigidities are a major obstacle to the continued strengthening of our economic performance. All too often the labour market has been dominated by the outdated and debilitating concept of "them and us".

PRP has a key role to play in tackling that obstacle. It underlines the shared common interest in building better and stronger businesses.

In recent years there has been a rising interest in profit sharing of all types. There has been a growing take-up of schemes for employees to acquire shares in the companies in which they work, no doubt stimulated by the tax incentives introduced for schemes of that sort.

But there has also been a developing interest in cash-based profit sharing. That is what we now call profit related pay, an arrangement where a part of employees' pay is linked to the profit record of the business. Hitherto there have been no specific tax incentives for this type of profit sharing.

But the benefits PRP can bring are valuable and far-reaching - probably more so than for share-based schemes. Employers, employees and the economy at large all stand to gain from its wider spread.

For the employer it means a more committed work force, with better incentives to profitability and productivity. It means that if times are difficult, and profits fall, part of the strain can be taken by a temporary fall in pay, perhaps instead of redundancies. That extra flexibility helps to make output more secure - and in turn means more certainty and less caution about hiring extra labour to increase output when prospects look good. In short, PRP is part of successful management.

For the employee, PRP means a direct stake in business success. It means higher pay if that has been earned by higher profits. And if business conditions are difficult it means greater job security.

And the proposed tax relief can be very valuable. For a man on average earnings with 20 per cent of his pay as PRP - the maximum that will be eligible for tax relief - it is equivalent to 4 pence off the basic rate of income tax. Not only is this of major benefit to employees; it provides employers with a very useful and practical tool to help them introduce PRP.

And the benefits are not limited just to the businesses in which PRP schemes are introduced. The whole economy gains. Because a broad spread of PRP schemes means higher productivity, output and employment from which everyone stands to benefit - not least those who are at present unemployed.

Even without the benefit of tax relief, a number of firms have already seen the value of PRP, and have introduced their own schemes. It is clear that they have found them valuable. The proposals in this bill provide a major incentive to employers and employees to build on that success.

The detailed provisions in the Bill represent over a year's detailed consultations with practitioners of all sorts, as well as reflecting representations from academics and members of the public. Before tax relief can be given, it will be necessary for PRP schemes to meet certain basic statutory requirements, and to be registered with the Inland Revenue in advance of their first profit period. We believe we have struck the right balance between the regulation which is necessary with any tax relief, and flexibility for employers to tailor schemes to the particular circumstances of their businesses. We have aimed to keep the criteria for registration as simple and flexible as possible. This should help in particular smaller and unincorporated businesses, who will be able to benefit from PRP in the way that they cannot benefit from share-based schemes.

It is clear from what I have said that PRP offers a major opportunity further to strengthen our economic performance. I would urge all employers

and managers who are not already doing so to be thinking now about how to introduce a scheme which will qualify for the tax relief. I am greatly encouraged that already over 20,000 employers have contacted the Inland Revenue to establish their interest in the details of these proposals, and to order copies of the guidance notes which will be published later this year. I hope therefore that the whole House will want to see this measure on the Statute Book as soon as possible.



FROM: J J HEYWOOD
DATE: 7 July 1987

MR GRICE

cc PS/Chancellor / 2
Sir P Middleton
Mr Peretz
Mr Culpin
Miss O'Mara

FINANCIAL SECRETARY'S WIND-UP SPEECH: 8 JULY

1. The Financial Secretary understands that Leon Brittan is intending to speak on the economy during the Second Reading Debate on the Finance Bill tomorrow afternoon.

2. The Financial Secretary thinks that Mr Brittan will concentrate mainly on monetary policy. He would like defensive speaking notes on:

(i) Is the money supply growing too quickly?

(ii) Is inflation likely to rise over the medium term?

(iii) Is there a credit boom?

3. The Financial Secretary will only use these notes if he has to.

Quite. Not the time to say anything new on monetary policy.

J.H.

JEREMY HEYWOOD
Private Secretary

CONFIDENTIAL

From : Caryl's even
Date : 7 July



MISS RUTTER

cc PPS
PS/FST
PS/PMG
PS/EST
Mr Scholar
Mr Cayley

FINANCE BILL SECOND READING
COMPANIES' CAPITAL GAINS

As requested I attach a defensive speaking
note which I have cleared with Mr
Cayley.

Ca

C.

One part of this draft seems
over-defensive to me, so I have
suggested a redraft.

AMH

DEFENSIVE SPEAKING NOTE ON LIFE ASSURANCE
COMPANIES' CAPITAL GAINS

WHY HAS GOVERNMENT CHANGED ITS MIND - IS
THIS A CLIMBDOWN?

This is not a climb down at all. It was put to us that the proposed change would impact unfairly on the life assurance industry and undermine its competitive position. We are by no means persuaded by these arguments. ~~But some people in the industry suggested that the time has come to take a general look at its tax position and we have decided to pursue this. In the meantime it seems right to maintain the present tax rate on policy holders' gains. The review we propose will consider the overall level of tax on the companies concerned, its distribution between different companies and types of businesses and look at the scope for simplification. It will take account of the position of individual policy holders as well as of companies. As I have said, the review will be conducted with all due speed and all interested parties will have a full opportunity to comment.~~

But we have decided that it would be appropriate to take a wider look at the industry's tax position, and, in the meantime,



MR SCHOLAR

cc PPS

PS/FST

PS/PMG

PS/EST

Mr Cassell

Miss Sinclair

Miss O'Mara

PS/IR - by fax pl copy to

Mr Spence - IR

Mr Munro - IR

Mr Culpin

Mr Tynie

Ms GC Evans

Mr Gray

Mr Monck

SECOND READING

I attach the - new - final draft of the Chief Secretary's speech. I would be grateful for essential comments only by 1.00 p.m. if possible. The pensions and Lloyds material are unamended.*

The speech lacks a peroration, which the Chief Secretary will write on return from E(LA). The page in square brackets is likely to be dropped.

Sinclair

8. 7. 87

* Though Lloyds has been retyped.

THE RT HON JOHN MAJOR MP
OPENING SPEECH FOR SECOND READING OF THE FINANCE BILL
ON WEDNESDAY 8 JULY 1987

I beg to move, that the Bill be now read a second time.

As the House will recall many of the measures announced in my RHF's Budget in March were approved in the Finance Bill passed by the House before the General Election. These included the 2p reduction in the basic rate of income tax and in the small companies' corporation tax; extra help for the blind and the elderly; a package of measures to help small businesses with their VAT liabilities; and further reforms of inheritance tax. All these were welcome measures to the majority of H Ms.

The Bill before us today completes the proposals contained in my RHF's Budget. Both that Budget and the two consequential Finance Bills have been set against the most favourable economic circumstances we have seen in this country for many years. It is a background of steady and sustained growth, of low inflation; and of falling unemployment. It is also a background which has enabled my RHF in one year to cut taxes; to cut borrowing; and at the same time, to increase resources for priority services by £4¼ billion. That combination of events represents a remarkable tribute to my RHF's stewardship of our national accounts.

However, I am conscious that the House debated the state of the economy, and the latest economic indicators, only last Thursday and I shall deny myself the pleasure of re-opening that debate, enticing though the prospect may be.

The Bill before us this afternoon contains a number of important matters, to which I wish to turn without delay.

Profit-Related Pay

Clauses 1 to 17 re-introduce our proposals for tax relief for profit related pay. The detailed provisions follow very closely those in the earlier Bill although we have taken the opportunity to incorporate the Government Amendments which were put down on this subject before the Election. We have also made other minor detailed changes and improvements in response to representations.

Essentially, however these proposals are the same and they represent a significant initiative. They form an important - and imaginative - element in our strategy to improve the supply performance of the economy. The working of the labour market is one of the areas of greatest remaining weakness in this country. Its rigidities are well known and they are a major obstacle to the continued strengthening of our economic performance. And all too often the labour market has been dominated by the outdated concept of "them and us".

PRP can play an important part in tackling that obstacle because it underlines the shared common interest in building better and stronger businesses.

In recent years there has been a rising interest in profit sharing of all types. There has been a growing take-up of schemes for employees to acquire shares in the companies in which they work, and I have little doubt that the take up has been stimulated by the tax incentives available.

But at the same time there has also been a developing interest in cash-based profit sharing. That is what we now call profit related pay, an arrangement where a part of employees' pay is linked to the profit record of the business. Hitherto there have been no specific tax incentives for this type of profit sharing but this Finance Bill remedies that omission.

It does so because the benefits PRP can bring are valuable and far-reaching - probably more so than for share-based schemes. Employers, employees and the economy at large all stand to gain from its wider spread.

For the employer it means a more committed work force, with better incentives to profitability and productivity. It means that if times are difficult, and profits fall, part of the strain can be taken by a temporary fall in pay, perhaps instead of redundancies. That extra flexibility helps to make output more secure - and it means - something else too: it means more certainty and less caution about hiring extra labour to increase output when prospects look good. In short, PRP is part of successful management.

Nor are the benefits/^{simply}for the employer. For the employee, PRP means a direct stake in business success. It means higher pay if that has been earned by higher profits. And if business conditions are difficult it means greater job security.

And the proposed tax relief can be very valuable. For a man on average earnings with 20 per cent of his pay as PRP - the maximum that will be eligible for tax relief - it is equivalent to 4 pence off the basic rate of income tax. Not only is this of major benefit to employees; it provides employers with a very useful and practical tool to help them introduce PRP.

And the benefits are not limited just to the businesses in which PRP schemes are introduced. The whole economy gains. Because a broad spread of PRP schemes means higher productivity, higher output and employment from which everyone stands to benefit - not least those who are at present unemployed.

[Even without the benefit of tax relief, a number of firms have already seen the value of PRP, and have introduced their own schemes. It is clear that they have found them valuable. The proposals in this bill provide a major incentive to employers and employees to build on that success.]

The detailed provisions in the Bill represent over a year's consultation. Before tax relief can be given, it will be necessary for PRP schemes to meet certain basic statutory requirements, and to be registered with the Inland Revenue in advance of their first profit period. We believe we have struck the right balance between the regulation which is necessary with any tax relief, and flexibility for employers to tailor schemes to the particular circumstances of their businesses. We have aimed to keep the criteria for registration as simple and flexible as possible. This should help in particular smaller and unincorporated businesses, who will be able to benefit from PRP in the way that they cannot benefit from share-based schemes.

It is clear from what I have said that PRP offers a major opportunity further to strengthen our economic performance. I hope that all employers and managers who are not already doing so will

think now about how to introduce a scheme which will qualify for the tax relief. I am greatly encouraged that already over 20,000 employers have contacted the Inland Revenue to establish their interest in the details of these proposals, and to order copies of the guidance notes which will be published later this year. I hope therefore that the whole House will want to see this measure on the Statute Book as soon as possible.

PENSIONS

I should like to turn now to the largest group of clauses in the Bill clauses 18 to 57 - which contain important and far-reaching changes for private pensions. Again the legislation is substantially the same as that proposed in April although it has ~~in some places~~ been amended to repair certain technical faults. Our proposals have two main objectives: firstly to widen individual choice and to encourage job mobility and, secondly, to ensure a fairer deal for the taxpayer.

Widening the pension choice

I suspect there will be general agreement that it is desirable to widen the coverage of private pension provisions. Much has already been done. Many employers have established occupational pension schemes for their staff, with the help of generous tax reliefs. At present, over 10 million people are currently members of occupational schemes of which all but about a million are contracted-out of the Additional Component of the State Scheme. Moreover, to make entirely clear the scale of private pension provision, I should add that an increasing number of people - currently 5 million - are already receiving pensions from occupational schemes. And, as the FES revealed vividly recently, there has been a steady improvement in the average real income of pensioner households over recent years.

But more can be done. There are still some 10 million employees who are not in an occupational scheme and who make no private provision for retirement. A central feature of our strategy is to bring private pensions within the reach of these employees for two reasons: to provide them with a pension of their own and to increase their independence of the State.

Personal pension schemes

We propose to do this through the new personal pensions which will be available to all employees who are not in an occupational

scheme; to the minority of employees who choose to opt out of their occupational scheme; and to the self-employed.

Clauses 18 to 57, and Schedule 2, of the Bill introduce the tax regime for these schemes, which will be available from next January. The legislation has no novel ingredients but is based on the present, broadly similar, retirement annuities provisions enacted over thirty years ago. In addition to being brought up to date, the new measures also incorporate a number of new features which have been widely welcomed. The 1986 Social Security Act enables employees to contract-out of the Additional Component of the State Scheme through a personal pensions. Clause 42 provides the necessary tax procedures to achieve this result.

We propose other improvements in the rules, in order to make personal pensions more attractive. In particular, we shall allow people to have more than one personal pension plan, which will enable risks to be spread, and choice to be greater. The amount of contributions will be limited, but there will be no limit on the benefits which such schemes can provide.

Wider range of providers

In addition, Clause 20 enables a much wider range of pension providers to establish personal pension schemes. As well as insurance companies and certain friendly societies, ~~at present~~, the field ^{in future} will be open to banks, building societies and unit trusts. And, in response to representations, all registered friendly societies - not just those with income above a certain level - will be able to offer such schemes.

Additional voluntary contributions

The House will also be aware that the Bill also contains provision to allow members of occupational schemes to make additional voluntary contributions to a pension plan completely separate from their employer's scheme, up to the tax approval limits on contributions and benefits. This development has been widely

welcomed and, taken together with the other changes, will dramatically increase the choice of how to provide for retirement.

Job Mobility

A further purpose of our reforms is to remove - as far as possible - the pension obstacles to job mobility. The House will be well aware of the 'early leaver' problem: the person who changes jobs in mid-career and whose pension expectations are in consequence much reduced. There is no quick and easy solution to this problem. But the very existence of the new pension opportunities I have just described will have the additional advantage of greatly reducing its worst impact. Personal pensions and 'free-standing AVCs' schemes - together with much greater transferability of pension rights - will mean that, when someone changes his job, he will be able to take some or all of his pension with him.

The changes we have proposed do not increase the already generous tax regime for retirement provision, but simply extend it potentially to every employee. I believe these reforms will greatly improve the pension position and the freedom of choice of all employed and self-employed people in this country.

Exploitation of tax reliefs for pensions

But the improvements we propose can be justified only if the tax reliefs for pensions are not abused. We have felt it necessary to impose some limited restrictions, to guard against misuse of the tax reliefs - particularly by a small number of very high earners. The legislation is contained in Schedule 3. The tax rules for pensions were never intended simply as a tax-sheltered medium for investment generally - with scope for the postponement (and for lump sums, complete elimination) for a tax liability.

These restrictions will have no impact whatever on the vast majority of pension scheme members: for ordinary working people the scope for abuse has never been available. But for a few

highly paid people, the new rules will ensure that the tax reliefs are used only for their originally intended purpose.

I have seen suggestions that these changes will restrict job mobility, particularly among senior executives. I understand the argument, although this would generally be only one of the many factors which influence the decision to move.

In response to representations, however, we have amended our proposals in one important respect. We originally proposed that new members of occupational schemes should be permitted to have maximum lump sum benefits after as little as twenty years only if they obtained maximum pension benefits after the same period. In all other cases, maximum lump sums could only be obtained after 40 years.

It was put to us that this was somewhat harsh on an individual with less than 40 years service whose pension was boosted, but not completely up to the maximum possible. In such cases, it was argued, it should be possible for the lump sum to be boosted to the same extent. We accepted this point, and the legislation in Schedule 3 has been amended accordingly.

The measures I have outlined comprise some of the main changes in a continuing process of pensions reform which was initiated by my Rt Hon Friend, the previous Secretary of State for Social Services over three years ago. The proposals in this current Finance Bill build on, and extend, the changes made in recent Social Security legislation, and provide a better pensions deal for millions of employees - and the self-employed - in this country.

But there are a few changes to the pre-election Bill which I should mention to the House.

Lloyds

Clause 70 of the Bill deals with the tax treatment of Lloyd's Re-insurance to close arrangements. It re-introduces in revised form the proposal in Clause 58 of the April Finance Bill.

The House will recall that the need for legislation arises because of a defect in the present tax law. As matters stand, the Revenue does not have an effective locus for examining the justification for RIC, and if necessary adjusting it for tax purposes. If nothing were done, Lloyd's underwriters would be in the unique position of being able to determine the amount of a tax deduction without effective review by the Inspector of Taxes.

When the Chancellor announced these proposals in his Budget Speech, he said there would be immediate consultation with Lloyd's on the details of the legislation. The discussions have been extensive and thorough. We have considered Lloyd's representations very carefully. We have done so recognising there are two considerations to be satisfied. The first is that there must be an effective system for ensuring that the amount of the re-insurance premium can be properly scrutinised for tax purpose, and adjusted where necessary. This

is clearly right in principle, and necessary to achieve fairness to other taxpayers, whose claims for tax deductions have to satisfy scrutiny by the Tax Inspector. The second consideration is that the system must be fair to Lloyd's members, and take account of the special features of Lloyd's.

Lloyd's have, very properly, made it clear throughout the discussions that they recognise there should be a proper system for ensuring that tax deductions for RIC are not excessive. But they expressed concern about the original wording, which treated re-insurance to close as a provision. [The concern was directed at the principle of equating RIC premiums paid by one syndicate of Lloyd's members to another syndicate with the provisions for outstanding liabilities made by insurance companies.]

The revised Clause meets Lloyd's anxieties about the form of the original Clause. It now provides a free-standing test for the tax deductibility for re-insurance to close. The test is that the figure must be a fair and reasonable value of the liabilities, designed to produce neither a profit nor a loss to the Lloyd's members who assume the outstanding liabilities.

In its revised form, the Clause meets the twin objectives I set out a moment ago. It meets the objective of ensuring that the tax deductibility of RIC can be properly reviewed by the Tax Inspector. But it does so in a way which is fair to Lloyd's. It takes account of the special features of Lloyd's RIC arrangements, and meets their concerns about the proposals in their original form.

Capital gains streamlining

There is another important modification we have introduced that I wish to mention - That is a modification to the Bill's provisions on the taxation of companies' capital gains. As the House will know we received a number of representations about the impact of this change on the life assurance industry. The particular point of concern was whether the change to charging gains at the main corporation tax rate should apply to the gains which life assurance companies earn for their policyholders.

We considered this issue very carefully and concluded that we needed to take a general look at the tax arrangements for life assurance which have developed piecemeal over a long period.

There will be a full opportunity for the life assurance industry and other interested parties to contribute to the review. In an area as complex as this, the exercise is bound to take time but the Inland Revenue will be initiating consultations as speedily as possible. In the meantime we have decided that the tax rates on gains earned for policy holders should remain at 30 per cent pending the outcome of the review.

NEW MEASURES

Although the Bill is substantially unchanged I should mention briefly the four new clauses.

Clause 71 is simply designed to put it beyond doubt that tax relief for losses arising from capital gains indexation is not available against income where the loss arises on a withdrawal from a building society account.

Clause 80 is similarly designed to protect the spirit of existing legislation and makes it clear that capital gains 'rollover relief' is not available for gains or the disposal of interests in oil licences.

Wow. !
Clause 103 gives effect to the measure affecting fish processing ships known as Klondykers which my RHF announced in his speech in Perth in May and which will be particularly welcomed by Scottish fishermen. The clause will give a useful new relief from duty for stores imported for use on these factory ships. Without this relief there is a risk that these ships which provide a significant market for UK fishermen, would stop using British ports.

Clause 102 clarifies and supports existing legislation in relation to fees and charges for services and facilities provided by Government Departments. It enables Ministers to extend by Order the range of matters which they may take into account in setting such charges, in order to implement the normal policy of full cost recovery.

[OTHER CHANGES TO THE BILL IN RESPONSE TO REPRESENTATIONS

Finally, there are a few fairly minor changes to the Bill which I should mention briefly. We have made a number of improvements to the Pay and File provisions in response to representations from business groups. Again in response to representations we have made a change to Clauses 67 and 68 which end the present over generous treatment of tax credit relief for foreign withholding tax paid on interests on bank loans. This change will have the effect of doubling the length of the transitional period for loans already in existence on 1 April.

TECHNICAL AMENDMENTS TO 1987 ACT

There are also a couple of amendments to the Finance Act passed before the Election. Clause 97 fulfils our undertaking to extend the inheritance tax interest waiver facility created by Section 60 of the Act to estate duty and pre-1985 capital transfer tax. Clause 101 and Schedule 8 make technical amendments to the oil taxation provisions in Sections 61-63 of the Finance Act. They include a measure to counter arrangements to circumvent the petroleum revenue tax nomination scheme. This will take effect by Treasury order only if it becomes apparent that such arrangements are being made.]

CONFIDENTIAL



FROM: B O DYER
DATE: 8 July 1987

Alex
Tug
EP

01-270 4520

PS/FINANCIAL SECRETARY

cc PPS

PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Scholar
Miss Evans
Mr Halligan
Mr Cropper
1. Mr Savage
2. File

FINANCE BILL : LORDS

The Business Managers have earmarked Thursday 23 July for the Bill's Second Reading and remaining stages in the Lords. We do not know whether the Lords will wish, on this occasion, to have the customary economic day debate on Second Reading; it depends largely on the wishes of the Opposition. Personally, I think a debate unlikely. Peers Allowances and Ministerial Salaries are also scheduled for debate that day; and, I suspect, that subject is likely to be of more interest to Members of the Lords than a debate on the economy! (For the record, MPs Pay is down for debate in the Commons the previous day, Wednesday 22 July).

2. We expected Lord Brabazon to take charge of the Finance Bill's passage through the Lords; but I am advised that his diary engagements make it impossible on 23 July. I am pursuing alternatives with Lord Young's office. Currently, the front runner is Lord Beaverbrook.

A handwritten signature in dark ink, appearing to be 'B. O. Dyer'.

B O DYER
Parliamentary Clerk



01-270 4520

FROM: B O DYER
DATE: 9 July 1987

PS/FINANCIAL SECRETARY

cc PPS
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Scholar
Miss O'Mara
Miss Evans
Mr Cropper
1. Mr Savage
2. File

FINANCE BILL : LORDS

Lord Young has confirmed that he will take charge of proceedings on the Finance Bill in the House of Lords on Thursday 23 July (my minute of 8 July, refers).

2. If the Lords request a debate on Second (or Third) Reading, Lord Young will require draft speaking notes (about 10 to 15 minutes), and background briefing to enable him to field any supplementaries. I shall try to get a definitive view from the Business Managers on whether there is to be a debate by the end of next week. In the meantime, FP may like to consider what material may need to be commissioned.

A handwritten signature in dark ink, appearing to be 'B. O. Dyer'.

B O DYER



Inland Revenue

Policy Division
Somerset House

FROM: J H REED
DATE: 10 JULY 1987

FINANCIAL SECRETARY

LETTER FROM THE INSTITUTE OF TAXATION
CLAUSE 40 OF THE SPRING FINANCE BILL (CLAUSE 61 OF THE CURRENT
ONE)

At your meeting on 9 July, you asked for a draft letter to the Institute of Taxation explaining that it had not proved possible to do anything this year but their proposals would be considered before next year's Finance Bill. This is attached.

2. During the coming Finance Bill Starters exercise we shall bring forward starters on the two points which seem most meritorious

- i. the prevention of multiple apportionment of interest payments; and
- ii. excluding from apportionment any interest payments for which the company cannot get tax relief.

3. We shall soon show you our proposed Statement of Practice about our interpretation of the phrase "a member of a trading group".

J H REED

cc PPS
Chief Secretary
Paymaster General
Economic Secretary
Miss Sinclair
Mr Cropper
Mr Jenkins (OPC)

Mr Painter
Mr McGivern
Mr Campbell
Mr Whitear
Mr Gordon
Mr Reed
Mr Huffer
PS/IR

R M Ivison
President
The Institute of Taxation

FINANCE BILL 1987, CLAUSE 40

You wrote to John MacGregor on 21 April about the apportionment legislation and about the right of audience of your members before Commissioners upon any appeal. He replied on 12 May and said that the Revenue would be in touch with you to try to agree on the nature and seriousness of any problems with the apportionment legislation and the possible solutions.

Since then, your Mr Clark and Mr Ring have had a meeting with the Revenue to discuss the apportionment legislation. As the Revenue explained, Clause 40 (which has become Clause 61 of the current Finance Bill) will bring the law into line with the way they used to operate it before the decision in the Lansing Bagnall case, when they believed that they did not have wide-ranging discretionary powers. Inspectors will however continue to have the normal discretion under the Board's care and management powers not to pursue points which seem unlikely to be worthwhile. So the change does not represent a tightening-up of the apportionment legislation. I hope this will allay most of your worries.

You go on to mention various specific apportionment provisions which you think should be amended. One concerns the exclusion from the apportionment of interest etc (under Paragraph 3A of Schedule 16 to the Finance Act 1972) of a company which is a

member of a trading group. You say that a company will not fall within this exclusion if it has a single dormant subsidiary, or property investment subsidiary, even though the company exists wholly or mainly for the purpose of co-ordinating the administration of the trading subsidiaries. As the Revenue explained, they do not interpret the provision in this way: the exclusion can apply even where there are non-trading subsidiaries. Since there is clearly some doubt among tax practitioners about the interpretation of this provision, the Revenue will soon be publishing a statement of practice setting out their interpretation.

I understand that this interpretation weakens some of your other concerns about the apportionment legislation but that you think that some problems remain. I regret that, as Mr MacGregor anticipated, it did not prove possible to consider these points in sufficient depth before publication of the current Finance Bill but I can assure you that we shall think about them before next year's Finance Bill. Wherever possible, it would be helpful to have an indication of the practical difficulties that arise and actual examples of these.

NORMAN LAMONT



Inland Revenue

FROM: H B THOMPSON

DATE: 10 JULY 1987

Policy Division
Somerset House

FINANCIAL SECRETARY

SUMMER FINANCE BILL

INHERITANCE TAX : SCHEDULE 7

1. Mr Neil Hamilton (Tatton - Conservative) has tabled an amendment (number 30) which is technically defective but which we think is acceptable in practice. A copy of the relevant page of the Order Paper is annexed.

2. The amendment modifies the circumstances that trigger the special rate of inheritance tax charge on property that passes through an interest in possession (IIP) trust to a discretionary trust. The special rate of charge will not be triggered if the property passes out of the discretionary trust regime within six months.

cc	PS/Chancellor of the Exchequer	Chairman
	PS/Chief Secretary	Mr Isaac
	PS/Paymaster General	Mr Painter
	PS/Economic Secretary	Mr Houghton
	Sir P Middleton	Mr Calder
	Mr Cassell	Mr Lawrance
	Mr Monger	Mr Cleave
	Mr Scholar	Mr Scott
	Miss Sinclair	Mr Furey
	Mr Cropper	Mr Gonzalez
	Mr Haigh	Mr Brown
	Mr Graham (Parl. Counsel)	Mr Johns
	Miss Johnson (Parl. Counsel)	Mr Kent
		Mr Battersby
		Mr Thompson
		Mr McKean
		Mr Lakhanpaul
		PS/IR
		Mr Beighton
		Mr R Draper

3. The amendment provides a window of opportunity for trustees who are caught by the anti-avoidance provisions in Schedule 7 to rearrange matters so as to avoid the special rate of charge. If an interest in possession that was created by a potentially exempt transfer (PET) comes to an end within seven years of the PET, and the property then becomes subject to discretionary trusts, the termination may be subject to a special rate of charge (instead of the normal rate) if the settlor is still alive. The amendment will prevent the special rate from applying on that termination if within the following six months the property is made subject to another IIP or passed to outright individual ownership or to an Accumulation and Maintenance trust. The normal rate charge will however remain.

4. The merit of the proposal is that it will prevent people who have made perfectly proper trust provisions, with no avoidance motive, from being inadvertently caught by the special rate of charge. Without it, a trust which (for example) provided for successive interests in possession at the trustees' discretion would be caught if an interest in possession ended prematurely, perhaps on the death of a life tenant, before the trustees had appointed a successor. The amendments will allow trustees to make the appointment within six months after the life tenant's death without incurring a penalty.

Possible objections

5. In theory, the facility would be open to abuse to allow the total defeat of the special rate provisions. The device would be to hold the property in discretionary trusts for successive periods of six months, interspersed with bed and breakfast in IIP trusts, for the whole of the seven year period during which liability to the special rate of charge subsists. But this may be considered a rather fanciful scenario. It would involve finding up to fourteen men of straw to take the interests in possession.

6. The facility would also enable an avoider whose plans did not cover premature termination of an IIP to mount a rescue operation by putting in a replacement life tenant. But that hardly matters if the only effect is that apart from a short interregnum the property stays in the IIP regime for the seven years that is necessary to escape the special rate of charge.

7. The amendment is technically unsound, in that its phraseology does not match that of the clause it amends. The annex gives wording, drafted by Parliamentary Counsel, which would be more appropriate to achieve Mr Hamilton's purpose.

Options

8. If you consider that the "bed and breakfast" device is sufficient to rule out the amendment, the appropriate course, given the time constraints, would probably be to resist the amendment and undertake to consider the matter further for next year. If however you think the risks can be taken, the options are either to accept in principle in Committee and put forward Parliamentary Counsel's version as a Government amendment on Report; or to offer Counsel's version to Mr Hamilton for him to table for Committee in place of his own wording. If he did this, you could accept the revised amendment in Committee.

9. We shall be glad to have your instructions on the course you wish to pursue.

A handwritten signature in black ink, appearing to read 'H B Thompson', with a stylized flourish at the end.

H B THOMPSON

Finance Bill continued

Sir William Clark

25

- ★ Clause 87, page 56, line 1, leave out subsection (3) and insert—

'In relation to a repayment of income tax falling within subsection (1)(b) above the material date is the 15th day following the end of the period specified in paragraph 2(2) of Schedule 20 Finance Act 1972 in which the corresponding payments referred to in subsection (1)(b) above fell to be received.'

Sir William Clark

26

- ★ Clause 87, page 56, line 49, at end add—

'(a) For the purposes of subsection (1) above, where income tax is set-off against corporation tax under section 240(5) Taxes Act 1970, it shall be treated as a repayment of income tax made on the material date for payment of that corporation tax'.

Sir William Clark

27

- ★ Clause 90, page 60, line 6, after 'assessment' insert 'For the purpose of this subsection, income tax deducted at source from income received shall be deemed to be corporation tax paid on the material date in section 87(3)'.

Sir William Clark

28

- ★ Clause 90, page 60, line 17, at end insert 'this subsection shall take precedence over section 240(5) Taxes Act 1970'.

Sir William Clark

29

- ★ Clause 95, page 62, line 25, leave out subsection 3 and insert—

'(3) Except in relation to Clauses 87 and 90(5) for which the appointed day shall be 6th April 1988, no day may be appointed by virtue of subsection (2) above which falls earlier than 31st March 1992'.

Mr Neil Hamilton

- ★ Schedule 7, page 93, line 14, at end insert ' ; and
(d) within six months of the coming to an end of the relevant interest the property has neither—

- (i) become settled property either in which a qualifying interest in possession subsists or which falls within section 71 below; nor
(ii) become property to which an individual has become absolutely entitled'.

COMMITTEE OF THE WHOLE HOUSE

FINANCE BILL

Schedule 7, page 93, line 14, at end insert 'and

^{that,}
(d) within six months of the coming to an end
of the relevant interest, [any of] the
property in which that interest subsisted
has neither -

(i) become settled property in which
a qualifying interest in possession
subsists or to which section 71 below
applies, nor

(ii) become property to which an
individual is beneficially
entitled'.



FROM: P D P BARNES
DATE: 10 July 1987

APS/FINANCIAL SECRETARY

cc PS/Chancellor
Mr Cassell
Mr Scholar
Miss Sinclair
Mr Fawcett - IR
Miss Hill - IR
PS/IR

FINANCE BILL : RETROSPECTION

I understand the Financial Secretary spoke briefly to the Economic Secretary at Prayers this morning about retrospection, which is relevant to clauses 62 and 80 of the Finance Bill.

I understand that the Financial Secretary agreed to commission advice on:-

- (i) precedents for retrospective legislation; and
- (ii) who voted for these precedents when they were introduced.

2. The Economic Secretary would like to have a further word with the Financial Secretary about retrospection after his meeting with UKOITC on Monday morning. I understand that you will be arranging a meeting.

PB

P D P BARNES
Private Secretary

CC: . PDS, CST, PMG, EST
 MISS. SINCLAIR
 MR. CROPPER
 MR. JENKINS CPC
 MR. J. H. REED IR
 PS/IR.



Treasury Chambers, Parliament Street, SW1P 3AG

R L Jennings Esq
 President
 The Institute of Taxation
 12 Upper Belgrave Street
 LONDON
 SW1X 8BB

13 July 1987

Dear Mr Jennings

FINANCE BILL 1987, CLAUSE 40

Your predecessor wrote to John MacGregor on 21 April about the apportionment legislation and about the right of audience of your members before Commissioners upon any appeal. He replied on 12 May and said that the Revenue would be in touch with the Institute to try to agree on the nature and seriousness of any problems with the apportionment legislation and the possible solutions.

Since then, your Mr Clark and Mr Ring have had a meeting with the Revenue to discuss the apportionment legislation. As the Revenue explained, Clause 40 (which has become Clause 61 of the current Finance Bill) will bring the law into line with the way they used to operate it before the decision in the Lansing Bagnall case, when they believed that they did not have wide-ranging discretionary powers. Inspectors will however continue to have the normal discretion under the Board's care and management powers not to pursue points which seem unlikely to be worthwhile. So the change does not represent a tightening-up of the apportionment legislation. I hope this will allay most of your worries.

Mr Ivison went on to mention various specific apportionment provisions which you think should be amended. One concerns the exclusion from the apportionment of interest etc (under Paragraph 3A of Schedule 16 to the Finance Act 1972) of a company which is a member of a trading group. You say that a company will not fall within this exclusion if it has a single dormant subsidiary, or property investment subsidiary, even though the company exists wholly or mainly for the purpose of co-ordinating the administration of the trading subsidiaries. As the Revenue explained, they do not interpret the provision in this way: the exclusion can apply even where there are non-trading subsidiaries. Since there is clearly some doubt among tax practitioners about the interpretation of this provision, the Revenue will soon be publishing a statement of practice setting out their interpretation.

I understand that this interpretation weakens some of your other concerns about the apportionment legislation but that you think that some problems remain. I regret that, as Mr MacGregor anticipated, it did not prove possible to consider these points in sufficient depth before publication of the current Finance Bill but I can assure you that we shall think about them before next year's Finance Bill. Wherever possible, it would be helpful to have an indication of the practical difficulties that arise and actual examples of these.

Yours sincerely
Norman Lamont

NORMAN LAMONT



FROM: N WILLIAMS
DATE: 13 July 1987

18

MR H B THOMPSON IR

cc PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Mr Cassell
Mr Monger
Mr Scholar
Miss Sinclair
Mr Cropper
Mr Haigh
Mr Graham OPC
Miss Johnson OPC
PS/IR

SUMMER FINANCE BILL

INHERITANCE TAX : SCHEDULE 7

1. The Financial Secretary was grateful for your minute of 10 July.
2. This is to confirm as I told you by telephone this morning that the Financial Secretary was content that Counsel's version of the amendment should be offered to Mr Hamilton for him to table for Committee in place of his wording. I have arranged for a copy of the revised form of words attached to your minute to be sent to Mr Hamilton this morning.
3. On this basis the Financial Secretary will therefore accept the revised amendment in Committee.

NIGEL WILLIAMS
(Assistant Private Secretary)



Inland Revenue

Policy Division
Somerset House

FROM: N C MUNRO

14 July 1987

PS/Financial Secretary (Mr Williams - by fax)

128

SCHEDULE 3 SUMMER FINANCE BILL

MR TONY BLAIR'S AMENDMENT NO 36

1. Today's 'Guardian' reports that the NAPF have lent their support to Mr Blair's amendment. This is hardly surprising, since the amendment would entirely undermine the proposed change in the accelerated accrual rules for maximum pension benefits (twenty years service, rather than ten).
2. The Financial Secretary may therefore find it helpful to have this supplementary speaking note, which deals rather more fully with the objections to the amendment.

Nem.

N C MUNRO

cc PPS
PS/CST
PS/PMG
PS/EST
Mr Scholar
Miss Sinclair
Mr Cropper

Mr Isaac
Mr Beigjton
Mr Corlett
Mr Lusk
Mr Munro
Mr Hinton
PS/IR

MR TONY BLAIR'S AMENDMENT NO 36: SUPPLEMENTARY SPEAKING NOTE

Hon Member's amendment would mean that one employer would be providing employee with pension partly in respect of service with another, completely different, employer. This would entail substantial cross-subsidisation, particularly where schemes did not offer similar benefits.

Not clear that employers could obtain tax deduction, under general tax principles, for their higher contributions.

And of course only a handful of privileged employees would benefit from this amendment - the same handful who, under the old rules, could obtain maximum benefits after as little as ten years. Because employers are simply not prepared to fund for higher pensions generally.

DEFENSIVE

Public sector 'transfer club': civil servants treated favourably

Understand point, but it is misconceived. It has always been possible for employees to move between different schemes of same employer and retain past pensionable service. Hon Member's amendment would apply to schemes of entirely unconnected employers.



Inland Revenue

Policy Division
Somerset House

FROM: N C MUNRO

14 July 1987

PS/Financial Secretary (by fax)

CLAUSE 20 FINANCE BILL

SIR BRANDON RHYS WILLIAMS AMENDMENT NO 41

1. Contrary to expectations, this amendment has been selected.
2. I suggest the following speaking note.

"My hon Friend's amendment would require the Treasury to consult the Occupational Pension Board before making an Order to amend clause 20. This amendment is unnecessary. Clause 20 sets out which bodies may establish personal pension schemes. The main purpose of the Treasury Order would be to extend the range of personal pension providers, if and when this seems appropriate, without having to introduce primary legislation in a future Finance Bill. If such an Order were being made, the Treasury would naturally consult the Occupational Pension Board - and any other interested party - if appropriate.

N C MUNRO

cc PPS
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Scholar
Miss Sinclair
Mr Cropper

Mr Isaac
Mr Beighton
Mr Corlett
Mr Lusk
Mr Munro
Mr Hinton
PS/IR

1 Tony
2 Alex
pwp



FROM: Deputy Parliamentary Clerk
DATE: 14 July 1987

01-270 5006

PRINCIPAL PRIVATE SECRETARY

PS/CHIEF SECRETARY

PS/FINANCIAL SECRETARY

PS/PAYMASTER GENERAL

PS/ECONOMIC SECRETARY

cc Mr M C Scholar - FP
Mr P R C Gray - IAE3
Miss C E C Sinclair - FP
Mr K Bradley - CA
Miss C Evans - FP
Mr W Guy - IAE3
Mr M Haigh - FP
Mr A Hudson
Mr K Romanski - FP
PS/IR
PS/HMCE

FINANCE BILL : COMMITTEE OF THE WHOLE HOUSE

Mr Chairman of Ways and Means' selection of amendments for the first day of Committee of the Whole House is as follows:-

CLAUSE 1 (Interpretation)

35

Clause 2 (Taxation of profit-related pay)
Debate on Clause Stand Part

CLAUSE 3 (Relief from tax)

31

CLAUSE 4 (Exceptions from relief)
Debate on Clause Stand Part

CLAUSE 5 (Persons who may apply for registration)
Debate on Clause Stand Part

CLAUSE 6 (Excluded employments)
1+32+2

CLAUSE 7 (Applications for registration)
Debate on Clause Stand Part

CLAUSE 8 (Registration)
Debate on Clause Stand Part

CLAUSE 9 (Change of scheme employer)
Debate on Clause Stand Part

CLAUSE 10 (Cancellation of registration)
Debate on Clause Stand Part

CLAUSE 11 (Recovery of tax from scheme employer)
Debate on Clause Stand Part

CLAUSE 12 (Annual returns etc)
Debate on Clause Stand Part

CLAUSE 13 (Other information)
Debate on Clause Stand Part

CLAUSE 14 (Information : penalties)
Debate on Clause Stand Part

CLAUSE 15 (Appeals)
Debate on Clause Stand Part

CLAUSE 16 (Partnerships)
Debate on Clause Stand Part

CLAUSE 17 (Independent accountants)
Debate on Clause Stand Part

SCHEDULE 1 (Profit-related pay schemes: conditions for registration)

33

34

CLAUSE 18 (Interpretation)
Debate on Clause Stand Part

CLAUSE 19 (Approval of schemes)
Debate on Clause Stand Part

CLAUSE 20 (Establishment of schemes)
41

CLAUSE 21 (Scope of benefits)
Debate on Clause Stand Part

CLAUSE 22 (Annuity to member)
Debate on Clause Stand Part

CLAUSE 23 (Lump sum to member)
40+39

CLAUSE 24 (Annuity after death of member)
44+42+43

CLAUSE 25 (Lump sum on death of member)
Debate on Clause Stand Part

CLAUSE 26 (Return of contributions on death of member)
Debate on Clause Stand Part

CLAUSE 27 (Scheme administrator)
45

CLAUSE 28 (Transfer payments)
46

CLAUSE 29 (Excess contributions)
Debate on Clause Stand Part

CLAUSE 30 (Restriction on contributors)
Debate on Clause Stand Part

CLAUSE 31 (Deduction from relevant earnings)
Debate on Clause Stand Part

CLAUSE 32 (Limit on deductions)
Debate on Clause Stand Part

CLAUSE 33 (Carry-back of contributions)
Debate on Clause Stand Part

CLAUSE 34 (Carry-forward of relief)
Debate on Clause Stand Part

CLAUSE 35 (Meaning of "relevant earnings")
Debate on Clause Stand Part

CLAUSE 36 (Earnings from pensionable employment)
Debate on Clause Stand Part

CLAUSE 37 (Meaning of "net relevant earnings")
Debate on Clause Stand Part

CLAUSE 38 (Employer's contributions)
Debate on Clause Stand Part

CLAUSE 39 (Exemption for scheme investments)

47

CLAUSE 40 (Unit trusts)
Debate on Clause Stand Part

CLAUSE 41 (Treatment of annuities)
Debate on Clause Stand Part

CLAUSE 42 (Minimum contributions under Social Security Act 1986)
Debate on Clause Stand Part

CLAUSE 43 (Withdrawal of approval)
Debate on Clause Stand Part

CLAUSE 44 (Tax on unauthorised payments etc)
Debate on Clause Stand Part

CLAUSE 45 (Relief by deduction from contributions)
Debate on Clause Stand Part

CLAUSE 46 (Claims for relief)
Debate on Clause Stand Part

CLAUSE 47 (Appeals)
Debate on Clause Stand Part

CLAUSE 48 (Adjustment of relief)
Debate on Clause Stand Part

CLAUSE 49 (Exclusion of double relief)
Debate on Clause Stand Part

CLAUSE 50 (Information about payments)
Debate on Clause Stand Part

CLAUSE 51 (Information : penalties)
Debate on Clause Stand Part

CLAUSE 52 (Remuneration of Ministers and other officers)
Debate on Clause Stand Part

CLAUSE 53 (Contributions under unapproved arrangements)
Debate on Clause Stand Part

CLAUSE 54 (Retirement annuities)
Debate on Clause Stand Part

CLAUSE 55 (Transitional provisions: general)
Debate on Clause Stand Part

CLAUSE 56 (Transitional provisions: approvals)
Debate on Clause Stand Part

CLAUSE 57 (Minor and consequential amendments)
Debate on Clause Stand Part

SCHEDULE 2 (Personal Pension Schemes etc)
Debate on Clause Stand Part

CLAUSE 58 (Occupational Pension Schemes)

4+5+6

Richard Savage
RICHARD SAVAGE



01-270 4520

FROM: B O DYER
 DATE: 14 July 1987

MISS EVANS - FP

cc PS/Chancellor
 PS/Chief Secretary
 PS/Financial Secretary
 PS/Paymaster General
 PS/Economic Secretary
 Mr Scholar
 Miss O'Mara
 Mr Savage
 Mr Wallis
 Mr Cropper

PS/Inland Revenue
 PS/Customs and Excise

FINANCE BILL : HOUSE OF LORDS

We have been advised (Fred Jaeger, Government Whips, Lords) that the Opposition spokesman, Lord Donnington, has requested a debate on Second Reading (best guess, circa 2-3 hours).

2. Second Reading and remaining stages are scheduled for **Thursday 23 July**. Due to pressure of business, the House is expected to meet at 11am on that day. Oral questions will take the first 20 minutes, after which Lord Young will formally move the Bill's Second Reading and open the debate. Once Second Reading has been obtained, the remaining stages of the Bill will go through formally and be followed by a debate on a motion in respect of Peers Allowances.

3. As foreshadowed in my minute of 9 July, Lord Young will require some draft speaking notes and background briefing for the Second Reading debate. I should be grateful if you would approach Lord Young's Private Secretary (Tim Walker: 215-5422) to ascertain Lord Young's requirements in this context; and also to arrange a suitable date with the Secretary of State for an oral briefing meeting with appropriate Treasury and Inland Revenue officials.

B O DYER



FROM: J J HEYWOOD
DATE: 14 July 1987

PS/PAYMASTER GENERAL

cc PS/Chancellor
PS/Chief Secretary
PS/Economic Secretary
Mr Scholar
Mr Dyer
Mr Guy
Mr Munro IR
Mr Farmer IR
Mr Walker IR (BY FAX)
PS/IR
Mr Jenkins OPC

FINANCE BILL: COMMITTEE STAGE

1. The Financial Secretary has agreed with Mr Blair that the aim should be to get down to Clause 57 tonight, starting tomorrow afternoon with Clause 58 and Schedule 3. Although we cannot be certain we will get right down to Clause 57, we can be sure that Clause 58 will not be debated today.

2. Parliamentary Counsel has let me know that the following amendments have been selected by the Speaker: 35; 31; 1 + 32 + 2(Grouped); 33; 34; 41; 40 + 39(Grouped); 44 + 42 + 43(Grouped); 45; 46; 47; 4 + 5 + 6(Grouped).

3. I would be grateful if you could confirm that the Paymaster General is content to take on Clauses 60 and 65 in tomorrow's session, to lighten the load on the Financial Secretary.

JEREMY HEYWOOD
Private Secretary

COMMITTEE OF THE WHOLE HOUSE

WEDNESDAY 15 JULY 1987

FINANCE BILL

Provisional selection of amendments:

77 + 69 + 78

79 + 80

81 + 82

51 + 52

71 + 8 + 55 + 36 + 54 + 75

85

72 + 9 + 73

53 + 56

10

66

11 + 12 to 16 + 18

Govt 19 + Govt 20 + Govt 24

21 + 67 + 22 + 23

48 + 63 + 49

60 + 61

25 + 26 to 29

91

89

HAROLD WALKER
Chairman of Ways and Means

15th July 1987



1. G. H. G.
2. R. A.
FROM: Deputy Parliamentary Clerk
DATE: 15 July 1987

01-270 5006

PRINCIPAL PRIVATE SECRETARY

PS/CHIEF SECRETARY:

PS/FINANCIAL SECRETARY

PS/PAYMASTER GENERAL

PS/ECONOMIC SECRETARY

cc Mr M C Scholar - FP
Mr P R C Gray - IAE3
Miss C E C Sinclair - FP
Mr K Bradley - CA
Miss C Evans - FP
Mr W Guy - IAE3
Mr M Haigh - FP
Mr K Romanski - FP
PS/IR
PS/HMCE

FINANCE BILL : COMMITTEE OF THE WHOLE HOUSE

Mr Chairman of Ways and Means' selection of amendments for the second day of Committee of the Whole House is as follows:-

CLAUSE 58 (Occupational Pension Schemes)

4+5+6

SCHEDULE 3 (Occupational pension schemes)

77+69+78

79+80

81+82

51+52

71+8+55+36+54+75

85

72+9+73

53+56

10

CLAUSE 59 (Employee share schemes)

Debate on Clause Stand Part

CLAUSE 60 (Payments of interest etc. between related companies)

Debate on Clause Stand Part

CLAUSE 61 (Apportionment of income etc of close companies)

Debate on Clause Stand Part

CLAUSE 62 (United Kingdom members of partnerships controlled abroad)

66

CLAUSE 63 (Limitation of group relief in relation to certain dual resident companies)

11+12 to 16+18

SCHEDULE 4 (Dual resident investing companies)
Debate on Schedule Stand Part

CLAUSE 64 (Limitation of other reliefs in dealings involving dual resident investing companies)
Debate on Clause Stand Part

CLAUSE 65 (Controlled foreign companies: acceptable distribution policy)
Debate on Clause Stand Part

CLAUSE 66 (Offshore funds)
Debate on Clause Stand Part

CLAUSE 67 (Double taxation relief: interest on certain overseas loans)
Debate on Clause Stand Part

CLAUSE 68 (Double taxation relief: underlying tax reflecting interest on loans)
Debate on Clause Stand Part

CLAUSE 69 (Disclosure of employment information obtained from Inland Revenue)
Debate on Clause Stand Part

CLAUSE 70 (Lloyds underwriters)
Govt 19+Govt 20+Govt 24
21+67+22+23

CLAUSE 71 (Relief for losses on unquoted shares in trading companies)
Debate on Clause Stand Part

CLAUSE 72 (Allowances for dwelling-houses let on assured tenancies)
Debate on Clause Stand Part

CLAUSE 73 (Recognised investment exchanges)
Debate on Clause Stand Part

CLAUSE 74 (General rules)
Debate on Clause Stand Part

CLAUSE 75 (Life assurance business)
Debate on Clause Stand Part

CLAUSE 76 (Gains from oil extraction activities etc)
Debate on Clause Stand Part

SCHEDULE 5 (Companies' chargeable gains: transitional provisions)
Debate on Schedule Stand Part

CLAUSE 77 (Double taxation relief)
Debate on Clause Stand Part

CLAUSE 78 (Collective investment schemes)
Debate on Clause Stand Part

CLAUSE 79 (Building societies: groups of companies)
Debate on Clause Stand Part

CLAUSE 80 (Roll-over relief not available for gains on oil
licences)
48+63+49

CLAUSE 81 (Commodity and financial futures and options)
Debate on Clause Stand Part

Amendments provisionally selected up to the end of the Finance
Bill are as follows:-

CLAUSE 84 (Assessment of amounts due by way of penalty)
60+61

CLAUSE 87 (Interest on tax overpaid)
25+26 to 29

SCHEDULE 7 (Inheritance tax: interests in possession)
91

CLAUSE 97 (Acceptance in lieu: CTT and estate duty)
89

Richard Savage

RICHARD SAVAGE



From: B. O. DYER
Date: 16 July '87

Chancellor

cc Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Mr. Cropper
Mr. Syrie

Prangers: Finance Bill Third Reading

It is possible that the Opposition will press for a full scale Third Reading debate on Monday, 20 July. During the Business Statement today, the leader of the Opposition asked if time could be found next week for an economic debate - presumably, among other things, to pursue the Government on Lord Cockfield's proposals for the harmonisation of VAT (zero rates) and Excise Duties throughout the EEC. In reply, the LPS said that, with a little ingenuity on the part of the Opposition, Monday's Third Reading might provide a suitable opportunity.

I suspect this is likely to receive the tacit, if not active, support of the Govt. Business Managers. They do not want a lengthy debate on the Scottish Rate Support Grant Order, which is exempted business for 1½ hours on Monday; and, if proceedings on the Finance Bill continued until 10 pm, this would suit them (not us) very well.

The Treasury Whip may have more up-to-date intelligence to report at Prangers tomorrow. If the Opposition pursue this - e.g. table an amendment to the question for Third Reading, one of the Opposition spokesmen could be Gordon Brown (Shadow Chief Secretary).

Brian Dyer



FROM: Deputy Parliamentary Clerk
DATE: 16 July 1987

01-270 5006

PRINCIPAL PRIVATE SECRETARY

PS/CHIEF SECRETARY

PS/FINANCIAL SECRETARY

PS/PAYMASTER GENERAL

PS/ECONOMIC SECRETARY

cc Mr M C Scholar - FP
Mr P R C Gray - IAE3
Miss C E C Sinclair - FP
Mr K Bradley - CA
Miss C Evans - FP
Mr W Guy - IAE3
Mr M Haigh - FP
Mr K Romanski - FP
PS/IR
PS/HMCE

FINANCE BILL : COMMITTEE OF THE WHOLE HOUSE

Mr Chairman of Ways and Means' selection of amendments for the third day of Committee of the Whole House is as follows:-

CLAUSE 80 (Roll-over relief not available for gains on oil licences)

48+63+49

CLAUSE 81 (Commodity and financial futures and options)
Debate on Clause Stand Part

CLAUSE 82 (Return of profits)
Debate on Clause Stand Part

CLAUSE 83 (Failure to make return for corporation tax)
Debate on Clause Stand Part

CLAUSE 84 (Assessment of amounts due by way of penalty)
60+61

CLAUSE 85 (Interest on overdue corporation tax etc)
Debate on Clause Stand Part

CLAUSE 86 (Supplementary provisions as to interest on overdue tax)
Debate on Clause Stand Part

CLAUSE 87 (Interest on tax overpaid)
25+26 to 29

CLAUSE 88 (Recovery of overpayment of tax etc)
Debate on Clause Stand Part

CLAUSE 89 (Prescribed rate of interest)
Debate on Clause Stand Part

CLAUSE 90 (Corporation tax to be payable without assessment)
Debate on Clause Stand Part

CLAUSE 91 (Close companies: loans to participators)
Debate on Clause Stand Part

CLAUSE 92 (Amendments relating to PAYE)
Debate on Clause Stand Part

CLAUSE 93 (Sub-contractors in the construction industry)
Debate on Clause Stand Part

CLAUSE 94 (Failure to do things within a limited time)
Debate on Clause Stand Part

CLAUSE 95 (Interpretation of Chapter V and consequential and
supplementary provisions)
Debate on Clause Stand Part

SCHEDULE 6 (Management provisions: supplementary and consequential
provisions)
Debate on Schedule Stand Part

CLAUSE 96 (Interests in possession)
Debate on Clause Stand Part

SCHEDULE 7 (Inheritance tax: interests in possession)
91

CLAUSE 97 (Acceptance in lieu: CTT and estate duty)
89

CLAUSE 98 (Personal pension schemes)
Debate on Clause Stand Part

CLAUSE 99 (Stamp duty: options etc)
Debate on Clause Stand Part

CLAUSE 100 (Stamp duty reserve tax)
Debate on Clause Stand Part

CLAUSE 101 (Oil taxation)
Debate on Clause Stand Part

SCHEDULE 8 (Amendments of Schedule 10 to Finance Act 1987)
Debate on Schedule Stand Part

CLAUSE 102 (Government fees and charges)
Debate on Clause Stand Part

CLAUSE 103 (Consumption in port of goods transhipped for use
as stores etc)
Debate on Clause Stand Part

CLAUSE 104 (Short title, interpretation, construction and
repeals)
Debate on Clause Stand Part

NEW CLAUSE 18 (Option to Commute Annuity Rights for a Lump
Sum)
Debate on New Clause Stand Part

Richard Savage
RICHARD SAVAGE



Inland Revenue

Policy Division
Somerset House

Handwritten signature/initials

FROM: M F CAYLEY
DATE: 17 JULY 1987

1. MR HOUGHTON *M 17/7*
2. PS/FINANCIAL SECRETARY

SUMMER FINANCE BILL: REPEAL SCHEDULE

1. It has been decided that there should be no Report Stage amendment to correct the defect identified in my note of 16 July, but that an announcement should be made next week.

2. I attach a draft of a Question and Answer. If the Financial Secretary is content, I would be grateful if you could arrange for the Question to be tabled when Report Stage is over.

3. For a point as technical has this, we do not think a press release is appropriate.

Michael GJ

M F CAYLEY

cc PS/Chancellor
Mr Scholar
Mr Cropper

Mr Isaac
Mr Houghton
Mr Cayley
Mr Hamilton
Mr Michael
PS/IR

Question

To ask Mr Chancellor of the Exchequer, whether the Finance Bill 1987 amends the definition of an investment trust, and if he will make a statement.

Draft Reply

Under the Finance Bill the whole of Section 93 Finance Act 1972 would be repealed. Most of the Section is concerned with the arrangements which were introduced to secure a 30 per cent note on the capital gains of companies. These arrangements would be overtaken by the changes in the Bill for companies' capital gains, and therefore need to be repealed. Section 93(6) however relates to the circumstances in which an investment trust can be approved under Section 359 of the Income and Corporation Taxes Act and hence qualify for tax exemption on its capital gains. The need for subsection (6) will remain. In the time available it has not been possible to correct the Repeal Schedule in the Finance Bill, but, we shall be introducing in next year's Bill a provision to preserve subsection (6). This provision will be effective from 17 March 1987, the date from which the repeal of Section 93 has effect under the Bill.

Andrew

Phyl

FROM: MISS C EVANS
DATE: 17 July 1987

FINANCIAL SECRETARY

cc **Chancellor**
Chief Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Mr Scholar
Miss O'Mara
Mr Gray
Mr Dyer
Mr Hudson
Mr Walker - IR
Ms French - C&E

C.
Looks OK to me.
[Signature]

FINANCE BILL: LORDS SECOND READING: 23 JULY

We have agreed to provide a draft of Lord Young's opening speech in the Lord's Second Reading debate on Thursday, 23 July, by next Monday. I attach the draft speech we propose to send which deals with

the economic background and tax reform
tax reform
PRP
pensions
Lloyd's
pay and file
CGT streamlining
unintended loopholes

2. Unavoidably this is familiar material but we have tried to revise it to *minimise repetition of* what has been said in the Commons.

3. I also propose to send Lord Young's office defensive speaking notes on Lloyd's and retrospection, a copy of the Lobby Notes, a factual summary of the measures in the 1987 Finance Act and the Summer Finance Bill, as well as selected notes on clauses. On other topical tax matters (VAT, tax burden) we will flag up the relevant sections of the Treasury weekly brief which will also be ready on Monday. We have offered to provide the usual official support for the Lord debate.

4. Are you content with the material we propose to send Lord Young?

CE

MISS C EVANS

LORD YOUNG'S OPENING SPEECH FOR THE SECOND READING OF THE FINANCE
BILL IN THE LORDS ON 23 JULY 1987

My Lords, I beg to move, that this Bill be now read a second time.

2. The Bill completes the package of measures announced in my right honourable Friend the Chancellor's Budget speech last March. The Budget, with the two Finance Bills which have succeeded it, was set against the most favourable economic background seen by this country for many years. It provided clear evidence of the success of the Government's policies of sound finance, low borrowing and low inflation. These policies have enabled the Chancellor in one year to cut taxes and borrowing, while at the same time increasing resources for priority public services. We intend to stick to these policies which have brought about our present economic success.

3. Noble Lords will recall the positive assessment of the economy which I gave in the debate on the Address. The key facts are striking. The UK economy is entering its seventh successive year of growth. From being at the bottom of the European growth league for two decades, we have now moved to the top. What we are seeing is a transformation in the performance of British industry - a transformation based on a record of achievement and confidence about the future. Over the twelve months to the first quarter of this year, both manufacturing and services' output grew by more than 4%, and manufacturing has risen further in April and May. Output in the construction industry - a key indicator of firms' confidence in the future - grew by nearly 12%. And a higher proportion of manufacturers are expecting output growth to continue over the next four months than at any other time since the CBI began to collect this information in its present form, over 10 years ago.

4. A further sign of industry's confidence in the future is the DTI's investment intentions survey, which indicates a rise of about 8% in real terms in industrial investment in 1987, and a similar one in 1988. The rate of growth of new businesses is also striking, with net business startups averaging 550 per month between 1980 and 1986.

5. Although the main international institutions are revising down their forecasts for other industrial economies, they have revised up their forecasts for the UK. They share our confidence that the growth of our economy will be sustained - even in the face of a slowing down of world growth generally.

6. For five years now, growth in the UK has been combined with low inflation. During last year, inflation reached its lowest level for almost twenty years. And it is increasingly accepted that inflation is set to stay low. We shall not let up in the fight against inflation which is at the heart of our economic strategy.

X 7. High growth and low inflation are now also being accompanied, at last, by a significant ^{fall in unemployment} ~~improvement in the labour market~~. Figures released last week showed that employment has now grown every quarter for four years, and unemployment has fallen every month for a year, and by a record amount. Indeed, the fall in the unemployment rate over the last year is faster than in any other major industrial country. And it is not just the official statistics that show that since 1983, the UK has created over 1 million jobs - more than the rest of the EC put together - it is also clear from newspapers all over the country, which have pages full of job advertisements.

8. But while we are reaping the benefits of this unparalleled record of achievement, we must hold firm to ^{the} disciplines which were needed to bring it about in the first place, and are still vital to ensure continued success. We have shown that steady sustained growth can be achieved in the long run only by strengthening the

supply side of the economy and liberating the enterprise and productive potential of the British people. We have achieved this by firm control of public expenditure, by containing the public sector's demands on the country's resources, by reducing controls, by releasing enterprises from the shackles of state control, by encouraging the spread of wealth and ownership and thereby promoting the sense of freedom and personal responsibility which gives people a real incentive to work harder for themselves and for their families.

9. Tax reform has had a vital part to play in this process. The measures already implemented in the Finance Act, together with those before us today, continue the key themes which we have pursued since 1979. The major objective is tax reduction to allow people to keep more of their own money to spend or save as they wish and to allow companies to keep more of their own profits. We have reduced the basic rate of tax from 33 per cent to 27 per cent and we are committed to reducing it further as soon as we can prudently do so. Our main rate of corporation tax is now among the very lowest in the industrial world. Hand in hand with tax reduction, we have reformed and simplified the tax structure to reduce distortions, to lighten the administrative burden and promote fair competition.

10. The future prosperity of the economy depends critically on continuing this process of tax reduction and reform. We must sustain the conditions for continued growth to create more jobs and support the improvements in public services we all want to see. But this will be possible only if we exercise continued restraint in public spending in order to make room for further reductions in the burden of tax. Success does not remove the need for tough decisions.

11. The Bill before us today contains a number of measures designed to continue the programme of reform which I have outlined above. ~~In particular~~ I will discuss ~~in detail~~ the measures designed to improve the flexibility of the economy, to promote greater personal choice and to improve further the system of corporation tax.

*It will not be possible to mention all the Bill's clauses
but*

PROFIT RELATED PAY

12. Noble Lords will recall that I spoke, in the Finance Bill second reading debate almost exactly a year ago, about the Green Paper on profit related pay which was presented to Parliament jointly by the Chancellor, my predecessor as Secretary of State for Industry and myself as Secretary of State for Employment. I spoke then about the need for wider adoption of profit related pay to help break down the "them and us" barrier which has bedevilled British industry for years. I am very glad indeed to report that following the consultation period, we have decided to go ahead with this worthwhile new scheme to encourage the extension of profit related pay throughout the economy.

13. This is a scheme which builds on success. Many successful companies already have schemes which give employees a direct stake in the future of their company through share ownership. A record number of all employee share schemes were approved by the Inland Revenue in the year to June 1987 - a further 210 schemes bringing the total to 1,313. And there is a growing recognition of the importance of cash-based profit sharing, or profit-related pay, which owes something to the success with which such arrangements are already applied by some employers, and something to the interest which has been aroused by the development of our own proposals over the last 18 months.

Importance of pay flexibility

14. Improving the flexibility of the labour market is a vital part of our strategy to improve the supply performance of the economy, and thus increase the prospect for output and jobs. We have recently seen record falls in unemployment, and record levels of unfilled vacancies. But if unemployment is to come down more quickly, as we all wish, if there are to be more real jobs in the future for the unemployed and those entering the labour market, and if the new jobs which are being created are to be secure, we need to rise to the challenge of helping to reform and remove rigidities of the labour market. One part of that, but a critical part, is to

improve the ways in which our pay systems operate. Although there are some welcome signs of change, the rigidity of pay and the systems which determine it are still perhaps the greatest problem which our economy faces. We do not claim that PRP is a panacea. We do not believe in panaceas. And we reject the notion that markets can be made to work better through more bureaucratic interference, whether it be on incomes policy, or a national social contract, or call it what you will. But, if employers are ready to respond to the problems, and if Parliament is ready to support Government measures to assist them, that can make a vital contribution to tackling the problems, and making our economy better fitted to the fast changing and more competitive international markets of tomorrow.

Advantages of PRP

15. In essence, PRP is very simple. A part of employees' cash pay is formally linked in value to the profits of the business in which they work. Other things being equal, higher profits will lead to higher pay, and lower profits will mean that total pay is temporarily lower than it would otherwise have been. This means that employees have a direct stake in the success of the business. It means higher pay, if that has been earned by higher profits, and that is a route to higher living standards which can be sustained. If business conditions are difficult it means greater job security. For the employer a PRP scheme can mean a more committed work force with better incentives to profitability and productivity. It means that if times are difficult and profits fall, part of the necessary strain may be taken by a temporary fall in pay, perhaps as an alternative to redundancies. That extra flexibility helps to make output more secure helping the business to ride the difficulties and putting it in a better position to recover, and to improve pay levels again. And that can also lead to more certainty and less caution about hiring extra labour to increase output when prospects look good.

Operation of PRP

16. The conditions for eligibility to operate the tax relief may look complex, but that is because they contain a great deal of

flexibility for schemes to be tailored to the circumstances of individual business risks. The rules are not incompatible with a simple PRP scheme which is easy for employees to understand. Rather, they allow for a simple scheme to take a number of forms. Our proposals have been informed at all stages by the widest possible public consultation, and detailed discussions with practitioners. We believe we have got the balance between simplicity and flexibility right. Clear Guidance Notes will be issued by the Inland Revenue in September.

Challenge to employers

17. Essentially PRP is about two things: first employee identification with the success of the company, and second pay flexibility which is vital to any company's competitive performance. The measures introduced in this Bill will give workers a valuable tax relief worth up to the equivalent of 4p off the basic rate. PRP will send strong signals throughout ~~the~~ business unit, ^{and these signals} which could in the long run have a profound effect on industrial relations and management in this country ~~today~~. The scheme is a challenge to employers throughout Britain. 20,000 have already established their interest with the Inland Revenue, including 120 out of our top 250 companies. I very much hope that this number will grow once the tax relief has been enacted, and that they will follow this up and take advantage of the relief which is on offer to use it as a tool to help them install PRP schemes. Thus output, employment and productivity can rise and the whole economy can benefit.

PENSIONS

18. The largest group of clauses in the Bill^x contain important and far-reaching changes for private pensions. The objectives are to widen individual choice, to encourage job mobility and, to ensure a fairer deal for the taxpayer.

⁹
18. Much has already been done to widen the pensions choice. Many employers have established occupational pension schemes for their staff, with the help of generous tax reliefs. At present, over 10 million people are currently members of occupational schemes.

But more can be done. There are still some 10 million employees who are not in an occupational scheme and who make no private provision for retirement. A central feature of our strategy is to bring private pensions within the reach of these employees for two reasons: to provide them with a pension of their own and to increase their independence of the State.

Personal pension schemes

2019. The new personal pensions will be available to all employees who are not in an occupational scheme; to the minority of employees who choose to opt out of their occupational scheme; and to the self-employed.

20. These schemes will be available from next January. The legislation is based on the present, broadly similar, retirement annuities provision but, in addition to being brought up to date, the new measures incorporate a number of new features which have been widely welcomed. The 1986 Social Security Act enables employees to contract-out of the Additional Component of the State Scheme through a personal pension. The Finance Bill provides the necessary tax procedures to achieve this result.

Wider range of providers

21. In addition, the Bill enables a much wider range of pension providers to establish personal pension schemes. As well as insurance companies and friendly societies, the field will be open to banks, building societies and unit trusts.

Additional voluntary contributions

22. The Bill also contains provision to allow members of occupational schemes to make additional voluntary contributions to a pension plan completely separate from their employer's scheme, up to the tax approval limits on contributions and benefits. This development has been widely welcomed and, taken together with the other changes, will dramatically increase the choice of how to provide for retirement.

Job Mobility

24. A further purpose of our reforms is to remove - as far as possible - the pension obstacles to job mobility. The House will be aware of the 'early leaver' problem; the person who changes jobs in mid-career and whose pension expectations are in consequence much reduced. There is no quick and easy solution to this problem. But the very existence of the new pension opportunities I have just described will - together with much greater transferability of pension rights - greatly reduce its worse impact.

25. The changes we have proposed do not increase the already generous tax regime for retirement provision, but simply extend it potentially to every employee. I believe these reforms will greatly improve the pension position and the freedom of choice of all employed and self-employed people in this country.

Exploitation of tax reliefs for pensions

26. But the improvements we propose can be justified only if the tax reliefs for pensions are not abused. We have felt it necessary to impose some limited restrictions, to guard against misuse of the tax reliefs - particularly by a small number of very high earners. The tax rules for pensions were never intended simply as a tax-sheltered medium for investment generally - with scope for the postponement (and for lump sums, complete elimination) for a tax liability.

27. These restrictions will have no impact whatever on the vast majority of pension scheme members: for ordinary working people the scope for abuse has never been available. But for a few highly paid people, the new rules will ensure that the tax reliefs are used only for their originally intended purpose.

28. The measures I have outlined comprise some of the main changes in a continuing process of pensions reform which was initiated by my Right Honourable Friend, the previous Secretary of State for Social Services over three years ago. The proposals in this current Finance Bill build on, and extend, the changes made in

recent Social Security legislation, and provide a better pension deal for millions of employees - and the self-employed - in this country.

29. The Bill contains a number of clauses dealing with the taxation of companies which I would like to draw to the attention of the House. These are designed to promote further the principles of simplicity, fairness and effectiveness which underlay the major reforms of the corporation tax regime which we introduced in 1984.

Lloyd's.

30. 29 Noble Lords will be aware that one of the main points of debate on the Bill in the other place related to its provisions on the tax treatment of Lloyd's reinsurance to close arrangements. The legislation is necessary to ensure that the amount of the reinsurance to close premium can be properly scrutinised for tax purposes. The original proposals in the April Finance Bill have been revised in the light of discussions with Lloyd's. In its revised form, the Clause provides a free-standing test for tax deductibility, which takes full account of the special nature of the Lloyds RIC arrangements. It meets the concern which Lloyd's expressed about the proposals in their original form. The Chairman of Lloyd's has said that Lloyd's regard the Clause as "workable and acceptable".

Pay and File

31 30. The Bill puts in place a new system of accounting for and paying corporation tax known as Pay and File, will make life a lot easier for companies of all sizes. In 1984 we initiated radical changes to the structure of corporation tax, with a phased withdrawal of outdated tax reliefs linked with a staged reduction of tax rates. The new Pay and File system, which follows on from recommendations of the Keith Committee, will add an efficient and modern administrative system for collecting the tax. It does away with the present antiquated rules and the inefficient practices which have developed out of them. It replaces those rules with a proper

legal framework under which taxpayers will have clear rights and responsibilities. We have consulted widely with the business community which has generally welcomed the new system. Pay and File will mean major changes for the revenue, the taxpayers and for tax practitioners. It cannot be introduced until 1992, but we are legislating now to allow sufficient time for all those affected to make the necessary changes to their operating systems.

Companies' capital gains aligned with CT rates

- 32 31. The Bill also contains a measure to streamline the taxation of companies' capital gains. These gains will now be taxed at normal corporation tax rates, and qualify for set off of advanced corporation tax. Now that we have brought the main corporation tax rate down from 52 to 35 per cent we see no justification for a different rate on capital gains. This is a useful simplification removing the need for the present complicated adjustment. For the X per cent of companies who pay at the small companies' rate the rate of tax on gains will fall from 30 to 27 per cent.

Life assurance policyholders' gains

33. The change will not, however, apply to the gains which life assurance companies earn for their policy holders. The Government received a number of representations about the affect on the life assurance industry of taxing policy holders' gains at normal corporation tax rates. My right honourable Friend the Chancellor considered this issue very carefully and concluded that it was time to take a general look at the tax arrangements for life assurance as they have now developed. There will be full opportunity for the life assurance industry and other interested parties to contribute to the review. In the meantime, the tax rate on gains earned for policy holders will remain at 30 per cent pending the outcome of the review.

Stopping unjustified loopholes

34. As part of our continuing programme of tax reduction and tax reform we intend to eliminate unintended or unjustified tax reliefs,

which can give some companies an unfair competitive advantage and cause tax rates for the majority of taxpayers to be higher than they would otherwise need to be. The Bill contains a number of clauses designed to meet this objective. For example we did not think it right that companies in multinational groups which enjoy dual residence should secure tax relief twice on one and the same interest payment. A further clause ensures that the controlled foreign companies legislation is not side-stepped by moving the residents of the foreign company to the United Kingdom before payment of a dividend. In respect of the clauses dealing with double taxation relief on interest on certain overseas loans, we received a number of representations from the banks. In the light of these we have decided to double - to 1 April 1989 - the transitional period before the new provision takes effect for loans which were already in existence on 1 April this year.

CONCLUSION

35. The measures before us today complete the programme of reforms announced in my Rt Hon Friend's Budget. These build upon our solid record of achievement in tax reform which has set an international trend. The Bill contains important measures which will further our objectives of increasing flexibility and freedom and promoting simplicity and fairness in the tax system. The programme of tax reduction and reform will continue as a vital part of our strategy to liberate the energy and enterprise of the British people.



CC

PPS

CST

PMG

EST

MR Scholar

MRS LOMAX

Miss Sinclair

MR Ilett

MR Nelson

MR Cropper

MR Munro IR

PS/R

Treasury Chambers, Parliament Street, SW1P 3AG

Judah C Sommer Esq
Goldman Sachs & Co
Suite 450
1825 Eye Street NW
WASHINGTON DC 20006
USA

20 July 1987

Dear Mr Sommer

I am sorry for the long delay in replying to your letter of 3 June about what was Clause 68 of the Finance Bill. As I am sure you will be aware, this provision has now been reintroduced as Clause 81 of the new Finance Bill.

You express disappointment that the Clause does not extend to pension fund transactions in 'over the counter' traded options and futures. But this clause is a general provision relating to the capital gains tax treatment of 'over the counter' options and futures. In contrast, you are concerned about a specific problem relating to the income tax and capital gains tax position of one type of institution - ie. a pension fund - if it should engage in transactions in such options and futures.

The question is whether options and futures are investments held for the purposes of the pension scheme. If so, income arising from them will be exempt from tax by virtue of section 21(2) Finance Act 1970. Section 21(7) provides for a capital gains tax exemption on the same basis.

Section 45 Finance Act 1984 amended the law to enable certain futures and options to be regarded as 'investments' for Section 21 Finance Act 1970. This covered all financial futures, whether or not they are traded on a recognised exchange, and traded options provided they are quoted on a recognised stock exchange or LIFFE. So options quoted on some other financial futures exchange or traded 'over the counter' are not regarded as 'investments'.

If any extension were to be made to Section 45, Finance Act 1984, separate legislation would be required. There is clearly no prospect of an amendment to the current Finance Bill but I should certainly be willing to consider - without commitment - any representations for such an amendment in a future year.

Yours sincerely
Norman Lamont

NORMAN LAMONT

FINANCE BILL, as amended

Consideration of Bill

Mr Speaker's Provisional Selection of Amendments

NC1

NC3

By Order of Mr Speaker

20 July 1987

Confederation of British Industry
Centre Point
103 New Oxford Street
London WC1A 1DU
Telephone 01-379 7400
Telex 21332
Facsimile 01-240 1578

From
John M M Banham
Director-General

CBI

13 July 1987

JMMB/RHP

The Rt Hon Norman Lamont MP
Financial Secretary
HM Treasury
Parliament Street
LONDON
SW1P 3AG

FINANCIAL SECRETARY	
REC.	20 JUL 1987
ACTION	MR Munro IR
COPIES TO	PB CST PMB EST
	MR Scholke
	Miss Pearson
	MR Haugh MR Cropper
	MR Tyrie PS/IR

Dear Norman

We have now had the opportunity to consider the summer Finance Bill following its publication on 3 July. Our members are most disappointed that the Government have not felt able to take account of the views expressed in my letter of 1 May to the Chancellor concerning occupational pension schemes.

The two changes to existing arrangements which have aroused most opposition are the proposal to end the right to commute benefits derived from occupational additional voluntary contribution (AVC) arrangements for all but existing contributors and the proposed new limits on accelerated accrual of pension benefits. These changes would introduce new rigidities into the labour market, discouraging those employees already making AVCs or currently in the process of qualifying for accelerated accrual of benefits from changing jobs. Disincentives to mobility and/or additional business costs would be most unwelcome by-products of the changes you are proposing.

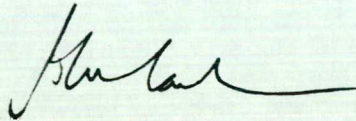
It would be particularly inequitable to remove the right to commute benefits built up through occupational AVC arrangements in the private sector whilst at the same time allowing this right to members of personal pension arrangements and of some public sector pension schemes. Moreover, for most members of occupational schemes, the provision of a lump sum at retirement represents the best opportunity they will ever enjoy to have access to a modest capital sum. It is a valued feature of nearly all occupational, including AVC, pension arrangements. In the future, individuals prevented from commuting their AVC benefits might choose instead to commute their basic scheme benefits. This would in most cases be to their, and their dependents', disadvantage as AVC benefits are not usually given the same level of protection as are basic scheme benefits.

The/

The new restrictions on accelerated accrual will act as real deterrent to mobility between occupational pension schemes. Members believe that the proposals will give rise to anomalies; for example, employees who change jobs late in their careers will be put at a very real disadvantage compared with those who move early.

Members appreciate that both these proposals are intended to curb what are perceived as instances of abuse of the tax privileges attached to pension provisions. They do, however, feel that the response is out of scale to the problem and will have very considerable adverse impact at a time when the Government and the CBI are seeking to remove barriers to mobility. I hope that, even at this late stage, you will think again about the implications of your proposals.

Yours sincerely

A handwritten signature in dark ink, appearing to read 'John M M Banham', with a long horizontal flourish extending to the right.

John M M Banham



28

FROM: N WILLIAMS
DATE: 20 July 1987

MR CAYLEY IR

cc PS/Chancellor
Mr Scholar
Mr Cropper
Mr Dyer
Mr Houghton IR
PS/IR

SUMMER FINANCE BILL: REPEAL SCHEDULE

1. The Financial Secretary was grateful for your minute of 17 July.
2. This is to confirm that he is content with the draft Question and Answer attached to your minute.
3. I have arranged with Parliamentary Section that the Question will be tabled on 22 July for answer on 23 July.

A handwritten signature in black ink, appearing to read "Nigel Williams", with a long horizontal flourish extending to the right.

NIGEL WILLIAMS
(Assistant Private Secretary)



Handwritten initials

FROM: N WILLIAMS
DATE: 21 July 1987

MISS C EVANS

cc PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Mr Scholar
Miss O'Mara
Mr Gray
Mr Dyer
Mr Hudson *GH*
Mr Walker IR
Ms French C&E

FINANCE BILL: LORDS SECOND READING: 23 JULY

1. The Financial Secretary was grateful for your minute of 17 July.
2. This is to confirm that the Financial Secretary was content with the material which you have now sent to Lord Young's office.

Handwritten signature: N Williams

NIGEL WILLIAMS
(Assistant Private Secretary)



18

FROM: N WILLIAMS
DATE: 21 July 1987

MISS C EVANS

cc PS/Chancellor
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Mr Scholar
Miss O'Mara
Mr Gray
Mr Dyer
Mr Hudson
Mr Walker IR
Ms French C&E

FINANCE BILL: LORDS SECOND READING: 23 JULY

1. The Financial Secretary was grateful for your minute of 17 July.
2. This is to confirm that the Financial Secretary was content with the material which you have now sent to Lord Young's office.

NIGEL WILLIAMS
(Assistant Private Secretary)



FROM: J J HEYWOOD
DATE: 21 July 1987

PS/CHAIRMAN

cc **Principal Private Secretary**
PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Mr Scholar
Mr Bradley
Mr Dyer
Ms Evans
Mr Guy
Mr Cropper
Mr Isaac IR
Mr Painter IR
Mr Bryce IR
Mr Cayley IR
Mr Draper IR
Mr Driscoll IR
Mr Farmer IR
Mr Fawcett IR
Miss Hill IR
Mrs Hubbard IR
Mr Johns IR
Mr Munro IR
Mr Shaw IR
Mr Spence IR
Mr Sullivan IR
Mr Thompson IR
Mr Walker IR
PS/C&E

FINANCE BILL (No 2) 1987

1. The Financial Secretary would like to thank copy recipients and their technical and other colleagues who worked so hard, both in the House and behind the scenes, to ensure the successful passage of the Finance Bill through its Commons stages.

2. The Financial Secretary is very grateful indeed for the tireless and consistently excellent support he and colleagues have received over the last few busy weeks.

9.11

JEREMY HEYWOOD
Private Secretary

FROM: MISS C EVANS
DATE: 22 JULY 1987

MR WALKER - FAX

cc PS/Chancellor 12/2
PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary

Mr Scholar
Miss O'Mara
Miss Sinclair

Mr Guy
Mr Dyer
Miss Simpson
Miss French C + C (Fax)

LORDS SECOND READING: 23 JULY

I understand that the following Lords are down to speak in tomorrow's debate. I should be grateful if you could do a Revenue trawl to discover what is known about their special interests. Perhaps we could then discuss what further briefing is needed.

Lord Banks

Lord Houghton of Sowerby (ex IRSF)

✓ Lord Bruce of Donnington (VAT injection proceedings?)

Lord Bruce Gardyne

Lord Graham of Edmonton

Lord Boyd Carpenter

2. In view of Lord Houghton's IRSF connections do we need any defensive briefing on IR manpower issues?

CE

MISS C EVANS

UNCLASSIFIED

purp.



FROM: N G FRAY

DATE: 22 July 1987

PS/PAYMASTER GENERAL

FINANCE BILL: 20 JULY 1987

The Chancellor has read Hansard for 20 July and congratulates the Paymaster General on a splendid speech.

Nigel Fray
N G FRAY



OP

CC PPS

CST
EST

MR CASSELL

MRS LOMAX

MR SCHOLAR

MR Haigh

MR Cripps

MR Spence JR

MR M. Hewitt (BOE)

MR Muir (DTI)

MR Jenkins (GPC)

Treasury Chambers, Parliament Street, SW1P 3AG

Sir William Clark MP
House of Commons
LONDON
SW1A 0AA

22 July 1987

Law Bill

In the course of the debate at Committee on Clause 70 you raised one point which I said I would consider. As you said, the effect of subsection 2 and subsection 3 in combination is that if some of the RIC is disallowed there will be a corresponding reduction in the taxable receipt of the members of the syndicate in year 2. You suggested this would produce an anomalous result where someone left the syndicate and was replaced (in the new syndicate) by somebody else, because the old name has to pay tax and the new name saves tax. (Hansard, 15 July, Column 1195 and - again - Column 1196).

I can see that - on this simple example - there might seem to be something of an anomaly. In practice - as I know you recognise - the position is more complicated. One consideration is that most Lloyd's names are members of a number of syndicates, and a member who left one syndicate at the end of the year would normally join another syndicate instead. The whole issue was, in fact, thoroughly gone over in the discussions between the Revenue and Lloyd's. At the time, Lloyd's came to the view that, whatever the theoretical anomaly of the present position, any attempt to remedy it would produce complexity and anomalies which would be rather larger in scale. We had, independently, come to the same view. Lloyd's decided not to pursue the point, and we agreed that the idea of some special treatment for those who leave and join syndicates should be dropped.

Subsequently, Lloyd's have said that they would like to discuss this matter further with the Inland Revenue. I am, of course, quite ready for these discussions to take place, though as I am sure you will understand, I cannot commit myself to further legislative action on RIC.

Yours faithfully
Norman Lamont

NORMAN LAMONT



28

FROM: FINANCIAL SECRETARY
DATE: 22 July 1987

MR MUNRO IR

cc Principal Private Secretary
Sir P Middleton
Mr Battishill IR
Mr Isaac IR
Mr Corlett IR

FINANCE BILL (No 2) 1987

1. Could I just thank you for all the support and briefing that you have provided during the course of the Finance Bill. It became quite a prolonged session on pensions and I am very grateful to you for your hard work.

NORMAN LAMONT