PO-CH/NL/0037

PART B

SECRET

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PO -CH /NL/0037

PART B

1986 BUDGET EXCISE DUTY OPTIONS ON ALCOHOLIC DRINKS TOBACCO AND FUEL

DD'S 25 years 2-02-95 N.Agg

PO -CH /NL/0037

PART B

STARTS:-19-03-86

THE SCOTCH MALT WHISKY SOCIETY
THE VAULTS · LEITH · SCOTLAND

PSC thanks dividends re.

The Right Honorable Nigel Lawson P.C.M.P.
The House of Commons
Westminster
London

19th March 1986

Dear Sir,

We appreciate the help you have given the whisky industry with this budget and in particular the fastest growing section which is malt whisky.

As a young company (two and a half years old) this will particularly help us in the home market and with strong trading here we can start exporting.

The enclosed bottle is a small mark of our appreciation, we do hope you enjoy it, it is a Longmorn Glenlivet 13 years old.

Yours faithfully,

[signature]

pp. J L G LAMOTTE
CHAIRMAN

pp. signed in his absence.

THE VAULTS · LEITH · 87 GILES STREET · EDINBURGH EH6 6BZ · (031) 553 1003

THE SCOTCH MALT WHISKY SOCIETY LIMITED. REGISTERED NUMBER 83022, REGISTERED OFFICE, THE VAULTS LEITH.

Gmp

SECRET

CMO 19 MARCH 1986

ECONOMIC STRATEGY

Memorandum by the Chancellor of the Exchequer

1. The approach to the 1986 Budget is inevitably dominated by the dramatic changes taking place in the oil market. The large price fall that has already occurred means a sharp reduction in prospective oil tax revenues.

2. The current North Sea oil price of $17-18 per barrel is some 40 per cent below the end-November level - a change almost as great as the price increases of 1973 and 1979. It is hard in current circumstances to make a reliable judgement about the new level at which oil prices may settle. We therefore have to consider the Budget against the prospect not merely of greatly reduced oil revenues but also considerable uncertainty about how large the reduction will be.

3. Our current estimates suggests that if oil prices settle at $15 a barrel our revenues from the North Sea will be reduced to £6 billion for the next financial year. This compares with receipts of £12 billion in 1984-85. In last year's Medium Term Financial Strategy (MTFS) we expected revenues of £11½ billion for 1986-87.

4. There has inevitably been some turmoil in financial markets as they have responded to the oil price change. Sterling has fallen by about 7½ per cent and there has been persistent upward pressure on short term interest rates. So far we have weathered the collapse in oil prices and consequent financial market turbulence pretty well - though it may not be over yet. In so doing we are helped both by the underlying strength of the economy, in terms of growth, inflation and the external account; and above all by the reputation we have acquired for sound and prudent policies.

Fiscal position

5. Faced with this background my judgement is that we must approach the Budget with considerable caution. We must avoid going above the £7½ billion Public Sector Borrowing Requirement (PSBR) figure set out in last year's MTFS. Indeed there is a strong case for going below it, bearing in mind the proceeds of privatisation, estimated at £4¾ billions next year.

6. Much may change between now and Budget Day. Because non-oil revenues are now projected to be higher than expected I hope to be able to avoid a net increase in taxes in the Budget. But there looks like being little, if any, scope for a net reduction in taxation. We should just meet the public expenditure planning total set for the current financial year. The need to cope successfully with the unprecedented situation which the oil price fall has created for the public finances underlines the importance of holding public spending next year similarly within the planning total we have announced.

Economic prospects

7. But while lower oil prices have a profound impact on what is possible in the Budget, they should not greatly affect our overall economic performance - although there will be significant changes <u>within</u> the economy. For the world as a whole, lower oil (and commodity) prices will have beneficial effects in 1986 on the oil-consuming countries. The forecast for the major industrialised countries is for output growth averaging 3 per cent - a little better than achieved last year. Inflation will stay low: indeed in Germany and Japan it is likely to approach zero.

8. For the UK, the oil price fall has not caused me to revise my view that 1986 will be a further year of steady growth, at an annual rate of about 3 per cent, accompanied by declining inflation. Different parts of the economy will be affected in different ways by lower oil prices. While the oil sector

will not do so well, manufacturing industry in particular should benefit considerably.

9. The UK economy is now in a stronger position to take advantage of the opportunities created by lower oil prices. The underlying improvement shows up in a number of indicators. Last year manufacturing productivity increased by a further 4 per cent. Since 1979 it has now grown at an average annual rate of 3¾ per cent. As the table below shows, our performance here compares very favourably with the recent past; and even with the majority of our principal overseas competitors.

Output per man hour in manufacturing
average annual growth rates, per cent

	1973-79	**1979-85**
US	1½	2½
Japan	6½	6½
Germany	3	3
France	5	3½
UK	1	3¾

10. Capital spending by business has generally been rising faster than output in recent years and further growth is expected in 1986, as a response to higher profits and continued expansion in output. Exports performed well in 1985: indeed, UK exporters increased their share of world trade. The prospect is for continued export growth, albeit at a slower pace. Even after the fall in oil prices, another sizeable current account surplus is in prospect for 1986, helped by rising earnings from our increasing stock of overseas assets. (Our net overseas asset position is now second only to that of Japan).

11. This year is likely to see a significant rise in consumer spending. This reflects rapid growth in real disposable incomes - itself a result of the high level of wage settlements in 1984 and 1985 and the reduction in inflation expected this year. Earnings are currently rising at or over 7½ per cent.

With inflation likely to fall to 4 per cent this year, the average employee's pay may rise by some 4 per cent in real terms during 1986.

12. However, this excessive earnings growth remains the chief threat to jobs. Despite five years of continuous output growth, and a growth in the number of people in work of over 600,000 since the last election, which I expect to continue, unemployment is unlikely to show much of a reduction while wages rise so far ahead of prices. The plain fact is that, despite our very good productivity record, UK unit labour costs have been increasing much more rapidly than those of our competitors.

13. Annex 1 sets out key figures from the forecast. Annexes 2 and 3 set out the revenue effects of selected tax changes, together with a note on the tax burden.

Summary and conclusions

14. The dramatic change in oil prices has had a major - and adverse - impact on the public finances; but I very much hope that, thanks to the sound financial policies we have been following, it will prove possible to avoid raising taxes overall in the Budget. The impact of lower oil prices on the UK economy as a whole is more neutral. I expect to see continuing steady growth for the sixth year in succession; and lower inflation. This is a measure of the strength of our underlying economic performance.

15. I seek colleagues' views on the appropriate shape of the Budget in the light of the circumstances I have outlined.

N.L

SECRET

ANNEX 1

SELECTED ECONOMIC INDICATORS

	1979	1980	1981	1982	1983	1984	1985	1986 (1)
World GNP, in major 7 economies (per cent change) (2)	3½	1	1½	- ½	2½	4½	2½	3
UK GDP, (per cent change) (2)	2½	- 2½	- 1½	2	3½	2½	3½	3
Domestic demand, (per cent change) (2)	4	- 3½	- 2	2½	4½	2½	2	3½
Retail prices Q4 (per cent change)	17½	15½	12	6	5	5	5½	4
Interest rates (average 3-month interbank)	13½	16½	14	12½	10	10	12	13 (3)
Current balance (£ billion)	- ½	3	6	4	3	1	3½	3½
Unemployment (UK, per cent excluding school leavers)	5	6	9½	11	12	12½	13	13 (4)
Sterling Index	87	96	95	90½	83	78½	78	74½ (3)
Oil prices, $, North Sea	20½	34½	37½	33	30	29½	27½	17½ (5)

(1) Provisional pre-Budget figures.

(2) At constant prices.

(3) February 7.

(4) Not a forecast. Figures based on assumptions in PEWP.

(5) Brent price for delivery in March, as of February 7.

ANNEX 2

REVENUE EFFECTS OF TAX CHANGES

A. Direct Taxes: Indexation

The RPI increased in the year to December 1985 by 5.7 per cent. With indexation by this amount and statutory rounding, the figures for the main allowances and other thresholds would be:

Personal allowances	1985-86 £	1986-87 £
Single and wife's earned income allowance	2205	2335
Married allowance	3455	3655
Bands eg		
30% rate	0-16200	0-17200
60%	over 40200	over 42700

The total revenue costs of indexation of income tax (reflected in the forecast) are £1140m in 1986-87, and £1490m in a full year, at forecast 1986-87 prices and incomes.

B Indirect Taxes: Indexation

The effects of 5.7 per cent revalorisation of the exercise duties (including VAT effects, price changes rounded) are as follows:

	Typical Price Change	Revenue effect (1986-87 prices) £m	RPI impact £m
Beer	1p/pint	100	0.07
Wine	5p/70cl light wine	20	0.02
Spirits	31p/bottle	45	0.04
Tobacco	5p/20 King size	150	0.14
Petrol	5p/gallon	260	0.13
Derv	5p/gallon	65	nil
VED	£5/car	100	0.05
Overall effect (reflected in forecast)		740	0.45

Note: First year and full year revenue effects are virtually identical.

C. Ready Reckoner: Illustrative Tax Changes

£ million at forecast 1986-87 income levels

	1986-87	Full Year
INCOME TAX		
Allowances and Thresholds		
1% above indexation on all statutory allowances	210	175
1% above indexation on all statutory allowances and thresholds	245	190
Rates		
Change basic rate by 1p	1175	975
CORPORATION TAX		
Change main rate by 1 percentage point	180	310
Change small companies' rate by 1 percentage point	16	30
OTHER TAXES		
Change VAT rate by 1 percentage point(1)	700(2)	925

(1) A 1% change in the VAT rate would change the RPI by 0.5%.

(2) Provisional forecast

ANNEX 3

THE TAX BURDEN

Since the Government came to power total taxes and NICs as a proportion of GDP at market has risen by about 5 percentage points, though the ratio has fallen slightly since 1981-82. The figures are as follows:

Table 1

Total taxation* as a % of GDP (market prices)	
1978-79	33.9
1979-80	35.2
1980-81	36.4
1981-82	39.3
1982-83	39.1
1983-84	38.6
1984-85	39.2
1985-86 (estimate)	38.7
1986-87 (assuming indexation)	38.6

* Including NICs and the local authority rates.

Personal sector

2. Despite reductions in income tax, total personal taxes (direct and indirect, including employees' NIC and domestic rates) in 1985-86 are about £15 billion higher in real terms (ie 1985-86 prices) than they were in 1978-79. For income tax and national insurance contributions the following table shows how the proportion of gross pay they represent has risen, particularly for the low paid:

Table 2

Income tax and NICs as a % of gross earnings*

	½ average earnings	Average earnings	2 average earnings
1978-79	16.0	27.8	31.4
1981-82	20.8	29.3	32.2
1982-83	20.8	29.8	32.3
1983-84	20.1	29.6	31.7
1984-85	19.3	29.2	31.5
1985-86 (estimate)	19.0	29.0	31.5
1986-87 (indexation)	19.3	29.1	31.7

* Adult male earnings (all occupations). Married couple, wife not working: the couple are assumed to have no children, to avoid distortion of the figures from the abolition of child tax allowances.

3. These figures reflect the rise in the standard employees' NIC rate from 6½% to 9%. The lower rates introduced in the 1985 Finance Act do not affect the cases shown. So far as income tax is concerned, personal allowances have increased by over 19% in real terms since 1978-79 and have increased slightly faster than earnings. The basic rate has been reduced from 33p to 30p, but the 25p reduced rate band has been abolished.

4. As the table shows, indexation of allowances in the Budget would lead to a very slight rise in the proportion of incomes taken in tax and NIC. This is because earnings are assumed to rise by 7% compared with the indexation percentage of 5.7%.

5. Since 1978-79 total taxes paid by businesses (outside the North Sea) have fallen slightly as a percentage of GDP. Within this total, the major change has been a fall in employers' NIC and NIS as a percentage of GDP, partially offset by an increase in business rates, and 'other' taxes as the following table shows:

Taxes paid by businesses £bn in 1985-86 prices
(figures in brackets are %s of GDP)

	Corporation tax[1]	Taxes on self employment incomes	Employers' NIC and NIS	Rates	Other[2]	Total
1978-79	7.1	2.4	9.9	4.7	3.7	27.7
	(2.2)	(0.7)	(3.1)	(1.4)	(1.1)	(8.6)
1985-86 (estimate)	8.2	3.1	8.0	5.9	4.8	30.0
	(2.3)	(0.9)	(2.2)	(1.7)	(1.4)	(8.4)

1. Excludes North Sea, but includes ACT
2. VED, car tax, road fuel duty, duty on rebated oils, capital taxes.

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3. These figures reflect the rise in the standard employees' NIC rate from 6½% to 9%. The lower rates introduced in the 1985 Finance Act do not affect the cases shown. So far as income tax is concerned, personal allowances have increased by over 19% in real terms since 1978-79 and have increased slightly faster than earnings. The basic rate has been reduced from 33p to 30p, but the 25p reduced rate band has been abolished.

4. As the table shows, indexation of allowances in the Budget would lead to a very slight rise in the proportion of incomes taken in tax and NIC. This is because earnings are assumed to rise by 7% compared with the indexation percentage of 5.7%.

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BR/010

SECRET

LW spoke.

Pl. let me know if happy OK - this needs to go to No 10 under a PS letter. (I have a copy so phone any changes)

ECONOMIC STRATEGY

Memorandum by the Chancellor of the Exchequer

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Fiscal position

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~~[illegible]~~ 4½ bn
[illegible] £4¾ bn

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12. However, this excessive earnings growth remains the chief threat to ~~unemployment~~ jobs. Despite five years of continuous output growth, and a growth in ~~employment~~ the number of people in work of over 600,000 ~~since the summer of 1983,~~ since the last Election, which I expect to continue, unemployment is unlikely to show much of a reduction while wages rise so far ahead of prices. The plain fact is that, despite our very good productivity record, UK unit labour costs have been increasing much more rapidly than those of our competitors.

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N.L

 ORA: 1987

273/001

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Memorandum by the Chancellor of the Exchequer

1. The approach to the 1986 Budget is inevitably dominated by the dramatic changes taking place in the oil market. The large price fall [that has taken place means a sharp reduction in prospective oil tax revenues] ~~has implications for the financial markets, public finances and prospects for the economy~~.

2. The current [N Sea oil] ~~Brent~~ price of [$16-17] per barrel is [some] ~~almost~~ [45] ~~50~~ per cent below the end-November level. ~~This~~ [a] change ~~is~~ almost [as great] ~~of the same order of magnitude~~ as the price increases of 1973 and 1979. ~~As we know from those experiences, the results of a shock of this magnitude are difficult [not easy] to predict and can have far-reaching effects.~~

3. It is also [harder] ~~very difficult~~ in current circumstances to make a reliable judgement about the new level at which oil prices may settle. We [thus] ~~have~~ to [consider] ~~prepare~~ the Budget against the [prospect] ~~background~~ ~~of great uncertainty about the prospect for oil revenues~~ [not merely of great reduction of revenue but also considerable uncertainty about how large the reduction will be].

4. Our current estimates suggest that if oil prices settle at $15 per barrel our revenues from the North Sea will be reduced to £6 billion for the next financial year. This compares with receipts of £12 billion in 1984-85. In last year's Medium Term Financial Strategy (MTFS) we expected revenues of £11½ billion for 1986-87.

5. Recently there has been considerable comment about the problems of adjustment the UK economy faces as the level of oil production declines. This was expected to ~~take place~~ [gradual] over ~~the next~~ [a generation or more] ~~[25] years or so~~. We are now faced with adjusting to the loss of [almost] half of the revenue in [a single] ~~one financial~~ year.

6. There has [probably] been some [turmoil] ~~turbulence~~ in financial markets as they have responded to the oil price change. Sterling has

fallen by about [7½] per cent and there has been persistent upward pressure on short term interest rates. So far we have been able to resist most of this but our continuing ability to do so must depend both upon future oil price movements and the market's view about our ability to cope with the results.

Fiscal position

7. Faced with this background my judgement is that we must approach the Budget with considerable caution. This means trying to avoid going above the £7½ billion Public Sector Borrowing Requirement (PSBR) figure set out in last year's MTFS. If anything there is a strong case for going somewhat below it.

8. Much may change between now and Budget day. Because non-oil revenues are now projected to be higher than expected I hope to be able to avoid a net increase in taxes in the Budget. But ~~there will be~~ there looks like being little, if any, scope for a net reduction in taxation. ~~It now looks as though~~ We ~~may~~ should just meet the public expenditure planning total set for the current financial year. ~~If we are~~ The need to cope successfully with the unprecedented situation which the oil price fall has created for the public finances ~~we will certainly need to hold~~ underlines the importance of holding public spending next year substantially within the planning total we have announced.

9. So far we have weathered the collapse in the oil price and its consequences for the financial markets and public finances pretty well - though there ~~We have so far weathered these storms - although there~~ may be some way yet to go. In so doing we are ~~being~~ greatly helped by the ~~strong~~ underlying ~~performance~~ strength of the economy, in terms of growth, inflation and ~~on~~ the external account; and above all by the reputation we have ~~built up~~ acquired for sound and prudent policies.

But while oil prices ~~affect~~ the pace and what is possible in the Budget, it should not greatly affect the overall economic performance - although there will be significant changes within the economy.

Economic Prospects

10. For the world as a whole, Lower oil (and commodity) prices will have beneficial effects in 1986 on the oil-consuming countries. The forecast

for the major industrialised countries is for output growth averaging 3 per cent - a little better than achieved last year. Inflation will stay low: indeed ~~there may be stable prices in the economies of~~ the virtual stability in Germany and Japan, it is likely to approach zero.

11. For the UK, the oil ~~market changes have~~ price fall has not caused me to revise my view that 1986 will be a further year of steady growth for the UK economy, at an annual rate of about 3 per cent; ~~and,~~ ~~again, with~~ accompanied by declining inflation.

12. Different parts of the economy will be affected in different ways by lower oil prices. While the oil industry will not do so well, manufacturing industry should benefit considerably. ~~Companies will tend to benefit relative to consumers; and manufacturing relative to non-manufacturing industry. Providing costs are contained, lower oil prices offer industry a considerable opportunity to improve its competitive position.~~

???

13. The UK economy is now in a stronger position to take advantage of this opportunity. The underlying improvement in its performance shows up in a number of indicators. Last year manufacturing productivity increased by a further 4 per cent. Since 1979 ~~It~~ it has now grown at an average annual rate of 3¾ per cent so ~~for the past six years~~. As the table below shows, our performance here compares very favourably with that ~~in earlier years~~ of the recent past; and ~~also~~ even with that of the majority of our principal overseas competitors ~~abroad~~.

Output per man hour in manufacturing
annual average growth rates, per cent

	1973-79	1979-85
US	1½	2½
Japan	6½	6½
Germany	4	3
France	5	3½
UK	1	3¾

14. Capital spending by business has generally been rising faster than output in recent years and further growth is expected in 1986, as a response to higher profits and continued expansion in output. Exports performed well in 1985; ~~responding to the rapid growth in world trade;~~ indeed, UK exporters increased their share of world trade. The prospect is for continued growth, albeit at a slower pace. Even after the fall in oil prices, another ~~substantial~~ sizeable current account surplus is in prospect for 1986, helped by rising earnings from our increasing stock of overseas assets.

15. ~~1986~~ This year is likely to see a ~~sizeable~~ significant rise in consumer spending. This reflects rapid growth in real disposable incomes - itself the result of the high level of wage settlements in 1984 and 1985 and the reduction in inflation expected this year. Earnings are currently rising at or above 7½ per cent. With inflation likely to fall to 4 per cent ~~or less~~ this year, the average employee's pay may rise by some 4 per cent ~~in~~ in real terms during 1986.

16. However, ~~This~~ excessive earnings growth remains the main threat to employment. Despite five years of continuous output growth, and a growth in employment of over ~~700,000~~ 600,000 since the summer of 1983, unemployment ~~remains at an unacceptably high level~~. ~~It~~ The pace is unlikely to ~~fall substantially~~ show much of a reduction while wages rise so ~~much~~ far ahead of prices. The fact is that despite our ~~excellent~~ very good productivity record UK unit labour costs have been increasing much more rapidly than those of our competitors.

17. Annex 1 sets out key figures from the forecast. Annexes 2 and 3 set out the revenue effects of selected tax changes, together with a note on the tax burden.

Summary and Conclusions

18. The dramatic change in oil prices has a major - and adverse - impact on the public finances; but I very much hope that,

~~because of~~ Thanks to the sound financial policies we have been following, it ~~may~~ will prove possible to avoid raising taxes, overall ~~next~~ in the Budget. ~~year.~~ The impact of lower oil prices on the UK economy ~~itself~~ as a whole is more neutral. I ~~continue to~~ expect to see continuing steady growth for the sixth year in succession and lower inflation. This is a measure of the strength of our underlying economic performance.

19. I seek colleagues' views on the appropriate shape of the Budget in the light of the circumstances I have outlined.

(N.L.)

ANNEX 1

SELECTED ECONOMIC INDICATORS

	1979	1980	1981	1982	1983	1984	1985	1986 (1)
World GNP, (2) in major 7 economies (per cent change)	3½	1	1½	- ½	2½	4½	2½	3
UK GDP, (2) (per cent change)	2½	- 2½	- 1½	2	3½	2½	3½	3
Domestic demand, (2) (per cent change)	4	- 3½	- 2	2½	4½	2½	2	3½
Retail prices Q4 (per cent change)	17½	15½	12	6	5	5	5½	4
Interest rates (average 3-month interbank)	13½	16½	14	12½	10	10	12	13 (3)
Current balance (£ billion)	- ½	3	6	4	3	1	3½	3½
Unemployment (UK, per cent excluding school leavers)	5	6	9½	11	12	12½	13	13 (4)
Sterling Index	87	96	95	90½	83	78½	78	74 (3)
Oil prices, $, North Sea	20½	34½	37½	33	30	29½	27½	17 (5)

(1) Provisional pre-Budget figures.

(2) At constant prices.

(3) February 7.

(4) Not a forecast. Figures based on assumptions in PEWP.

(5) Brent price for delivery in March, as of February 7.

ANNEX 2

REVENUE EFFECTS OF TAX CHANGES

A. Direct Taxes: Indexation

The RPI increased in the year to December 1985 by 5.7 per cent. With indexation by this amount and statutory rounding, the figures for the main allowances and other thresholds would be:

Personal allowances	1985-86 £	1986-87 £
Single and wife's earned income allowance	2205	2335
Married allowance	3455	3655
Bands eg		
30% rate	0-16200	0-17200
60%	over 40200	over 42700

The total revenue costs of indexation of income tax (reflected in the forecast) are £1140m in 1986-87, and £1490m in a full year, at forecast 1986-87 prices and incomes.

B Indirect Taxes: Indexation

The effects of 5.7 per cent revalorisation of the exercise duties (including VAT effects, price changes rounded) are as follows:

	Typical Price Change	Revenue effect (1986-87 prices) £m	RPI impact £m
Beer	1p/pint	100	0.07
Wine	5p/70cl light wine	20	0.02
Spirits	31p/bottle	45	0.04
Tobacco	5p/20 King size	150	0.14
Petrol	5p/gallon	260	0.13
Derv	5p/gallon	65	nil
VED	£5/car	100	0.05
Overall effect (reflected in forecast)		740	0.45

Note: First year and full year revenue effects are virtually identical.

C. Ready Reckoner: Illustrative Tax Changes

	£ million at forecast 1986-87 income levels	
INCOME TAX	1986-87	Full Year
Allowances and Thresholds		
1% above indexation on all statutory allowances	210	175
1% above indexation on all statutory allowances and thresholds	245	190
Rates		
Change basic rate by 1p	1175	975
CORPORATION TAX		
Change main rate by 1 percentage point	180	310
Change small companies' rate by 1 percentage point	16	30
OTHER TAXES		
Change VAT rate by 1 percentage point (1)	700 (2)	925

(1) A 1% change in the VAT rate would change the RPI by 0.5%.

(2) Provisional forecast

ANNEX 3

THE TAX BURDEN

Since the Government came to power total taxes and NICs as a proportion of GDP at market has risen by about 5 percentage points, though the ratio has fallen slightly since 1981-82. The figures are as follows:

Table 1

Total taxation* as a % of GDP (market prices)	
1978-79	33.9
1979-80	35.2
1980-81	36.4
1981-82	39.3
1982-83	39.1
1983-84	38.6
1984-85	39.2
1985-86 (estimate)	38.7
1986-87 (assuming indexation)	38.6

* Including NICs and the local authority rates.

Personal sector

2. Despite reductions in income tax, total personal taxes (direct and indirect, including employees' NIC and domestic rates) in 1985-86 are about £15 billion higher in real terms (ie 1985-86 prices) than they were in 1978-79. For income tax and national insurance contributions the following table shows how the proportion of gross pay they represent has risen, particularly for the low paid:

Table 2

Income tax and NICs as a % of gross earnings*

	½ average earnings	Average earnings	2 average earnings
1978-79	16.0	27.8	31.4
1981-82	20.8	29.3	32.2
1982-83	20.8	29.8	32.3
1983-84	20.1	29.6	31.7
1984-85	19.3	29.2	31.5
1985-86 (estimate)	19.0	29.0	31.5
1986-87 (indexation)	19.3	29.1	31.7

* Adult male earnings (all occupations). Married couple, wife not working: the couple are assumed to have no children, to avoid distortion of the figures from the abolition of child tax allowances.

3. These figures reflect the rise in the standard employees' NIC rate from 6½% to 9%. The lower rates introduced in the 1985 Finance Act do not affect the cases shown. So far as income tax is concerned, personal allowances have increased by over 19% in real terms since 1978-79 and have increased slightly faster than earnings. The basic rate has been reduced from 33p to 30p, but the 25p reduced rate band has been abolished.

4. As the table shows, indexation of allowances in the Budget would lead to a very slight rise in the proportion of incomes taken in tax and NIC. This is because earnings are assumed to rise by 7% compared with the indexation percentage of 5.7%.

5. Since 1978-79 total taxes paid by businesses (outside the North Sea) have fallen slightly as a percentage of GDP. Within this total, the major change has been a fall in employers' NIC and NIS as a percentage of GDP, partially offset by an increase in business rates, and 'other' taxes as the following table shows:

Taxes paid by businesses £bn in 1985-86 prices

(figures in brackets are %s of GDP)

	Corporation tax[1]	Taxes on self employment incomes	Employers' NIC and NIS	Rates	Other[2]	Total
1978-79	7.1	2.4	9.9	4.7	3.7	27.7
	(2.2)	(0.7)	(3.1)	(1.4)	(1.1)	(8.6)
1985-86 (estimate)	8.2	3.1	8.0	5.9	4.8	30.0
	(2.3)	(0.9)	(2.2)	(1.7)	(1.4)	(8.4)

1. Excludes North Sea, but includes ACT
2. VED, car tax, road fuel duty, duty on rebated oils, capital taxes.

 ORAL: 1987

273/001

ECONOMIC STRATEGY

Memorandum by the Chancellor of the Exchequer

1. The approach to the 1986 Budget is inevitably dominated by the dramatic changes taking place in the oil market. The large price fall ~~has implications for the financial markets, public finances and prospects for the economy~~ that has taken place means a sharp reduction in prospective oil tax revenues.

2. The current Brent price of $16-17 per barrel is ~~almost~~ some 45 ~~50~~ per cent below the end-November level~~. This~~ a change ~~is~~ almost as great ~~of the same order of magnitude~~ as the price increases of 1973 and 1979. ~~As we know from those experiences, the results of a shock of this magnitude are~~ not easy ~~difficult to predict and can have far-reaching effects~~.

3. It is also harder ~~very difficult~~ in current circumstances to make a reliable judgement about the new level at which oil prices may settle. We therefore have to prepare the Budget against the background ~~of great uncertainty about the prospect for oil revenues~~ not merely of great reductions of revenue but also considerable uncertainty about how long the reduction will be.

4. Our current estimates suggest that if oil prices settle at $15 per barrel our revenues from the North Sea will be reduced to £6 billion for the next financial year. This compares with receipts of £12 billion in 1984-85. In last year's Medium Term Financial Strategy (MTFS) we expected revenues of £11½ billion for 1986-87.

5. Recently there has been considerable comment about the problems of adjustment the UK economy faces as the level of oil production declines. This was expected to take place over the next [25] years or so. We are now faced with adjusting to the loss of half of the revenue in a single ~~one financial~~ year.

6. There has inevitably been some turbulence in financial markets as they have responded to the oil price change. Sterling has

fallen by about [7½] per cent and there has been persistent upward pressure on short term interest rates. So far we have been able to resist most of this but our continuing ability to do so must depend both upon future oil price movements and the market's view about our ability to cope with the results.

Fiscal position

7. Faced with this background my judgement is that we must approach the Budget with considerable caution. This means trying to avoid going above the £7½ billion Public Sector Borrowing Requirement (PSBR) figure set out in last year's MTFS. If anything there is a strong case for going somewhat below it.

8. Much may change between now and Budget day. Because non-oil revenues are now projected to be higher than expected I hope to be able to avoid a net increase in taxes in the Budget. But ~~there will be~~ there looks like being little, if any, scope for a net reduction in taxation. ~~It now looks as though~~ We ~~may~~ should just meet the public expenditure planning total set for the current financial year. ~~If we are~~ The need to cope successfully with the unprecedented situation which the oil price fall has created for the public finances ~~we will certainly need to hold~~ underlines the importance of holding public spending next year similarly within the planning total we have announced.

9. ~~We have, so far, weathered these storms - although there~~ So far we have weathered the collapse in the oil price and its consequences in the financial markets ~~[illegible]~~ underlines the importance pretty well - though there may be some way yet to go. In so doing we are ~~being~~ greatly helped by the ~~strong~~ underlying strength ~~performance~~ of the economy, in terms of growth, inflation and ~~on~~ the external account; and above all by the reputation we have ~~built~~ acquired up for sound and prudent policies.

But ~~[illegible]~~ while, oil prices profound ~~effect~~ impact on what we propose in the Budget, it should not greatly affect our overall econ. perf. — although there will be ~~[illegible]~~ significant changes within the economy.

Economic Prospects

10. For the world as a whole, Lower oil (and commodity) prices will have beneficial effects in 1986 on the oil-consuming countries. The forecast

for the major industrialised countries is for output growth averaging 3 per cent - a little better than achieved last year. Inflation will stay low: indeed ~~there may be stable prices in the economies of~~ Germany and Japan, it is likely to approach zero.

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12. Different parts of the economy will be affected in different ways by lower oil prices. Companies will tend to benefit relative to consumers; and manufacturing relative to non-manufacturing industry. Providing costs are contained, lower oil prices offer industry a considerable opportunity to improve its competitive position.

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13. The UK economy is now in a stronger position to take advantage of this opportunity. The underlying improvement in its performance shows up in a number of indicators. Last year manufacturing productivity increased by a further 4 per cent. Since 1979 it has now grown at an average annual rate of 3¾ per cent ~~for the past six years~~. As the table below shows, our performance here compares very favourably with that ~~in earlier years~~ of the recent past; and ~~also~~ even with that of the majority of our principal competitors ~~abroad~~ overseas.

Output per man hour in manufacturing
annual average growth rates, per cent

	1973-79	1979-85
US	1½	2½
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14. Capital spending by business has generally been rising faster than output in recent years and further growth is expected in 1986, as a response to higher profits and continued expansion in output. Exports performed well in 1985, responding to the rapid growth in world trade: indeed, UK exporters increased their share of world trade. The prospect is for continued growth, albeit at a slower pace. Even after the fall in oil prices, another sizeable ~~substantial~~ current account surplus is in prospect for 1986, helped by rising earnings from our increasing stock of overseas assets.

15. 1986 is likely to see a significant ~~sizeable~~ rise in consumer spending. This reflects rapid growth in real disposable incomes - itself the result of the high level of wage settlements in 1984 and 1985 and the reduction in inflation expected this year. Earnings are currently rising at or above 7½ per cent. With inflation likely to fall to 4 per cent ~~or less~~ this year, the average employee's pay may rise by some 4 per cent in real terms during 1986.

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Thanks to

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(N.L.)

SECRET

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Retail prices Q4 (per cent change)	17½	15½	12	6	5	5	5½	4
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Current balance (£ billion)	- ½	3	6	4	3	1	3½	3½
Unemployment (UK, per cent excluding school leavers)	5	6	9½	11	12	12½	13	13 (4)
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* Including NICs and the local authority rates.

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2. Despite reductions in income tax, total personal taxes (direct and indirect, including employees' NIC and domestic rates) in 1985-86 are about £15 billion higher in real terms (ie 1985-86 prices) than they were in 1978-79. For income tax and national insurance contributions the following table shows how the proportion of gross pay they represent has risen, particularly for the low paid:

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1984-85	19.3	29.2	31.5
1985-86 (estimate)	19.0	29.0	31.5
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* Adult male earnings (all occupations). Married couple, wife not working: the couple are assumed to have no children, to avoid distortion of the figures from the abolition of child tax allowances.

3. These figures reflect the rise in the standard employees' NIC rate from 6½% to 9%. The lower rates introduced in the 1985 Finance Act do not affect the cases shown. So far as income tax is concerned, personal allowances have increased by over 19% in real terms since 1978-79 and have increased slightly faster than earnings. The basic rate has been reduced from 33p to 30p, but the 25p reduced rate band has been abolished.

4. As the table shows, indexation of allowances in the Budget would lead to a very slight rise in the proportion of incomes taken in tax and NIC. This is because earnings are assumed to rise by 7% compared with the indexation percentage of 5.7%.

5. Since 1978-79 total taxes paid by businesses (outside the North Sea) have fallen slightly as a percentage of GDP. Within this total, the major change has been a fall in employers' NIC and NIS as a percentage of GDP, partially offset by an increase in business rates, and 'other' taxes as the following table shows:

Taxes paid by businesses £bn in 1985-86 prices

(figures in brackets are %s of GDP)

	Corporation tax[1]	Taxes on self employment incomes	Employers' NIC and NIS	Rates	Other[2]	Total
1978-79	7.1	2.4	9.9	4.7	3.7	27.7
	(2.2)	(0.7)	(3.1)	(1.4)	(1.1)	(8.6)
1985-86 (estimate)	8.2	3.1	8.0	5.9	4.8	30.0
	(2.3)	(0.9)	(2.2)	(1.7)	(1.4)	(8.4)

1. Excludes North Sea, but includes ACT
2. VED, car tax, road fuel duty, duty on rebated oils, capital taxes.

REPORT BY
SCOTCH WHISKY
ASSOCIATION

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I think there is
a copy floating about.

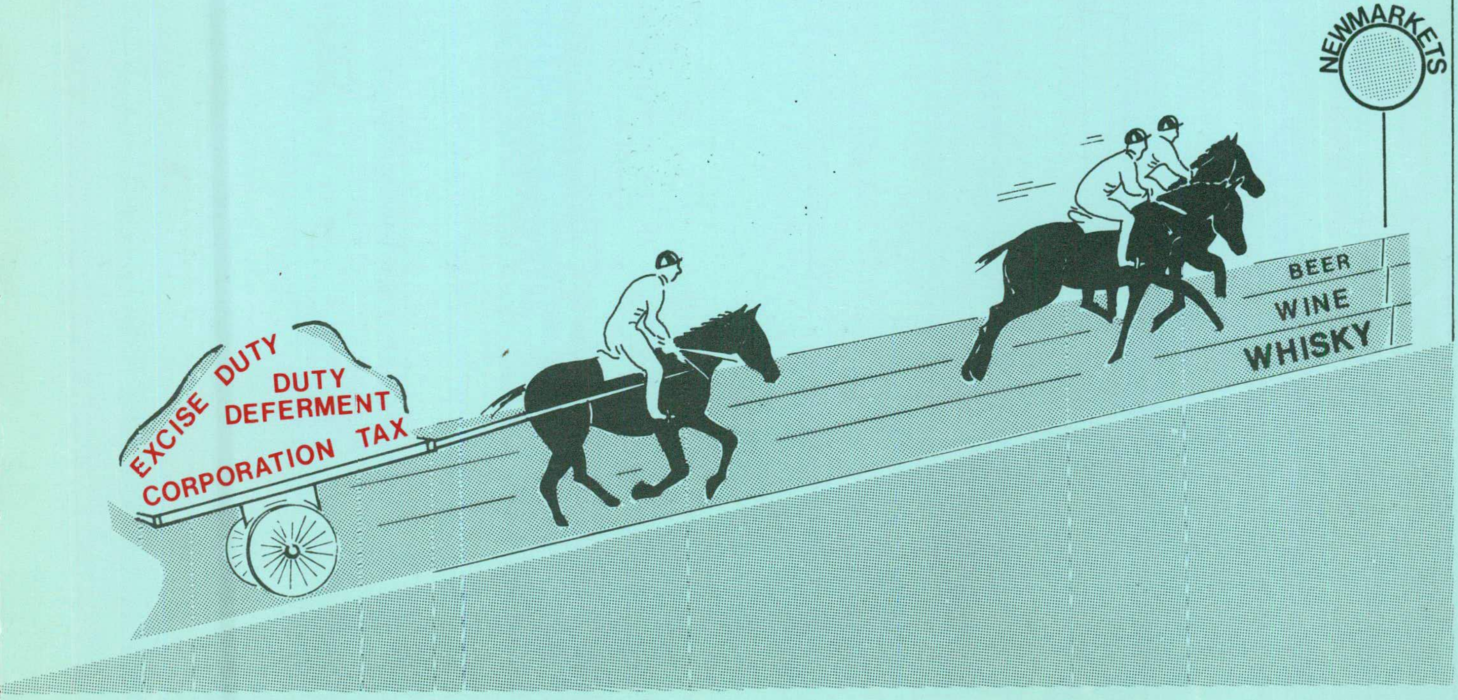
THE SCOTCH HANDICAP

A Report prepared for
THE SCOTCH WHISKY ASSOCIATION

BY

PEIDA

1986



THE SCOTCH HANDICAP

1986

A Report Prepared for

THE SCOTCH WHISKY ASSOCIATION

by

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December,1985

PEIDA

TABLE OF CONTENTS

PEIDA

1.0 SUMMARY

1.1 This submission has three main objectives:

* to argue that the 1986 budget should continue the move toward equalisation of taxes on a per degree of alcohol basis;
* to suggest a compromise method, based on the legal requirement for maturing Scotch whisky, of treating stocks of maturing Scotch for taxation purposes which will reduce, but not remove, the inherent discrimination in the present tax system which makes Scotch whisky less competitive; and
* to advocate that the period of duty deferment be increased from four to eight weeks.

1.2 The structure of UK taxation for alcoholic drinks discriminates heavily against the spirits industry, including Scotch, in favour of beer and wines. The tax per degree of alcoholic strength is 15.77p for spirits, this being very substantially greater than both the 8.17p and 8.60p for table wines and beer respectively.

1.3 As all alcoholic drinks compete with each other in the market place, the current structure of taxation must distort competition. Moreover, it does so in a manner which encourages overseas production (of wines) against domestic production of spirits. Consumption of wine has increased by 23% in the fiscal year 1984/85.

1.4 The UK structure of taxation for alcoholic drinks is rooted in historic prejudices which have no present justification, in terms of social, health or economic considerations.

1.5 During the 1960s Scotch whisky was able to withstand discriminatory treatment in the UK market as it was enjoying strong and rapidly growing sales worldwide. However, by the 1970s prices were under severe pressure in both domestic and overseas markets. With the high incidence of tax in the retail price, it was becoming increasingly difficult to pass on increases in excise duties to the consumer.

1.6 In recent years, and especially from 1979, the industry's problems have become noticeably more severe, as evidenced by the decline in sales volume, and by distillery and bottling plant closures, with consequential losses of employment in Scotland.

1.7 Falling sales do not, in themselves, constitute a case for favourable tax treatment, but they do consitute an overwhelming reason for less unfavourable tax treatment. After all, an income earner does not continue to pay tax at a high rate after his income has fallen.

1.8 The industry fully accepts that, in recent years, there has been more recognition of its problems and that over a number of budgets, including the 1985 Budget, excise duty changes have reduced the degree of discrimination against it. Nonetheless, existing market conditions are still unfavourable and require continued change toward a system of tax based on alcohol content.

1.9 Although the UK excise duty structure has become less unfavourable, the industry is now having to contend with major changes in the corporation tax structure, which does not take into account its unique dependence on stocks which require to be matured for several years. With the abolition of stock relief and with corporation tax being levied on historical cost profits, which make no allowance for the high replacement cost of the whisky sold, the effective rate of taxation being borne by the industry is excessive by comparison with all other industries. This is particularly the case in the transitional period, but, more importantly, will constitute a permanent burden on the industry.

1.10 There is an average period of three months between payment of excise tax by the trader and its recovery from the consumer. The industry at present has a tax deferment period on spirits of one month only. Therefore the industry finances this additional two month excise duty, which places an additional financial burden on Scotch Whisky. The industry requests that the government considers a further four week deferment for the collection of duty in order to strengthen the financial base of the industry.

2.0 THE DECLINING HOME MARKET

2.1 The UK home market for whisky has witnessed:

* five years of falling consumption
* a seriously ageing consumer profile
* a diminishing share of consumer expenditure
* a contraction in the number of whisky companies
* closures of distilleries and loss of jobs

Falling Consumption

2.2 For the fifth consecutive year, 1984 saw a further contraction in the home market, this persisting despite the sharp recovery evident in the domestic economy. The severity of the change is illustrated in Figure 1. That this is part of a longer term difficulty is evidenced by Figure 2. It is clear that increased volume growth in the 1970s was not accompanied by a corresponding increase in the real value of sales. Instead, in real value terms, the 1970s saw a small decrease. In the 1980s, the industry experienced both decreasing volume and a decline in the real value of its sales.

Figure 1

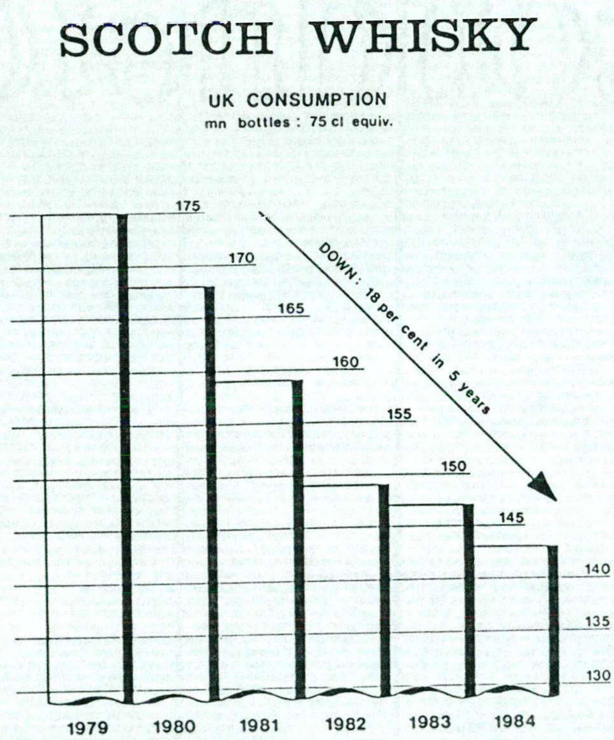

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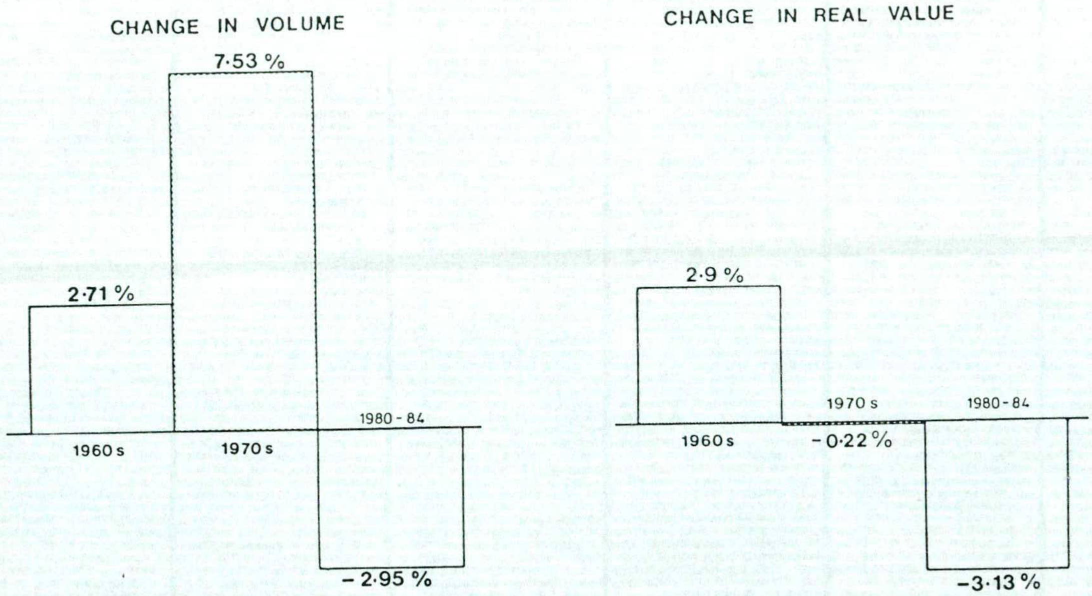
Figure 2

DOMESTIC CONSUMPTION — Compound Growth/Decline Rates



Note: The above figure demonstrates that the high growth rates experienced through the 1970s particularly, have given way to declining sales levels, this occuring at some 3% per annum.

Ageing Consumer Profile

2.3 Tastes and preferences have moved against the whisky industry which now faces an ageing consumer profile in contrast to its main competitors. The relative age structure of consumers of alcoholic drinks is shown in Table 2.1.

Table 2.1

Age Profile of Consumers of Alcoholic Drinks
% Distribution by Age

Market	18-24	25-34	35-49	50+
All Beer	23	27	25	25
Still Wine	18	21	27	34
Whisky	14	20	24	42
Weekly Whisky Drinkers	8	14	26	52

Source: PAS, Beer Market Survey, 1982

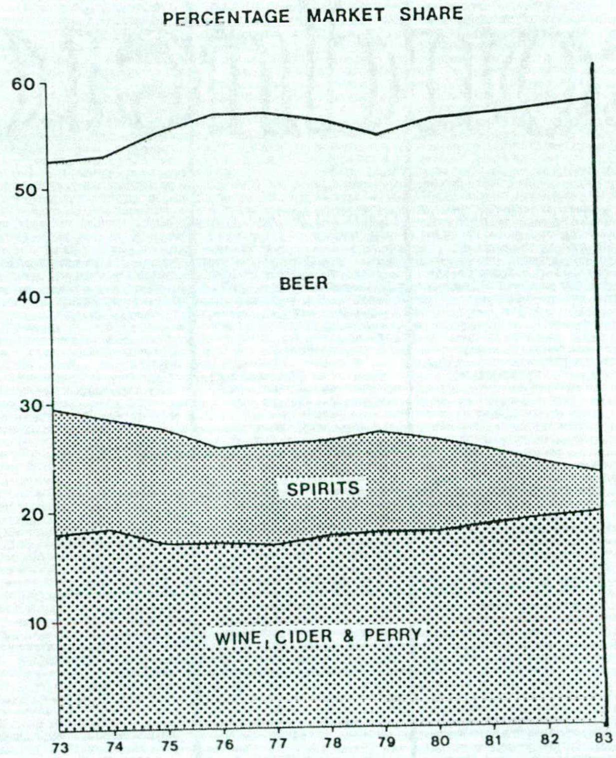
2.4 Whisky tends to be an older persons drink. Some 78% of all whisky drinkers are aged 35 years or over (compared with 66% of the population) and over 50s account for 52% of regular whisky drinkers (but only 42% of the population).

2.5 Unless a major impact is made on the drinking tastes and preferences of the under 35 market, the home industry will experience a continued decline in sales. In turn, this requires a profitable industry able to finance a major marketing campaign in an increasingly competitive market.

2.6 As consumption of whisky contracts, the wine market is enjoying rapid growth, as shown in Figure 3. However, it is beer sales which dominate the alcoholic drinks market and this industry has had sufficient profitability to expand into many new markets in recent years.

Figure 3

CONSUMER EXPENDITURE ON ALCOHOLIC DRINKS
1973-83



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2.7 Consumer expenditure on beer rose from 52% of the alcoholic drinks market in the UK to 57% between 1973-1983, whereas expenditure on spirits fell from 29% to only 23% of the total drinks market in this period. Whisky's share of the spirits market, historically around half, is also falling over the long term against its main competitors, which include imported spirits like brandy and rum. Changing levels of consumer expenditure are shown in Figure 3.

Contraction in the Number of Whisky Companies

2.8 There are now only five quoted companies whose main business is the eventual sale of blended whisky, or whose business is a combination of sales for fillings, malt and blended whisky. There were seven such companies at our last meeting with the Chancellor in January 1985 but since then Tomatin plc has ceased trading and Bells have been bought by Guinness.

Closure of Distilleries and Loss of Jobs

2.9 The most recent survey, carried out in mid 1984 for the Distillery Sector Working Group, showed a reduction in the work force of approximately 7,400, almost 30% since the Group previously reported in 1978. In January 1985 ten distilleries closed with 180 job losses in the North East of Scotland. In Spring 1985, 700 jobs were lost with the closure of DCL plants in Glasgow and South Queensferry.

2.10 The latest survey on capacity records distilleries working at 50% capacity and blending and bottling plants at 64% capacity.

2.11 To sum up, the home market for whisky has been shrinking over a number of years, with all the evidence suggesting that trading conditions will remain extremely difficult unless the industry's competitive environment can be made less unfavourable. The excise duty structure within which the industry operates will be crucial to the industry's ability to arrest the ageing consumer profile and recover a growth market.

3.0 GROWTH MARKETS

3.1 Within the difficult general market conditions faced by whisky, there have been two growth sectors:

* retail sales in the UK;

* the export market in bottled malt

Retail Sales in the UK

3.2 The share of retail sales to total consumption in the alcoholic drinks market has been rising steadily in the last few years. The share of the on-trade has fallen from an estimated 79.5% in 1973, to some 74.9% in 1983.

3.3 Only 45% of whisky is consumed on licensed premises. However, this 45% accounts for 62% of the value of whisky sales. This contrasts with the situation of beer sales, where 89% of both volume and value were consumed on licensed premises.

3.4 Retail sales provide a more attractive market for whisky brand owners as here they are more price competitive with the brewers. There is a much higher mark-up on spirits in on-licence sales than there is on beer, as indicated in the volume/value differences in paragraph 3.3.

3.5 The competition for retail sales is waged through product diversification and advertising. The success of product diversification is largely dependent on marketing and advertising. The most recent MEAL survey on advertising expenditure (1982) estimated that the major brewers alone spent £104.8 million on advertising, whereas the comparable expenditure for whisky was £7.5 million. The Scotch whisky industry, together with other spirit producers, have a successful 'gentleman's agreement' not to advertise on television in the UK.

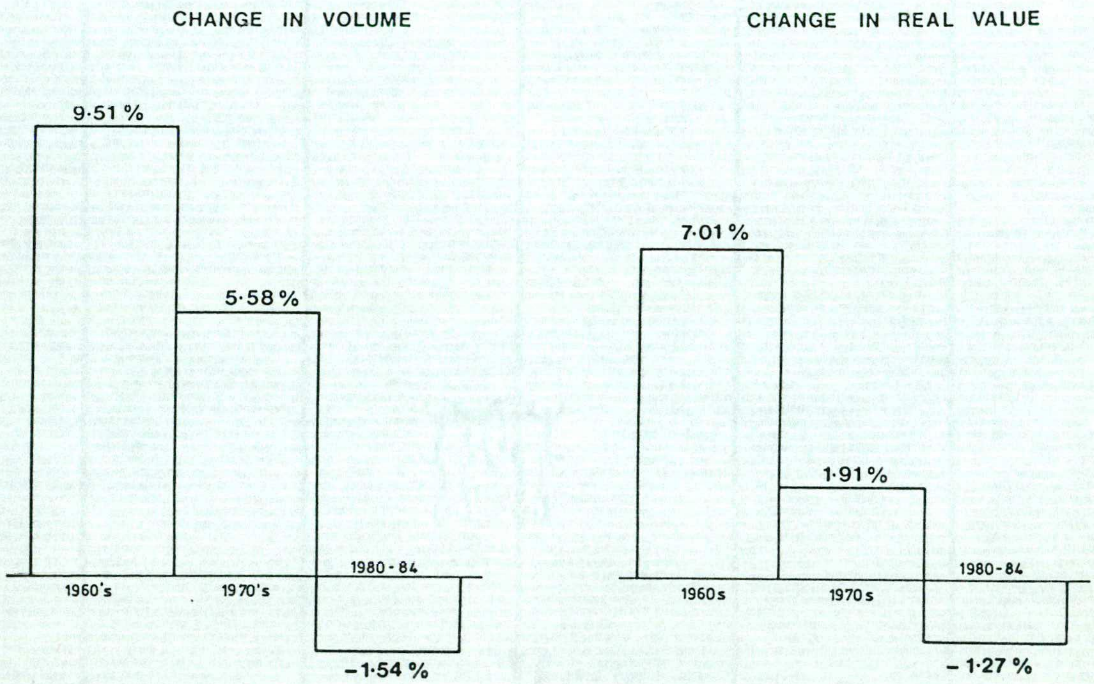
The Export Market in Bottled Malt

3.6 In overall volume terms, the export market fell by 12% between 1979 and 1984, with an encouraging increase in volume of 3% in the first nine months of 1985. Within this market, exports of bottled malt increased by 49%.

In contrast, over the same period (1979-84) the bottled blend export market fell by 20% in volume terms. The longer term trends in the export market in volume and value are shown in Figure 4.

Figure 4

WHISKY EXPORTS – Compound Growth/ Decline Rates



3.7 The difficulty the industry faces is that it takes many years of effort to establish a foothold in export markets and the return on the heavy initial investment required is slow to mature. Hence, a profitable UK market is a necessary base for exporting, again underlining the need for a structure of excise duties which does not discriminate against spirits, and a treatment of profits which does not discriminate against companies with a high stock:output ratio - this being deemed necessary both from a quality standpoint and to compete in world markets.

3.8 Impressive if erratic growth of bottled malts has taken place in the last ten years in world markets, as well as the UK market. However, it is still a tiny sector (2%) of the total whisky market. Malts and de luxe brands of blended whisky account for a disproportionately high share of total advertising expenditure on whisky. With some 4% of total UK volume these two sectors account for some 25% of the total spent on advertising by the industry. Hence, the continued development of these brands requires a profitable industry, an outcome which is particularly difficult to achieve given that the taxation of profits on an historic cost basis is particularly detrimental to the malt and de luxe categories.

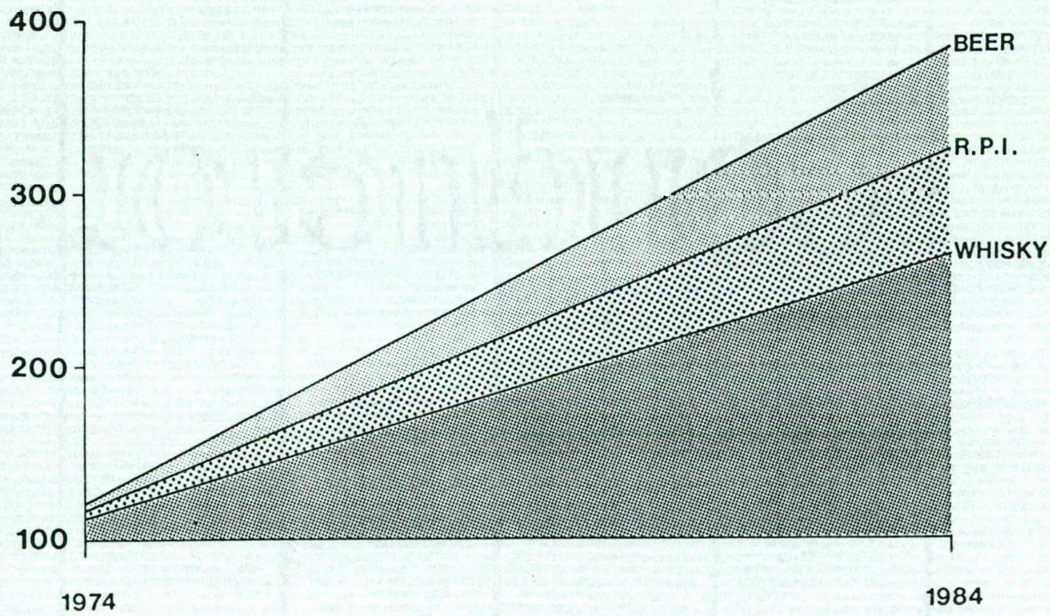
4.0 PROFITABILITY

Prices

4.1 Through the period 1974 to 1984, whisky prices in the UK rose by a factor of only 2.6 - well below the rise in the Retail Price Index as shown in Figure 5. Beer prices over the same period rose by a factor of 3.8, much faster than retail prices in general. Most brewers, particularly regional brewers, have managed to increase both sales and profits throughout the first half of this decade, in spite of static or falling volumes. Despite the much more substantial price increase for beer as opposed to whisky over 1973-83, consumer expenditure on beer has risen from 52% to 57% of the alcohol market, while expenditure on spirits has fallen from 29% to 23%. Whisky's share of the spirit market has also been decreasing over this period from 52% to 48% of the market. This situation emphatically demonstrates the much more unfavourable market circumstances faced by the Scotch whisky industry.

Figure 5

RETAIL PRICE INDICES

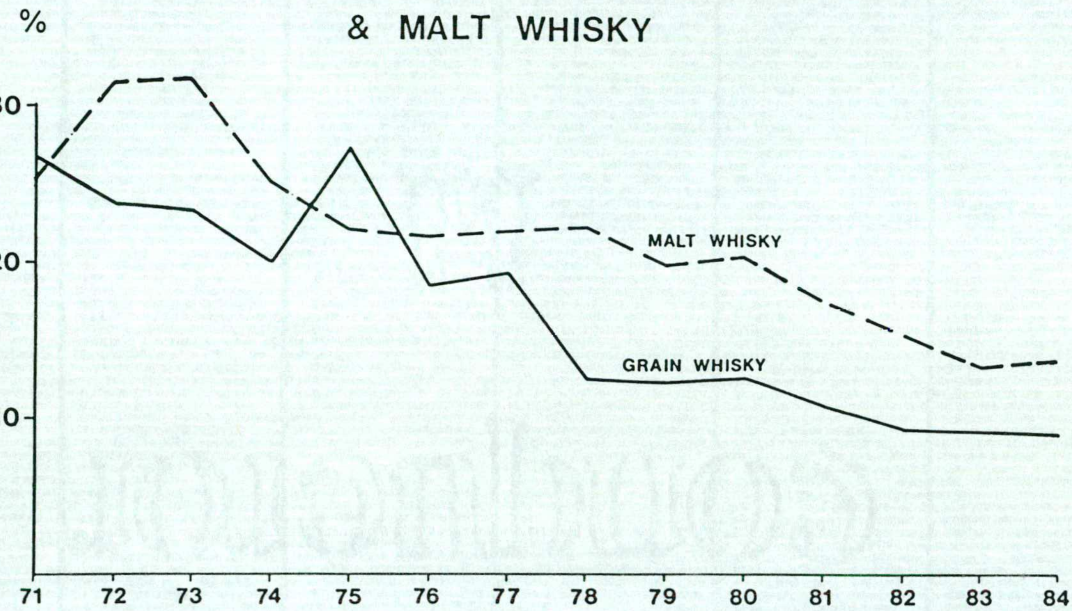


Profitability

4.2 These unfavourable price trends are reflected in all measures of profitability, particularly where this is measured on a current cost accounting basis. Figure 6 shows the sharp decline in estimated profit margins for new grain and malt production, these being based on the published reports of the stockbrokers Cambell Neill & Co. These are based on the experience of average sized distilleries. The contraction of profit margins post-1979 is particularly apparent.

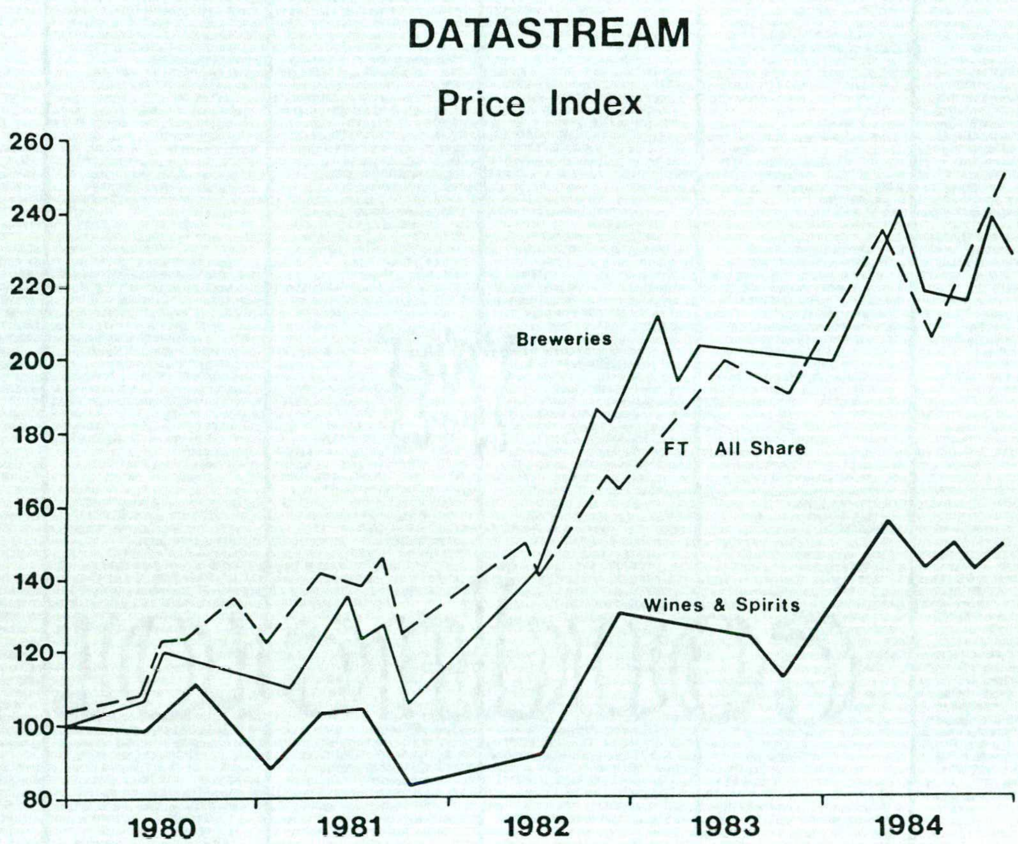
Figure 6

PROFIT MARGIN (Before Tax) ON SELLING PRICE OF NEW GRAIN WHISKY & MALT WHISKY



4.3 The consequence of falling profit margins and profits is now evident in Stock Exchange valuations. The valuation of breweries on the London Stock Exchange has grown at a far greater pace than wine and spirit firms over the five year period 1980-1984. Taking 1980 as 100, brewers valuation has risen to 240, whereas wines and spirits have achieved 140. Comparisons with the FT All Share Price Index are equally unfavourable (Figure 7).

Figure 7



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4.4 Within major drinks concerns the contrasting experience between the profit performance of whisky and beer is even more startling. For example, Whitbread and Company plc have only disaggregated their beer (brewing and wholesaling) and wines and spirits (distilling, blending and wholesaling) in the last two financial years with the following results:

		Turnover	Profit	Profit as % Turnover
1985	Beer	510.5	70.5	13.8
	Wines & Spirits	524.1	26.3	5.0
1984	Beer	468.3	55.2	11.8
	Wines & Spirits	439.9	23.3	5.3

4.5 Due to low profitability the industry has much less to invest in product diversification and marketing than its competitors. Above all, it does not have the financial resources required to maintain and sustain the marketing campaign necessary in fiercely competitive markets.

4.6 The industry's proposals are therefore aimed at allowing some improvement in profit margins in order to allow it to recover lost ground at home and abroad. As we have repeatedly emphasised, the industry does not seek subsidy, but it does believe that the structure of excise duties, the taxation of profits on an historic cost basis (particularly the treatment of stocks) and the treatment of duty deferment combine to create an environment which is not conducive to a healthy and progressive industry. It therefore seeks action on each of these fronts.

5.0 EXCISE DUTY

5.1 As Figure 8 illustrates, the tax take from excise duty has declined substantially in real terms from a peak in 1968. Figure 9 demonstrates that this has occurred despite a reduction in the degree of tax discrimination against the industry which is particularly evident from 1980. Quite simply, the tax burden has had to be lightened as the industry has been unable to sustain this burden in the changed market circumstances of the 1970s and 1980s.

5.2 It is evident that this shift in demand against Scotch is not simply the result of tax-led pricing, but the tax structure is still of first importance in increasing the price of whisky relative to other drinks.

Figure 8

Total Whisky Tax in real terms and Whisky Consumption

(1954 - 1984)

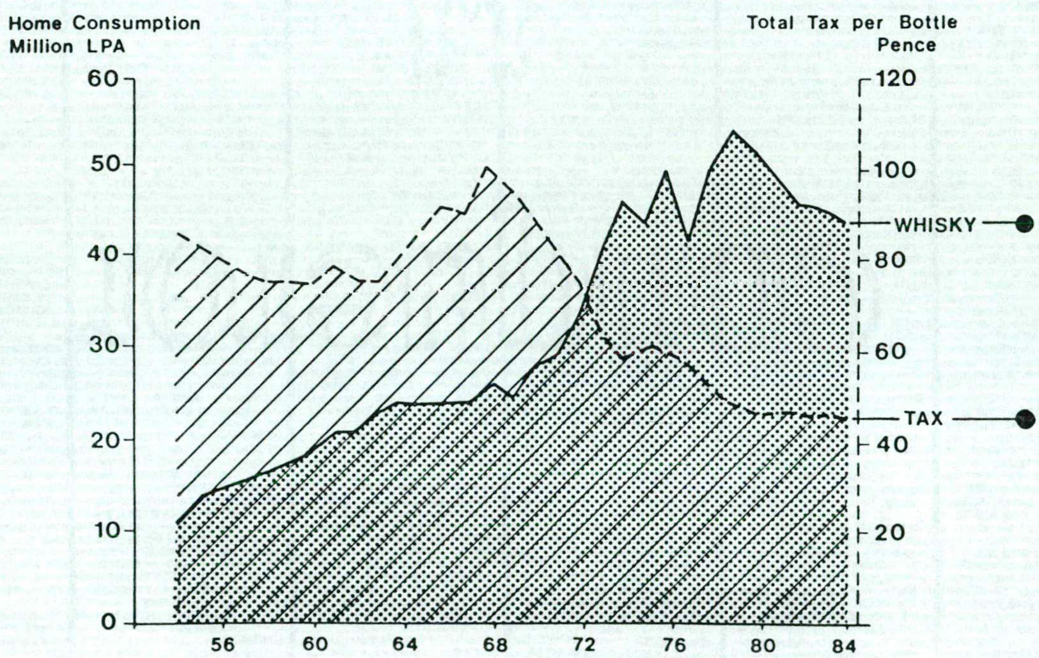

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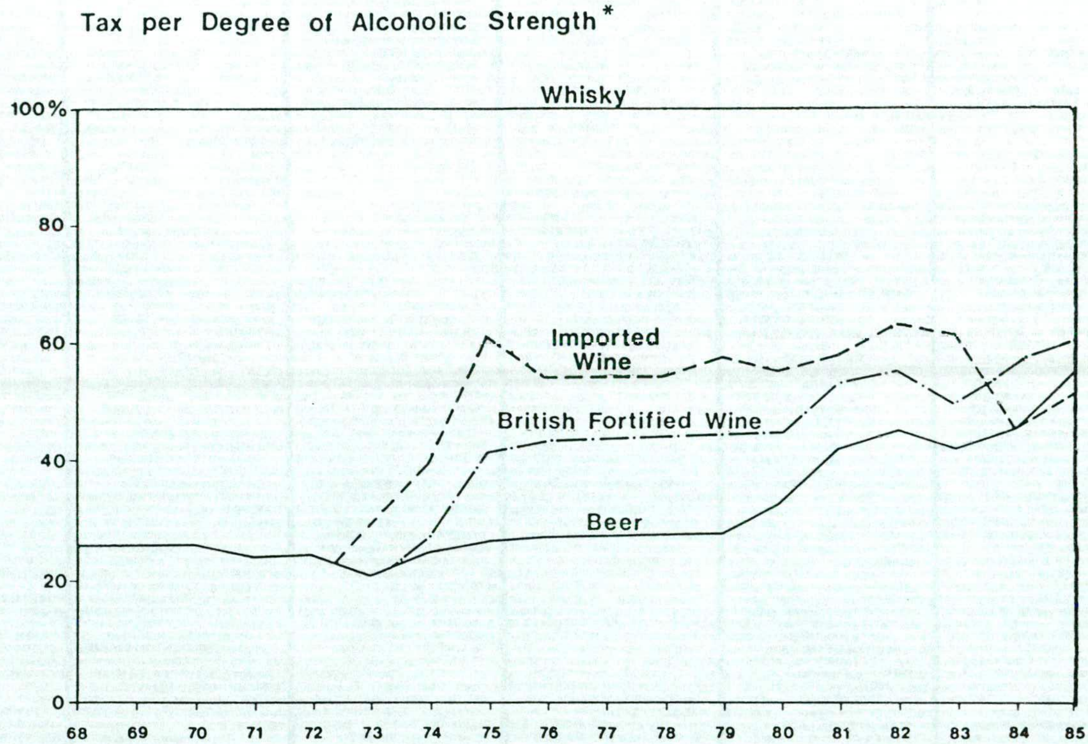
Figure 9



* Whisky Tax = 100 each year

Relative Tax is taken as Excise Duty, plus VAT on Excise Duty only

5.3 A model incorporating current data on quantities sold, basic tax rates and demand elasticities with a stated tax target, considered possible changes in the price of a pint of beer and consequent implications for the tax rates of various alcoholic beverages, and for their sales volumes. This exercise has been repeated for present purposes, the model now incorporating final assumptions regarding Scotch discussed in previous meetings with Customs and Excise officials. The tax target for the financial year 1986/87 is taken as £4,360 million, this being 4% above that forecast by the Customs and Excise for 1985/86 (Hansard April 1985).

5.4 On the basis of previous discussions with Customs and Excise officials, the price data entered relate to the best available data on the distribution of sales between retail outlets and licensed premises. As compared to our previous analysis, this makes the largest impact on spirit prices raising them from £7.50 to £12.88 per bottle.

5.5 Our model differs from the Customs and Excise in two regards. First, we incorporate two different types of wine, as this better reflects the drinks market. Second, we have considered the likely results with a system incorporating both own price and cross price elasticities, as well as the simpler own price elasicities employed by the Customs and Excise.

5.6 The own price and cross-price elasticities adopted in model A are shown below:

Own Price Elasticities:		Cross Price Elasticities:	
Spirit	-0.93	Spirits/Wine	0.12
Wine	-0.76	Spirits/Beer	0.30
Beer	-0.20		

While the own price elasticities without any cross-price elasticities are taken as:

Spirits	-1.3
Wine	-1.1
Beer	-0.2

5.7 As previously, the model is run on the assumption that the Chancellor wishes to maintain the real value of tax revenues, taken to represent a target of £4,360 million in 1986/87 (i.e £4,200 plus 4%). The model assumes certain changes in the final price of beer and then calculates the changes in the prices of other alcoholic beverages which will allow the realisation of the tax target, given the price elasticities shown above.

5.8 The changes in the price of a pint of beer considered are:

Case 1 1.0 pence increase
2 1.5 pence increase
3 2.0 pence increase

A: Own and Cross Elasticities

5.9 The results are as follows:

Required Changes in the Price of Alcoholic Beverages

(£4,360 million Excise Tax Target)

	Beer (pint)	Wine 17% (bottle)	Wine <15% (bottle)	Spirits (bottle)
Case 1	1.00	0.08	3.21	-9.08
2	1.50	0.18	5.25	-40.45
3	2.00	0.38	7.24	-69.80

5.10 This would result in the following changes in sales volumes.

Estimated % Changes in Annual Sales Volumes

	Beer (pint)	Wine 17% (bottle)	Wine <15% (bottle)	Spirits (bottle)
Case 1	---	+1	---	+1
2	-1	+2	---	+4
3	-1	+4	---	+6

B: Own Price Elasticities

5.11 The results are as follows:

Required Changes in the Price of Alcoholic Beverages

(£4,360 million Excise Tax Target)

	Beer (pint)	Wine 17% (bottle)	Wine <15% (bottle)	Spirits (bottle)
Case 1	1.00	0.72	3.21	-0.50
2	1.50	0.22	5.25	-40.02
3	2.00	-0.04	7.24	-75.45

5.12 This would result in the following changes in sales volumes:

Estimated % Changes in Annual Sales Volumes

	Beer (pint)	Wine 17% (bottle)	Wine >15% (bottle)	Spirits (bottle)
Case 1	---	---	-1	---
2	---	---	-2	+4
3	-1	---	-2	+8

Conclusion

5.13 Both A and B provide broadly comparable results. That is, the smallest increase on beer which would meet the stated revenue target and hold spirit consumption stable is 1.0 pence on a pint (Case 1). There would be no measurable change in beer sales. This would be consistent with a small decrease of 9.0 pence and 0.5 pence (A and B) on a bottle of spirits, spirits being the residual in this tax target. There would be little change in spirits volume sales (1% increase in A: no change in B).

5.14 In short, the calculations indicate that the Chancellor would be able to meet such a tax target by freezing the existing level of duty on spirits and making modest changes to the duty on wine and beer. The consequent changes in volume would be small. This is consistent with the own-price elasticities adopted by the Treasury, which confirm that spirit sales are price sensitive while beer sales are not.

6.0 CORPORATION TAX

6.1 Stock relief was abolished in the Budget of 1984, without any transitional arrangement as applied to capital allowances. As our previous submissions have demonstrated this has resulted in a dramatic increase in the effective rate of tax borne by the industry in the transitional period. This has been evidenced in the accounts recently produced by a number of companies, the most significant being the Distillers Company plc where the effective rate of tax on the historical cost profits rose from 33% to 44%, and in the current cost accounts from 55% to 68%. Although this fact has been accepted by the Treasury officials, no new transitional arrangements were effected.

6.2 Of greater concern to the industry however is the permanent impact which the new regime will have in depressing its real level of profits relative to other industries. In the Scotch whisky industry, where stocks are held for maturation for periods varying from three to twelve years (and more), even modest rates of annual inflation result in high levels of historical cost profits which are subject to corporation tax, with no regard given to the considerable additional cost of replacement which requires to be funded.

6.3 A simple illustration of the situation is as follows:

Assumed inflation rate of 5% per annum
Assumed age of whisky when sold - 5 years

Cost of production of 100 units, say - Year	1	£100
	2	£105
	3	£110.2
	4	£115.8
	5	£121.6
	6	£127.6

6.4 The industry carries its stock for many years, particularly for producing the malts and de luxe blends which are so vital to its reputation. In consequence, its stock to sales ratio is around 9:1, with investment in stocks being the predominant feature of its balance sheet, 2.5 times higher than investment in plant. The industry is stock intensive, while almost all other industries are plant intensive.

6.5 The outcome of such a situation is self evident. If historical cost profits are taxed without any allowance for the fact that the cost of replacement of stock is now considerably higher because of price inflation, the effective rate of tax for the industry (i.e after allowing for the additional cost of replacing stock - the CCA cost of sales adjustment) will be significantly higher than the nominal rate of corporation tax and the effective rates of all other industries calculated on the same basis.

6.6 This can be illustrated by recent whisky company results which are shown overleaf. In each case the latest available information has been taken. Some companies provide their own cost of sales adjustment (COSA) in their accounts; for others COSA has been calculated after discussion with the company. For each company the effective rate of corporation tax is calculated, with the unweighted and weighted average at the foot of the table relating to all companies included. A common rate of corporation tax of 35% has been used as the basic tax rate. The results show:

* for all companies the effective rate of corporation tax is significantly higher than the nominal rate only one company having an effective tax rate of less than 40%;

* the weighted and unweighted averages are 45.7% and 58.7%; and

* the effective rate of tax is particularly high for companies specialising in bottled malts, as exemplified by the extremely high effective tax rates for Macallan Glenlivet and Macdonald Martin; this also applies to de luxe Whiskies.

6.7 There has to be recognition of one outstanding fact. The present method of taxing whisky companies on a historical cost basis must seriously jeopardise, in particular, those companies whose malts and de luxe brands are so important for the industry's qualitative image. Companies which specialise in quality aged products will have grave difficulty if inflation continues at any level.

6.8 Comparison with other non-whisky companies is difficult firstly, because a declining number of companies produce COSA data and, secondly, because those who do, may provide a biased sample. We have however attempted to estimate the impact of COSA adjustments on the effective rate of tax for two randomly selected groups of

Company	Reporting Year	Pre-tax Profits £m	Tax at 35% £m	COSA actual/ estimate* £m	COSA % of Pre-tax Profits	Effective tax rate after COSA %	Stock Relief on Whisky Actual Stock Relief at Average £m
Seagram Distillers plc	31.1.85	25.2	8.8	8.0*	31.7	51.2	2.98
Distillers Company plc	31.3.85	236.2	82.7	43.1	18.2	42.8	20.68
Edrington Holds Ltd	31.12.84	12.9	4.5	2.7*	20.9	44.1	0.62
Wm Grant & Sons Ltd	31.12.84	11.1	3.9	4.1	36.9	55.7	0.38
The Highland Distilleries Co plc	31.8.84	8.3	2.9	2.6	31.3	50.9	0.13
Hiram Walker & Sons (Scotland) plc	31.7.84	35.7	12.5	5.1*	14.3	40.8	(0.17)
Invergordon Dists (Holdings) plc	31.12.84	4.1	1.5	0.3	7.3	39.5	0.21
Wm Lawson Distillers Ltd	31.12.84	2.1	0.7	1.3*	61.9	87.5	0.12
Long John International Ltd	2.3.85	6.0	2.1	2.5	41.7	47.6	0.92
Macallan Glenlivet plc	31.12.84	0.8	0.3	0.5*	62.5	100.0	0.07
Macdonald Martin Distilleries plc	31.12.84	2.0	0.7	1.2*	60.0	87.5	0.36
Stewart & Son of Dundee Ltd	5.3.85	0.9	0.3	0.3	33.3	50.0	0.18
William Teacher & Sons Ltd	5.3.85	10.7	3.8	5.0*	46.7	66.7	0.93
Whyte & Mackay Distillers Ltd	30.9.84	2.3	0.8	2.4*	104.3	taxable loss	0.17

* estimate

Arthur Bell & Sons plc, IDV (Export) Ltd, Inver House Distillers Ltd, and Chas MacKinlay & Co Ltd did not have the above data currently available.

Effective Rate of Tax after COSA:

Unweighted Average: 58.7% Weighted Average: 45.7%

companies. The first group consists of 25 companies who themselves produce current cost accounts. The second is composed of 23 companies who do not publish current cost accounts and for whom COSA was estimated using the method detailed in Appendix 1.

6.9 The results of the analysis can be summarised as follows:

	Assumed Tax Rate %	Effective Tax Rate After COSA %	Difference %
Whisky Companies	35	46	+11
Companies producing CCA	35	39	+4
Companies not producing CCA	35	38	+3

All figures refer to the weighted average for the group of companies concerned. This clearly shows that the whisky industry because of its stockholding policies will suffer significantly higher effective tax rates than other industrial classifications.

6.10 The industry accepts that having greatly simplified the system of corporation tax, the Chancellor does not wish to return to a regime riddled with exceptions. However, unique circumstances require unique treatment and Scotch Whisky is certainly in this category.

6.11 The uniqueness of the product is, indeed, enshrined in the 1915 Immature Spirits Act as the industry has a statutory requirement to hold its stocks for a minimum period of three years. It may be argued, ignoring quality considerations, that the industry makes a commercial decision to hold stocks beyond this period, and should suffer the discriminatory tax implications and financial consequences of such a decision, but until three years has passed it has no such choice. The law requires it to hold whisky in stock for a minimum three year period.

6.12 In view of this, it is proposed that each year companies should have relief, measured by applying the current annual inflation factor (the RPI) to the opening balance sheet value of all stocks of maturing single whiskies distilled in the previous three years only. In this manner an allowance would be given related only to the statutory maturation period.

6.13 Had this system applied previously, its value to the industry in 1985 would have been of the following order, assuming corporation tax at 35%:

(a) Malt Whisky

Year	Volume Warehoused	Cost Incl. Storage Chgs.	Balance Sheet Value
	m la	p per la	£m
1982	96	90	86
1983	93	95	88
1984	98	100	98

(b) Grain Whisky

Year	Volume Warehoused	Cost Incl. Storage Chgs.	Balance Sheet Value
	m la	p per la	£m
1982	151	48	72
1983	145	52	75
1984	154	55	84
			503

(c) Relief

say 5.5% x £500 m = £27.5 m @ 35% = £9.6m

6.14 We should emphasise that the above proposal would still leave the industry with a higher effective rate of corporation tax than other industries. This, we consider, is manifestly unfair.

6.15 Frankly, the industry requires a taxation structure that takes into account the effects of inflation on stocks held for prolonged periods, instead of the discriminatory situation at present. We ask for recognition of our unique problem and, in doing so, have tried to formulate a reasonable proposal which would involve relatively little cost to the Exchequer and would not have a 'knock-on' effect on other claims. The legal requirement to hold whisky stocks for three years is unique and provides a valid case for special treatment through a "statutory maturation allowance" as proposed.

7.0 DUTY DEFERMENT

7.1 To facilitate collection of excise duty on alcoholic drinks, the tax is charged not at the moment of purchase by the consumer, but an average of four weeks after withdrawal from bond. There is an interval of, on average, a further eight weeks between payment of the tax by the trader and its recovery from the consumer. The trader is, therefore, effectively borrowing to finance the cost of tax collection, this being two-thirds of the period between clearance from bond and cash collection.

7.2 This is an ongoing commitment, representing a financial burden on the industry which could be avoided, or substantially alleviated by the Government by further deferment of the collection date. This would involve a delay in revenue collected in the year in which the change was made, but would add nothing to the administrative costs of revenue collection. (Parliamentary answer by Mr B Hayhoe - Hansard 30th April 1985 - Column 96.)

7.3 The treatment accorded to the UK spirits industry compares very unfavourably with that of our competitors within the European Community, the respective deferment periods being shown in Table 7.1.

Table 7.1

Tax Deferment Periods on Spirits

United Kingdon	1 month
Belgium	4 months
Luxembourg	2-6 months
Denmark	45 days
France	2 months
West Germany	3 months

Source: Parliamentary answer from Mr B Hayhoe - Hansard 30th April 1985.

7.4 The duty deferment accorded to European competitors places the UK industry at a further comparative tax disadvantage. In view of this, we request that an immediate concession of an additional 28 days deferment be granted on the existing period. Such a move would mean that the trade would not be asked to finance more than the average one month of the cost of duty collection. This would have the advantage of placing UK practice on a framework more consistent with existing Community practice, and would provide a vehicle through which the industry's financial burden in the home trade could be lightened.

APPENDIX 1:

CALCULATION OF COSA FOR COMPANIES NOT PRODUCING CCA

1.1 To calculate COSA for companies not producing CCA is not an easy task. Three elements are required:

i) Opening and closing stock figures
ii) Average age of stock
iii) Appropriate price index for stocks

Information is not readily available on all three elements and approximations have therefore had to be made. The resulting COSAs can therefore only be regarded as estimates.

Assumptions

1.2 i) Opening and closing stock figures were taken from the most recently published accounts of the companies concerned, per Datastream.

ii) The average age of both opening and closing stock was estimated by reference to the Stock : Turnover ratio in each year. Turnover figures for this purpose were also taken from Datastream.

iii) In the analysis the Retail Price Index was used for all companies.

1.3 A sample of 19 quoted companies was selected at random from within the industrial classifications previously used for the sample of companies which did produce CCA. A further 4 companies were selected, again at random, from two previously unused classifications (namely Timber and Stores-Multiple). This gave a total sample of 23 companies. One of the industrial classifications orginally selected was that of building. Different accounting treatments of long-term work-in-progress are however particularly prevalent in the building industry, making the estimation of COSA susceptible to significant error. For this reason companies in the building sector have been omitted from the sample defined above.

Results

1.4 Table 1.1 gives details of changes in the effective rate of tax brought about by deducting the COSA (calculated on the basis outlined above) from pre-tax profits.

Table 1.1

Effects on Tax Rate of COSA

Name	Year Ended	Pre-tax Profit £000s	Tax at 35% £000s	Cost of Sales Adjustment £000s	Adjusted Tax Rate %	Change to Effective Tax Rate
Brewers						
Belhaven Brewery	3/85	1,352	473	37	36	+ 1%
Scottish & Newcastle	4/85	63,200	22,120	4,070	37	+ 2%
Food Manufacturing						
Bernard Matthew	12/84	5,080	1,778	1,026	44	+ 9%
Tate & Lyle	9/84	61,500	21,525	6,852	39	+ 4%
Unigate	3/85	62,600	21,910	7,448	40	+ 5%
Food Retailing						
Associated Dairies	4/84	104,505	36,577	4,988	37	+ 2%
Hintons	3/84	1,910	668	450	46	+11%
Tesco	2/85	81,504	28,526	8,840	39	+ 4%
Health & Household Products						
Smith & Nephew	12/84	49,739	17,409	3,114	37	+ 2%
Fisons	12/84	46,300	16,205	3,716	38	+ 3%
Leisure						
Queen Moat Houses	12/84	6,562	2,297	64	35	-
Mount Charlotte	12/84	10,027	3,509	28	35	-

Table 1.1 (contd.)
Effects on Tax Rate of COSA

Name	Year Ended	Pre-tax Profit £000s	Tax at 35% £000s	Cost of Sales Adjustment £000s	Adjusted Tax Rate %	Change to Effective Tax Rate
Paper & Packaging						
DRG	12/84	24,700	8,645	4,746	43	+ 8%
Wm Sommerville	5/85	359	126	60	42	+ 7%
Tobacco						
Dunhill	3/85	15,405	5,392	1,424	39	+ 4%
Chemicals						
Croda Int	12/84	19,386	6,785	2,677	41	+ 6%
Ellis & Everard	4/85	3,589	1,256	420	40	+ 5%
Electricals						
Dubilier	9/84	5,533	1,937	430	38	+ 3%
Electronics						
Racal	3/85	133,305	46,657	9,892	38	+ 3%
Timber						
Aaronson Bros	9/84	3,818	1,336	655	42	+ 7%
May & Hassell	3/85	81	28	1,002	Effective Loss	
Stores - Multiple						
John Menzies	2/85	17,600	6,160	1,545	38	+ 3%
Marks & Spencer	3/85	303,100	106,085	11,041	36	+ 1%

Weighted Average Adjusted Tax Rate: 37.7%

1.5 Comparing these results firstly with the sample of quoted companies who themselves produced CCA, draws attention to the following points:

i) Food manufacturing: one of the companies for which COSA was estimated experienced a significantly greater change in effective tax rate than others in this category. This may be a function of size as the company concerned was considerably smaller (in turnover and profit terms) than other companies within this classification.

ii) Paper & Packaging: Chemicals : the companies within these classifications for which COSA was estimated showed slightly greater changes in effective tax rates than the companies who produced their own CCA.

iii) At 37.7% the weighted average of tax rates after COSA for this group of companies, is slightly lower than that for the sample of CCA producing companies (38.9%). This may be seen as slight support for the view that those companies producing CCA do so because their business results are more significantly affected by inflation than are those of the non-CCA producing companies.

1.6 Turning now to a comparison of results with those for the whisky industry, the following points can be made:

- none of the other industrial classifications considered, experienced such a consistently high level of increases in effective tax rates;

- it appears that companies within the timber industry experience significant tax effects. This is due to the lengthy periods for which stock is held by such companies (although, unlike the whisky industry there is no legal requirement for them to do so). However, details were obtained for only two timber companies and from such a limited base only tentative conclusions can be drawn on this sector;

- the weighted average of tax rates after COSA for the whisky industry, of 45.7%, is significantly higher than those of the other two groups studied.

1. [initials] 2. [initials]

Any sign of response?

Ro 4/4

PM

10 DOWNING STREET

From the Private Secretary

24 March 1986

To note letter below. Ro 25/3

Phil,
Mr Robson does not think we need to put any input into this
[initials] 7/4

I enclose a copy of a letter which the Prime Minister has received from David Gent, Director General of the Motor Agents Association.

I should be grateful if you would provide a draft reply for the Prime Minister's signature, to reach this office by Monday 7 April.

I am sending copies of this letter and its enclosure to Philip Wynn Owen (HM Treasury) and Stephen Sklaroff (Department of Energy).

Timothy Flesher

Miss Catherine Bradley,
Department of Trade and Industry.

CH/EXCHEQUER

REC.	25 MAR 1986
ACTION	MR ROBSON (Pl. note No. 10 deadline)
COPIES TO	CST, FST, MST, EST
	SIR P. MIDDLETON
	SIR T. BURNS
	MR CASSELL, MR MOORE
	MR MONCK
	MR SHAW
	MS. LEAHY

25/3

From the Director General

Motor
Agents Association
In Association with the
Scottish Motor Trade Association
201 Great Portland Street
London W1N 6AB
Telephone 01·580·9122
Telex 261962

DG/H302B/DO

21 March, 1986 R24/3

Rt Hon Margaret Thatcher MP
Prime Minister
10 Downing Street
London SW1

Dear Prime Minister

You have been reported as making comments which, in effect, advise members of the public not to buy petrol from retail sites which pass on the 7.5p increase in tax introduced in this year's Budget.

You may not be aware that:

- in most cases (other than perhaps a small number of relatively large independent petrol retailers who can negotiate special terms) the oil companies largely determine the prices at the pump;

- the great majority of petrol retailing sites are operated by small independent businessmen of the kind it is this Government's policy to foster and encourage. They have to accept all the risks involved in such a situation, but are at the same time compelled to operate within constraints laid down by their supplying companies;

- petrol retailer margins are among the constraints determined by the petrol companies, are reviewed relatively rarely, and do not normally either improve when international oil prices fall - nor are they adjusted upwards when oil company price increases or tax increases impact on retailers' stocking and related finance costs.

/2.

Motor Agents Association Ltd
Registered Office
201 Great Portland Street
London W1N 6AB
Registered in England Number 133095

Therefore, customer resistance to posted price increases reflecting the new tax rate will directly impact on small businessmen who are powerless to do anything about the situation in which they find themselves.

The Government itself is directly responsible for this powerlessness on two counts:

- there is a major weakness in British competition law, in that it does nothing to protect individual retailers against pressure or unreasonable demands from large, often multi-national suppliers to them and, in fact, positively inhibits such retailers from working together and taking joint positions in seeking to improve their supply terms;

- the Director General of Fair Trading seems to feel so inhibited by the present circumstances under which he operates that he has actively resisted requests for assistance in persuading the major oil companies to update and review the terms of the (petrol company appointed retailer) Licensee Code of Practice originally prepared under his auspices.

The position is made worse by the fact that although the Government has promised a review of the Restrictive Trade Practices legislation, your Ministers have so far failed to take active steps to implement it.

Finally, a Prime Minister who is rightly in favour of maximum acceptance of individual responsibility should recognise that:

- if a Chancellor of the Exchequer decides to increase the tax rate on petrol or any other commodity, he should be prepared to accept the natural consequences of his action, and

- if your theory of competition is right, and national competition legislation is soundly based, competitive forces will ensure that oil companies and others will react to falls in feed stock prices in a manner that responsibly reflects both their interest in maintaining customer loyalty and their responsibility to their shareholders. Government should not need to intervene in commercial pricing by either advice or diktat.

I am making the contents of this letter to you public in the hope that consumers, as well as you and your Ministers, will become better informed as to the facts of the situation, and that your Ministers will now take more determined action to rectify the present deficiencies in this country's Competition legislation.

Yours sincerely

David Gent

David Gent

McKenzie
27/2

ITEM: EXCISE DUTIES: RATES

STARTERS NUMBER: 1

CLASSIFICATION: A

DEPARTMENT: CUSTOMS AND EXCISE

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
+£760m in 1986-87 +£805m in a full year	Nil	Yes. Up to 8 separate resolutions	2 pages and 12 pages of schedule

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
Chancellor				

BACKGROUND AND COMMENTS

This assumes revalorisation of all specific excise duties by 5 per cent, the inflation rate assumed for the 12 months to December 1985.

The estimate of revenue yield includes Vehicle Excise Duty for which the official Treasury (FP) has the policy responsibility.

Of the estimated length of legislation, all but about 1 page plus 1 page of schedule is attributable to VED.

A submission on the excise duty rates will be made in the normal way nearer the time of the Budget.

Official in lead:	P G WILMOTT	2913-5023
Official in support:	J P BONE	2913-5028
FP contact:	K ROMANSKI	233 5237

PAGE NO:

ITEM: VAT: REVALORISATION OF REGISTRATION AND DEREGISTRATION LIMITS

STARTERS NUMBER: 2

CLASSIFICATION: B2

DEPARTMENT: CUSTOMS AND EXCISE

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Negligible cost	Nil	No	SI (assuming no increase in real terms)

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
Chancellor/MST				

BACKGROUND AND COMMENTS

The VAT registration thresholds are intended to relieve the smallest businesses from the obligation to register and account for VAT. The VAT Act 1983, Schedule 1, paragraph 12, provides that increases in the VAT registration and deregistration thresholds can be made by Treasury Order. If such an Order were made at the time of the 1986 Budget in line with forecast inflation we estimate that the threshold could be raised from £19,500 to about £20,500.

This would do no more than maintain the real value of the limit at its 1973 level. Our right to do even this is, however, disputed by the European Commission which claims that indexation should be from the day on which the EC Sixth VAT Directive was implemented (1 January 1978); it is calculated on that basis that our 1986 registration limit should not exceed £15,120. The Commission is currently considering whether to issue a Reasoned Opinion against the UK.

The White Paper "Lifting the Burden" explained the Government's view that EC Member States should have more flexibility to raise their VAT threshold if they wish. This goal is being pursued via the UK deregulation initiative in the EC.

The interdepartmental working group, set up to discuss the optimum level of the VAT registration limit in the UK, submitted its final report to the Chancellor of the Exchequer on 11 November 1985.

Official in lead:	P TREVETT	2019 6285
Official in support:	R A STOREY	2019 7127
FP contact:	K ROMANSKI	233 5237

ITEM: VAT: MOTORING EXPENSES

STARTERS NUMBER: 7

CLASSIFICATION: C

DEPARTMENT: CUSTOMS AND EXCISE

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
+ £25m in 1986-87 +£50m in a full year	Nil	No	One page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	5.09.85 8.10.85			

BACKGROUND AND COMMENTS

In January 1985 the Department attempted to introduce changes in the way in which the private motoring element of business cars is treated for VAT purposes. As a result of representatives these changes were withdrawn and Ministers stated that consultations would take place before any further change. As a result of these consultations, Customs and Excise have concluded that the best way in which to obtain more revenue from private use of business cars would be to employ a simplified scale of the kind used by Inland Revenue in taxing the benefit of cars and free petrol. This would have the advantage that no mileage records would need to be kept and would lead to greater equity of treatment. The MST approved the issue of a consultation document on 10 October and it was discussed on 18 October. The agreement of the EC Commission will need to be obtained and a submission was made to UK Rep on 15 October and is now lodged with the Commission. Representations arising from the consultations have now been examined. A meeting with the EC Commission has been arranged for 22 January. A further submission to the MST will be made shortly after that meeting.

Official in lead:	E N TAYLOR	2913 5295
Official in support:	G J ELANDER	2913 5313
FP contact:	K ROMANSKI	233 5237

BUDGET SECRET

ITEM: VAT: AVOIDANCE BY DISAGGREGATION

STARTERS NUMBER: 8

CLASSIFICATION: C

DEPARTMENT: CUSTOMS ANDD EXCISE

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
+15-20 (see below)	Nil	No	½ page OR 3 lines plus regulations

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	25.9.85	1.10.85	19.12.85	

BACKGROUND AND COMMENTS

The VAT registration threshold, which is intended to relieve the smallest businesses from the obligation to register and account for VAT, is being manipulated by artificially dividing what would normally be considered to be a single business into a number of parts, each of which trades at a level below the registration threshold.

There is no question of preventing the bona fide registration of genuinely separate businesses. However, following examination of the growing problem by an internal Customs working party, we seek authority for legal provision to enable us to stop such cases as a company which found it worthwhile to split itself into 40 separate firms each trading for one or two weeks a year, and the artificial disaggregation of a club's gaming machine and/or bar activities from the other activities of the club. Advice on such schemes is currently being advertised for sale.

The revenue loss at present is impossible to gauge accurately but the £15-20 million is the nearest estimate we are able to make.

Official in lead:	P TREVETT	2019 6285
Official in support:	D C HEWETT	2019 7135
FP contact:	K ROMANSKI	233 5237

PAGE NO:

CONFIDENTIAL

41/1a

ITEM: VAT: DIRECTORS' LIABILITY

STARTERS NUMBER: 9

CLASSIFICATION: C

DEPARTMENT: CUSTOMS AND EXCISE

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Negligible	Negligible	No	Short clause (less than 10 lines)

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST				

BACKGROUND AND COMMENTS

Under Section 171(4) of the Customs and Excise Management Act 1979, a director may be made liable for a criminal offence committed by a corporate body where that offence is proved to have been committed with the consent or connivance of that director. Keith Committee VAT recommedation 35(d) proposed that this section of the law should also apply to liability for civil penalties. The Government accepted the view that the time was not appropriate for legislating for this recommendation in the 1985 Finance Act, in the light of the Insolvency Bill discussions taking place on penalising a director, on liquidation of a company, for wrongful trading. As a result the penalty provision in s. 13 FA 1985 for the civil treatment of VAT evasion is less effective because it cannot apply against the director of a company responsible for the evasion.

The Insolvency Bill was given Royal assent on 30 October 1985 and we doubt whether previous sensitivities about making directors answerable for the activities of their companies will apply in 1986. (We are seeking confirmation that officials in other interested departments share this view.) By making directors responsible for their company's VAT evasions this proposal seeks to apply a more limited version of recommendation 35(d). Directors would become liable to the civil penalty for VAT evasion in s. 13FA 1985 although not to the other penalties contained in sections 14-17 FA 1985 which deal with other civil infractions. (Section 13 concerns evasion where a person's conduct involves dishonesty; the others are absolute offences.)

Official in lead: P HOGG 2238 245

Official in support: G TAYLOR 2238 423

FP contact: K ROMANSKI 233 5237

PAGE NO:

BUDGET SECRET

ITEM: **VAT: DIRECT EXPORTS BY SUPPLIER**

STARTERS NUMBER: 11 **CLASSIFICATION:** C

DEPARTMENT: Customs and Excise

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Nil	Nil	No	7-8 lines

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	03.12.85	10.1.86		

BACKGROUND AND COMMENTS

A provision is required to allow the Commissioners to make Regulations prescribing the conditions attaching to goods exported directly by the supplier. Article 15(1) of the VAT Sixth Directive requires Member States to exempt the supply of goods exported direct by the supplier under conditions which Member States "shall lay down for the purpose of ensuring the correct and straightforward application of such exemptions and of preventing any evasion, avoidance or abuse". In the UK VAT relief in such circumstances is governed by Section 16(6) of the VAT Act 1983, but the Section does not lay down conditions nor does it allow subordinate legislation to be made laying down conditions. Our legal advice is that implementation of the Directive by administrative menas (we lay down conditions in our Public Notice) is insufficient; European Court judgements indicate that Directives must generally be implemented by binding means. Amendment of the VAT Act is required to provide the Commissioners with powers to impose conditions with statutory force.

Official in lead:	B J COCKERELL	2913 5319
Official in support:	R A FLAVILL	2913 5327
FP contact:	K ROMANSKI	233 5237

ITEM: VAT: TRANSFER OF IMPORT RELIEF AND OF ASSOCIATED OBLIGATIONS

STARTERS NUMBER: 14

CLASSIFICATION: C

DEPARTMENT: Customs and Excise

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Nil	Nil	No	5 lines

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	03.12.85	10.1.86		

BACKGROUND AND COMMENTS

A provision is required to allow the transfer of VAT import relief and of its obligations to a person other than the original importer. This requirement stems from "transfer of relief" provisions in Directives 83/181 (VAT relief on certain final importations) and 85/362 (VAT temporary importation relief). Explanatory Memoranda on both Directives have referred to the need for primary legislation. (A Treasury order was laid on 8 November 1985 which came into effect on 1 January 1986, requiring fulfilment of our obligations.) No consultative document has been issued, but forthcoming Public Notices will mention the availability of this transfer facility.

Official in lead: B J COCKERELL 2913 5319

Official in support: M C GREEN 2913 5320

FP contact: K ROMANSKI 233 5237

ITEM: VAT: LONG-TERM LETTINGS OF ACCOMMODATION

STARTERS NUMBER: 15 **CLASSIFICATION:** C

DEPARTMENT: Customs and Excise

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
+ £10m	No actual saving of staff but this measure would lead to a reduction in time spent in dealing with the complexities which arise from the present legislation	No	5-6 lines

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	8.10.85	10.1.86		

BACKGROUND AND COMMENTS

A reduced tax value provision operates from the 29th day for occupations of hotel or similar bedroom accommodation in excess of 28 days. There is no relief for the boarding element of the overall charge but the value for VAT of the balance of the total charge, ie for accommodation and other facilities, is reduced by up to 80 per cent. The intention behind this relief was to allow long-term residents in hotels and similar accommodation (eg pensioners living in hotels and boarding houses; low paid workers living in hostels) a relief roughly equivalent to the exemption available for ordinary residential rents. However, contrary to these intentions the lack of precision in the legislation has required the relief to be extended to any long term supplies of accommodation in hotels, including block lettings to tour operators.

In practice, apart from unregistered individuals, the main beneficiaries have been overseas holiday companies and their clients, who should be required to pay VAT on the same basis as UK citizens or foreign individuals arranging their own hotel accommodation. It is difficult to justify such a relief on grounds of equity or logic in either EC or domestic contexts. The law needs to be amended in such a way as to implement the original intention to afford relief only to individuals, and not to corporate bodies or in respect of non-bedroom accommodation.

Official in lead: B J COCKERELL 2913 5319

Official in support: G R BURGESS 2913 5346

FP contact: K ROMANSKI 233 5237

PAGE NO:

BUDGET SECRET

ITEM: **EXCISE DUTIES: BEER DRAWBACK**

STARTERS NUMBER: 16

CLASSIFICATION: C

DEPARTMENT: Customs and Excise

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Nil	Negligible	No	10 lines

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	9.8.85	11.9.85	12.12.86	

BACKGROUND AND COMMENTS

Amendment of the law would enable traders to off-set beer drawback against duty payable. This would speed up payment of drawback and reduce the administrative cost to Customs and Excise the saving of official time spent in checking, in the abolition of forms, and in reduction in accounting.

Official in lead: W D WHITMORE 2913 5072

Official in support: R J CAIN 2913 5082

FP contact: K ROMANSKI 233 5237

PAGE NO:

BUDGET SECRET

ITEM: EXCISE DUTIES: SPOILT BEER RELIEF

STARTERS NUMBER: 17

CLASSIFICATION: C

DEPARTMENT: Customs and Excise

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Negligible cost	-5 to -10 man hours (see below)	No	5 lines

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	9.8.85	11.9.85	12.12.85	

BACKGROUND AND COMMENTS

The amendment would remove the condition in Section 46(2) of the Alcoholic Liquor Duties Act 1979 that beer must have become accidentally spoilt to be eligible for relief. The relief amounts to only about 0.5 per cent of the total revenue for beer but because of the difficulty of differentiating between eligible spoilt and ineligible waste beer it accounts for about 17 per cent of the manpower used on control of beer duty. In return for making the relief unconditional the trade have suggested that the repayment gravity be reduced by 1^o; on this basis Customs and Excise have calculated that the change would not cost more than £1 million. The proposals would allow radical simplification of documentation and control, with a consequent increase in efficiency and better use of official resources.

The reduced workload on Customs & Excise staff would be taken into account, in future scheming of Excise work in the outfield. It would contribute to savings of whole posts over time.

Official in lead:	W D WHITMORE	2913 5072
Official in support:	R J CAIN	2913 5082
FP contact:	K ROMANSKI	233 5237

ITEM: EXCISE DUTIES: LICENCES

STARTERS NUMBER: 18

CLASSIFICATION: C

DEPARTMENT: Customs and Excise

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Nil	Nil	No	1½ page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	8.11.85	12.11.85	17.1.85	

BACKGROUND AND COMMENTS

The amendment would abolish certain licences in the alcoholic drinks legislation and make the remaining licences free and not required to be renewed annually. This would reduce the cost of administering these licences by removing the need to account for small sums of money and to chase up and deal with annual renewals.

Official in lead:	W D WHITMORE	2913 5072
Official in support:	J R TULLBERG	2913 5085
FP contact:	K ROMANSKI	233 5237

ITEM: EXCISE DUTIES: BETTING AND GAMING (NORTHERN IRELAND)

STARTERS NUMBER: 19 **CLASSIFICATION:** C

DEPARTMENT: Customs and Excise

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Negligible gain	Negligible addition	No	1/3 page clause + up to 2 pages schedule

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	25.11.85	28.11.85	30.12.85	

BACKGROUND AND COMMENTS

A certain amount of bingo is already promoted commercially in Northern Ireland despite the lack of legal sanction. This is untaxed since the NI revenue law - the Miscellaneous Transferred Excise Duties Act (Northern Ireland) 1972 (MTEDA) - naturally contains no provision for bingo duty. As a result of the Betting, Gaming, Lotteries and Amusements (Northern Ireland) Order 1985, commercial bingo in Northern Ireland can be expected to increase rapidly and there is no good reason why it should not be charged with bingo duty in the same way as bingo promoted in Great Britain. It is therefore proposed to extend the relevant provisions of the Betting and Gaming Duties Act 1981 (BGDA) to Northern Ireland so that the same revenue law will apply throughout the United Kingdom.

It seems sensible at the same time to complete the unification of the legal provisions (begun this year in respect of gaming machine licence duty) by revoking the provisions of MTEDA relating to the betting duties and applying the corresponding provisions of BGDA to Northern Ireland, with no significant practical implications. There would then be a single Act applying throughout the United Kingdom. (This additional proposal should not substantially increase the length of the schedule needed in any case for bingo duty, and will reduce the space required in future Finance Bills for changes in betting and gaming duties.)

Staffing implications are difficult to quantify, but the extra work involved could result in some small additional staffing requirements.

Official in lead: T M JENKINS 2913 5050

Official in support: R F J ATKINS 2913 5248

FP contact: K ROMANSKI 233 5237

BUDGET SECRET

ITEM: EXCISE DUTIES: LEGAL EVIDENCE BY CERTIFICATE

STARTERS NUMBER: 20

CLASSIFICATION: C

DEPARTMENT: Customs and Excise

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Nil	Negligible saving (Avoidance of additional staff)	No	½ page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	10/12/85	10/1/86	23/1/86	

BACKGROUND AND COMMENTS

The provision is intended to facilitate, and to avoid waste of resources in, producing evidence that returns and payments of betting and gaming duties have not been made. Similar provision already exists for VAT and car tax under which a certificate of the Commissioners is sufficient evidence unless the contrary is proved. This was unnecessary and inappropriate for betting and gaming duties when most payments went to local offices and a substantial proportion were required in advance. Now that two of the duties - including the main areas of enforcement action - have already been centralised and payment in arrears has been extended to cover all bookmakers, the need for evidence arises more often (because of the more effective enforcement action now possible) and its production has become more difficult without the facility to do this by certificate. The preparation of formal witness statements for each case (often in the event unused) and physical attendances at court threaten to place an intolerable burden on the existing resources of the central units. The provision now sought would remove this threat; it would also enable evidence to be provided in the simplest way and should be welcomed by the courts as well as Customs and Excise.

Official in lead: T M JENKINS 2913 5050
Official in support: E J S HERON 2913 5063
FP contact: K ROMANSKI 233 5237

BUDGET SECRET

ITEM: VAT: PROVISION TO APPLY PENALTIES FOR BREACHES OF REQUIREMENTS OF TREASURY ORDERS

STARTERS NUMBER: 21

CLASSIFICATION: C

DEPARTMENT: CUSTOMS AND EXCISE

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Nil	Nil	No	1/2 lines

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	03.12.85	10.1.86		

BACKGROUND AND COMMENTS

A provision is required to apply penalties for breaches of requirements of Treasury Orders.

At present the civil penalties provided for in the Finance Act 1985 for breaches of regulatory provisions cannot be applied in respect of breaches of requirements imposed by Treasury Order.

It is proposed to remedy this deficiency since it is expected that Treasury Orders will be used (rather than Commissioners' Regulations) to implement the requirements of forthcoming European legislation which is not directly applicable per se, eg the Value Added Tax (Temporarily Imported Goods) Relief 1985 and Council 1985 and Council Directive 85/362/EEC (17th VAT Directive).

This amendment will result in improved trader compliance and the collection of limited amounts as penalties but otherwise has no effect on revenue yield or staffing.

Official in lead:	B J COCKERELL	2913 5319
Official in support:	M C GREEN	2913 5320
FP contact:	K ROMANSKI	233 5237

ITEM: **VAT RELIEFS FOR THE DISABLED: EXTENSION TO EMERGENCY ALARM SYSTEMS AND LFITS**

STARTERS NUMBER: 22

CLASSIFICATION: B2

DEPARTMENT: CUSTOMS AND EXCISE

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
-£3 million	Nil	No	SI

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	20.09.85 12.11.85	10.1.85		

BACKGROUND AND COMMENTS

Group 14 of Schedule 5 of the VAT Act 1983 zero-rates the supply of certain goods to the handicapped for domestic or personal use, or to a charity or making available to the handicapped. Ministers have agreed that the relief should be extended to cover also the supply of emergency alarm call systems and the service of installation of lifts, for the benefit of handicapped persons.

It was originally intended to introduce these reliefs by Order to come into effect on 1 January 1986, but Ministers have decided that they should be kept as Budget 'lollipops'. A negative resolution SI will be required.

Official in lead:	P S JENKINS	2913-5387
Official in support:	A H HAMPSON	2913 5390
FP contact:	K M ROMANSKI	233 5237

BUDGET SECRET

ITEM: VAT: DISPOSAL OF CAPITAL ASSETS

STARTERS NUMBER: 24

CLASSIFICATION: C

DEPARTMENT: Customs and Excise

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Nil	Nil	No	1-1½ pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST	30.1.86	4.286	14.2.86	

BACKGROUND AND COMMENTS

The High Court judgement in the Hedges and Butler case in December 1985 has seriously restricted the Commissioners' powers to inspect records kept by warehouse-keepers and proprietors of warehoused goods. The inspection of records which are kept by the trader for the purpose of his business is vital to the economic control of excise warehouses and the proposed amendment does no more than achieve what was intended when the existing provisions were drafted. The new provision will require the production only of records which the trader keeps for trade and other purposes.

The present regulations are constrained by a requirement that they relate only to goods which have been warehoused and an extension of this to include goods which are to be warehoused and to goods which are removed from warehouse otherwise than on payment of duty is also provided for.

Official in lead:	W D WHITMORE	2913 5072
Official in support:	K G MATHEWS	2913 5089
FP contact:	K M ROMANSKI	233 5237

ITEM: INCOME TAX: THRESHOLDS AND RATES

STARTERS NUMBER: 101

CLASSIFICATION: A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Depends on decisions		Yes	0.7 pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
Chancellor	19.12.85	30.1.86	3.2.86	

BACKGROUND AND COMMENTS

This topic includes:

thresholds - basic personal allowances
- age allowances
- higher rate thresholds

rates - basic rate and higher rates

Cost of approximately 5½ per cent prices indexation of the thresholds (£1,300 million) is included in the forecast. Generally, at least earnings indexation required to ensure that Revenue staff requirement does not rise next year compared with 1985-86. (For example, had there been no increase in thresholds and allowances in 1985-86, Revenue staff requirement would have risen by 330 in a full year). Options for further reductions in income tax will depend, inter alia, on availability of resources and outcome of current consideration of appropriate strategy for the period up to the changeover to transferable allowances in 1990. Other items for consideration include restructuring of the higher rates.

Official in lead:	B A MACE	2541 6546
Official in support:	A P HUDSON	2541 7349
FP contact:	M D R HAIGH	233 5757

PAGE NO: ____

ITEM: CARS: CAR & FUEL BENEFIT UPRATING & RELATED BREAKPOINTS

STARTERS NUMBER: 102 **CLASSIFICATION:** A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million		Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1986-87	Nil *	+45 to 75**	No	N/A
1987-88	+35*	NIL		
Full Year	+50*	NIL		

* Yield from 10 per cent increase in scale charges

** Once for all transitional cost if breakpoints changed.

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	22.11.85	2.1.86	N/A	N/A
			(secondary legislation to be used)	

BACKGROUND AND COMMENTS

The Chancellor will wish to announce, as usual, the 1987-88 car and car fuel scale charges in his 1986 Budget Speech. The scale charges are invariably increased by way of Treasury Order (subject to negative resolution). Pressure from the industry is mounting to realign the cc breakpoints between benefit charging bands to match the new EEC exhaust emission regulations.

Official in lead: M PRESCOTT 2541 6303

Official in support: P SAVAGE 2541 7764

FP contact: M HAIGH 233 5757

BUDGET SECRET

ITEM: **STAMP DUTY: RATES AND THRESHOLDS**

STARTERS NUMBER: 103

CLASSIFICATION: A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
- £m80 (86/7) - £m180 (87/8)	Negligible	No	0.5

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
EST	4.12.85 (20.12.85)	30.1.86	3.2.86	

BACKGROUND AND COMMENTS

Ministers in favour of a rate reduction for shares only to take effect from Big Bang (27 October 1986) coupled with a broadening of the base (see starters 103A-C and starter 138) to produce a broadly revenue neutral package in 1986-7.

Ministers propose no change to stamp duty on houses.

Official in lead:	D G DRAPER	2541-6646
Official in support:	MISS A M RHODES	2541-6605
FP contact:	M HAIGH	233-5757

CONFIDENTIAL

BUDGET SECRET

ITEM: STAMP DUTY: AMERICAN DEPOSITARY RECEIPTS (ADRs)

STARTERS NUMBER: 103A

CLASSIFICATION: A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
+ £m16 to + £m36	Negligible	Yes	2

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
EST		30.1.86	3.2.86	6.2.86

BACKGROUND AND COMMENTS

Ministers have decided in principle that stamp duty at a higher rate (2½ per cent-5 per cent) should be charged on conversion of shares into ADRs.

Official in lead:

Official in support: (see above)

FP contact:

CONFIDENTIAL

BUDGET SECRET

ITEM: **STAMP DUTY: NON STAMPABLE TRANSACTION**

STARTERS NUMBER: 103B

CLASSIFICATION: A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
+ £m9 /24 1986-7 + £m20/40 1987-8	Negligible	No	3

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
EST	20.12.85	30.1.86	3.2.86	6.2.86

BACKGROUND AND COMMENTS

		1986-7	1987-8
Ministers are considering the following options for broadening the base of the duty on shares to include:			
(i)	intra-account transactions	+ £m2/+7	+£m5/+15
(ii)	transactions in renouncable documents	+ £m5/+7	+£m10/5
(iii)	foreign shares	+ £m2/+10	+£m5/10

This would take the form of a change on share transactions which do not result in the production of a stamped transfer. These changes cannot easily take effect before Big Bang.

Official in lead:

Official in support: (see above)

FP contact:

PAGE NO:

CONFIDENTIAL

BUDGET SECRET

ITEM: **STAMP DUTY: TAKEOVERS ETC**

STARTERS NUMBER: 103C

CLASSIFICATION: A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
£m+20/40	Not yet determined	Yes	2

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
EST	20.12.85			

BACKGROUND AND COMMENTS

Minsiters are considering as part of the stamp duty package on shares proposals involving the withdrawal of the relief for takeovers, the partial withdrawal of the relief for "schemes of reconstruction and amalgamation" and possibly the relief for demergers.

Official in lead:

Official in support: (see above)

FP contact:

PAGE NO:

CONFIDENTIAL

ITEM: Stamp Duty: Purchase of own shares

STARTERS NUMBER: 103D

CLASSIFICATION: A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
+1	(Whole Stamp Duty package + 20)	Yes	0.5

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
EST	30/1/86	3/2/86	18/2/86	

BACKGROUND AND COMMENTS

To withdraw the exemption for the purchase by a company of its own shares.

Official in lead: D G Draper 2541-6646

Official in support: Miss A M Rhodes 2541-6605

FP contact: M D R Haigh 233-5757

PAGE NO:

ITEM: Stamp Duty: Letters of Allotment

STARTERS NUMBER: 103E **CLASSIFICATION:** A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
86/7 + 10 87/8 + 15	(Whole Stamp Duty package + 20)	No	1.0

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
EST	13.2.86			

BACKGROUND AND COMMENTS

Proposal to withdraw exemption from Stamp Duty for Letters of Allotment.

Official in lead: D G Draper 2541-6646

Official in support: Miss A M Rhodes 2541-6605

FP contact: M D R Haigh 233-5757

PAGE NO:

ITEM: Stamp Duty: Bearer Duty

STARTERS NUMBER: 103F **CLASSIFICATION:** A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
NIL	NIL	NO	0.25

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
EST	13/2/86	17/2/86		

BACKGROUND AND COMMENTS

Proposal to maintain current rates for Bearer Instruments (currently charged by reference to rate of transfer duty).

Official in lead: D G Draper 2541-6646

Official in support: Miss A M Rhodes 2541-6605

FP contact: M D R Haigh 233-5757

PAGE NO:

BUDGET SECRET

ITEM: CAPITAL TRANSFER TAX: THRESHOLD AND RATE BAND CHANGES

STARTERS NUMBER: 104

CLASSIFICATION: A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
depends on decisions	depends on decisions	No	1 page at most

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	15.11.85			

BACKGROUND AND COMMENTS

In the absence of a clause, threshold and bands will be automatically indexed, at a cost of £50m (already assumed in the forecast).

Official in lead:	B T HOUGHTON	2541-7290
Official in support:	J P BATTERSBY	2541-6459
FP contact:	M HAIGH	233-5757

ITEM: CAPITAL GAINS TAX: ANNUAL EXEMPT AMOUNT

STARTERS NUMBER: 105

CLASSIFICATION: A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1986/87: nil Full year: - £m10	depends on decisions	No	N/A

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	29.11.85	12.1.86	N/A	N/A

BACKGROUND AND COMMENTS

In the absence of a specific measure, the annual exempt amounts (£5,900 for individuals and £2,950 for most trusts) will increase automatically under the statutory indexation formula. On present projections, the cost of this wil be £m10, which will be taken into account in the forecasts.

Official in lead:	J P B BRYCE	2541-7427
Official in support:	P A MICHAEL	2541-7571
FP contact:	M HAIGH	233-5757

BUDGET SECRET

ITEM: **ACT RATE FOR FINANCIAL YEAR 1986**

STARTERS NUMBER: 106

CLASSIFICATION: A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Yield/cost of 1 per cent change - £m 1986-87 ± 120 1987-88 ± 55 Full Year ± 12 (but see below)	Nil	Yes	2 lines (a ¼ to ½ page if IOT suggestion below adopted)

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST				

BACKGROUND AND COMMENTS

Budgetary matter determined by basic rate of income tax; costings of changes in the IT rate usually take in the effects on the CT yield.

It has also been suggested (by the Institute of Taxation) that the ACT rate could be permanently linked to the basic rate of income tax, thus avoiding need for legislation to fix the ACT rate each year. Last year the Financial Secretary thought this a good idea in principle, but decided to leave it over for reconsideration for 1986.

Official in lead: I R SPENCER 2541-6252

Official in support: A J BOLTON 2541-7517

FP contact: M HAIGH 233-5757

CONFIDENTIAL

BUDGET SECRET

ITEM: MORTGAGE INTEREST RELIEF LIMIT FOR 1986-87

STARTERS NUMBER: 107

CLASSIFICATION: A

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
-	£30,000 Apr 87 + 55 Apr 88 NIL Compared with 85/86 staffing levels	Yes	Few lines
Eventual cost* at 86/87 income levels £m200-300-			

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST				

BACKGROUND AND COMMENTS

Limit needs to be fixed annually in Finance Bill. 1985-86 limit £30,000; last increased in 1983.

If the limit remains at £30,000 additional staff will be required, as shown above, because the number of mortgages above £30,000 is increasing. Most loans above the limit are at present outside MIRAS, so that relief has to be given through PAYE or tax assessments, and this requires more staff to handle. In the longer run the manpower increase will be held down by the requirement in FA 1985 on lenders to bring into MIRAS new loans above the limit from April 1987 onwards.

Staffing estimates above for later years assume that the limit fixed for 1986-87 will then remain unchanged.

* The cost would build up over about 5 years, and include the effect of additional borrowing.

Official in lead:	B O'CONNOR	2541-6218
Official in support:	A C GRAY	2541-6785
FP contact:	M HAIGH	233-5757

CONFIDENTIAL

BUDGET SECRET

ITEM: BOARDING SCHOOL ALLOWANCES & DETACHED DUTY ALLOWANCES

STARTERS NUMBER: 108

CLASSIFICATION: B1

DEPARTMENT: Inland Revenue

	Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1.	BSA -26	Nil in Revenue Saving Negligible in Paying Departments	No	1 (but not in FB as published)
2.	DDA Nil	Nil		

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	6.12.85	16.12.85		

BACKGROUND AND COMMENTS

Tax on Boarding School Allowances to Crown Servants working in the UK is accounted for by departments by "grossing up". This increases the reckonable income of individuals for various purposes, notably the level of student grants. Ministers have decided to legislate to exempt BSA from tax from April 1986.

Detached Duty Allowances are taxable when paid for more than 12 months. By an unpublished ESC these are not taxed on Crown Servants at present. Ministers have also decided to legislate to exempt these allowances from tax from April 1986.

For both BSA and DDA it may be possible to relegate detailed definitions of allowances to be exempted to regulations by Statutory Instrument, particularly as definitions do change from time to time.

Official in lead:	M PRESCOTT	2541 6303
Official in support:	S S WILCOX	2541 7211
FP contact:	M HAIGH	233 5757

CONFIDENTIAL

BUDGET SECRET

ITEM: **REMOVAL OF RESTRICTIONS ON DISCLOSURE OF INFORMATION BETWEEN THE INLAND REVENUE AND THE CHARITY COMMISSION**

STARTERS NUMBER: 110

CLASSIFICATION: B1

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Negligible	Nil	No	A few lines

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST (or EST)	22.3.85			

BACKGROUND AND COMMENTS

An official working party on the supervision of charities recommended the removal of restrictions on disclosure of information between the Inland Revenue and the Charity Commission. At present such exchange of information is allowed only in connection with objections to registration or applications for deregistration. Such a provision would considerably assist in tackling a number of tax avoidance schemes in the charity field. The FST was content with the recommendation (28/3/85) with a view to the Finance Bill 1986. There is no public commitment to action.

Official in lead:	C STEWART	2541-7414
Official in support:	MRS E FLETCHER	2541-7784
FP contact:	M D R HAIGH	233-5757

PAGE NO:

BUDGET SECRET

ITEM: AGRICULTURAL BUILDINGS ALLOWANCE: RESTRUCTURING

STARTERS NUMBER: 113

CLASSIFICATION: B1

DEPARTMENT: Inland Revenue

	Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Balance adjustments:	NEG	(+30 by mid 1990s) NEG	No	1.5 pages for balancing adjustments (any more depends on extent of further restructuring)
Exclusion of Farm houses/ cottages	86/7) 87/8) Neg (+£m2-3 by 1990)			

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	13.12.85			

BACKGROUND AND COMMENTS

Ministers announced at Report Stage FB 1985 that a detailed review of the agricultural buildings allowance was being undertaken to consider ways in which the code might be restructured and that proposals to include the introduction of balancing adjustments on disposal would be introduced in the 1986 Bill with a starting date of 1 April 1986.

As part of the review Ministers may want to consider the present treatment of farm houses and farm cottages as well as the possibility of bringing IBA and ABA more closely into line with each other.

Official in lead:	G H BUSH	2541-6287
Official in support:	G A A ELMER	2541-7507
FP contact:	M HAIGH	233-5757

PAGE NO:

BUDGET SECRET

ITEM: **ACCRUED INCOME SCHEME: CONSEQUENTIAL AMENDMENT OF OTHER ANTI-BONDWASHING LEGLISATION**

STARTERS NUMBER: 114A

CLASSIFICATION: B1

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
NIL	NIL	NO	0.3 pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	19.12.85	24.12.85		

BACKGROUND AND COMMENTS

Enacted in Finance Act 1985, the Accrued Income Scheme commences on 28 February 1986. It prevents "bondwashing" (conversion of income into capital by "selling interest"), charging tax on the interest which accrued during a person's ownership of a security even if he sells it before interest becomes payable.

Except for equities and preference shares (which are not covered by the Accrued Income Scheme), old anti-bondwashing rules in Section 469 and 471-75 ICTA 1970 may no longer be necessary. Ministers have already announced that Section 469 will be revised in FB to let-out certain sale & repurchase transactions (Repos.)

Official in lead:	I R SPENCE	2541-6252
Official in support:	A J BOLTON	2541-7517
FP contact:	M HAIGH	233-5757

CONFIDENTIAL

BUDGET SECRET

ITEM: CITY RESTRUCTURING: INCOME TAX AND CGT RELIEFS FOR MARKET MAKERS

STARTERS NUMBER: 114B

CLASSIFICATION: B1

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
NIL	NIL	NO	0.5 to 1.5 page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	19.12.85	24.12.85		

BACKGROUND AND COMMENTS

It is essential to amend statutory reference to "jobbers", a term which will disappear with the "Big Bang". Other terms (eg "brokers") also appear and need to be reviewed. The minimum change necessary would be to translate these reliefs to market-makers and jobbers on the Stock Exchange. But the extension of special treatment to cover market makers and dealers in new markets outside the Stock Exchange needs to be reviewed.

Official in lead:	I R SPENCE	2541-6252
Official in support:	A J BOLTON	2541-7517
FP contact:	M HAIGH	233-5757

PAGE NO:

BUDGET SECRET

ITEM: ACCRUED INCOME SCHEME: TECHNICAL POINTS

STARTERS NUMBER: 114C

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
NIL	NIL	NO	1 to 2 pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	19.12.85	24.12.85		

BACKGROUND AND COMMENTS

Some technical defects have become apparent in the 1985 Accrued Income Scheme legislation, which takes effect on 28 February 1986. These are niggling points but could result in unjustified tax charges on some, and unjustifiable reliefs for others.

Official in lead:	I R SPENCE	2541-6252
Official in support:	A J BOLTON	2541-7517
FP contact:	M HAIGH	233-5757

PAGE NO:

CONFIDENTIAL

BUDGET SECRET

ITEM: **EXTENSION OF RELIEF UNDER SECTION 22(2) FA 1974 FOR PENSIONS PAID TO VICTIMS OF NATIONAL-SOCIALIST PERSECUTION**

STARTERS NUMBER: 115

CLASSIFICATION: B1

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1986-87 - 1 1987-88 - 1	Nil	No	0.3 page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	9.10.85	14.10.85	7.11.85	27.11.85

BACKGROUND AND COMMENTS

The purpose of the change is to increase to 100 per cent the deduction (currently 50 per cent) afforded by Section 22(2) FA 1974 to certain pensions payable to victims of Nazi persecution under special provisions of German and Austrian Law.

The Chancellor asked the Financial Secretary to make this concession a 1986 Budget Starter following representations last year from Sir William Clark MP. In reply to Sir William the Chancellor maintained the previously held view that relief of 50 per cent is fair and reasonable and that any increase would be difficult to justify. There is not therefore any public commitment to action.

In the absence of any reliable information the above costing is only an educated guess. It does however tally with the Association of Jewish Refugees' own estimate.

No staff saving is envisaged because most of the work turns around establishing entitlement to relief, and that will continue to be necessary.

Official in lead: M F CAYLEY 2541-6372

Official in support: G F E COOK 2541-6654

FP contact: M HAIGH 233-5757

CONFIDENTIAL

BUDGET SECRET

ITEM: MINES AND OIL WELLS ALLOWANCES (MOWA)

STARTERS NUMBER: 116

CLASSIFICATION: B1

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1986/87 neg 1987/88 - 45 1988/89 - 40 1989/90 - 35 1990/91 - 30 declining thereafter	Nil	Yes	10 or so pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	19.12.85	24.12.85		

BACKGROUND AND COMMENTS

Following a review of the MOWA code, announced in 1983, a consultative document containing the Government's proposals was published on 16 July 1985. The FST at that time announced (by PQ) that legislation on these proposals would be introduced in the 1986 Finance Bill.

The main effect of the proposals is to bring the MOWA allowances more closely into line with the general system of capital allowances following the changes in 1984 and 1985 Finance Acts. In particular they include the change to straight forward percentage based writing down allowances, on a reducing balance and an incurred basis. It is also proposed for example to repeal certain provisions which have outlived their usefulness, and to take the opportunity to bring secondhand costs of licence interests onshore into line with the regime offshore.

Official in lead:	MRS C HUBBARD	2541-6576
Official in support:	Y S PANG	2541-6250
FP contact:	M HAIGH	233-5757

BUDGET SECRET

ITEM: EMPLOYEE SHARE SCHEMES: USE OF RESTRICTED SHARES

STARTERS NUMBER: 118

CLASSIFICATION: B2

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1986-87: Nil Full Year: Up to £m10	+6 units, declining to +3 by April 1988	Yes (in respect of closure of loopholes)	Up to 3 pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	18.11.85	3.12.85		

BACKGROUND AND COMMENTS

Shares used in employee share schemes approved under the Finance Acts 1980 and 1984 (savings-related and discretionary share option schemes respectively) must not be subject to restrictions under which their employee owners may be required to sell them when they leave their jobs. Many representations have been made on the matter since the discretionary share options scheme provisions in the Finance Act 1984 were published. The Financial Secretary promised during the Finance Bill debates in June 1985 to consider removing this disqualification. Up to four sets of tidying amendments to existing approved scheme legislation, and four loopholes identified in existing legislation relating to unapproved employee share schemes also merit legislative action in their own right. This might conveniently accompany any action taken on the restriction disqualification.

(See also starters 119 and 135).

Official in lead:	J D FARMER	2541 7652
Official in support:	MISS D M GREEN	2541 6457
FP contact:	M HAIGH	233 5757

BUDGET SECRET

ITEM: **EMPLOYEE SHARE SCHEMES: ACCESS FOR CERTAIN COMPANIES CURRENTLY EXCLUDED**

STARTERS NUMBER: 119

CLASSIFICATION: B2

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1986-87: Nil	Nil	No	1 page
Full Year: Up to-£m5			

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	18.11.85	3.12.85		

BACKGROUND AND COMMENTS

Shares used in employee share schemes approved under the Finance Acts 1978, 1980 and 1984 must satisfy certain conditions. One has the effect of preventing the adoption of schemes where compnies have more than one class of ordinary shares, and the class which the company wishes to use does not meet the 'majority test' (the majority of such shares must be held by outsiders, not employees or the company's parent). The effect of this on employee-controlled companies was debated by the 1985 Finance Bill Committee, when the Financial Secretary promised further consideration. Other conditions on scheme shares prevent the use of shares of an unquoted subsidiary of an unquoted parent. A relaxation in the Finance Act 1985 on lines suggested by Save & Prosper was refused, but the Financial Secretary promised the company in July 1985 to consider an amendment if one could be drafted to help more companies. These and similar problems faced by other companies could usefully be considered together.

(See also starters 118 and 135).

Official in lead:	J D FARMER	2541 7652
Official in support:	MISS D M GREEN	2541 6457
FP contact:	M HAIGH	233 5757

PAGE NO:

CONFIDENTIAL

BUDGET SECRET

ITEM: **REMOVAL OF LIMIT ON CHARITABLE DONATIONS DEDUCTIBLE FOR HIGHER RATE TAX PURPOSES**

STARTERS NUMBER: 120

CLASSIFICATION: B2

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
- 2 or 3	+ 5 to 10	No	Uncertain. Likely to be 3 pages minimum, but possibly considerably more depending on extent of safeguards.

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	13.12.85			

BACKGROUND AND COMMENTS

This starter (known to Ministers as the "John Green option") arose out of recent correspondence with Sir Emmanuel Kaye. When a close company makes charitable donations, such donations are apportioned among the members (usually shareholders) of the company, and then taxed if over the (£10,000) limit for charitable donations.

The Chancellor resisted Kaye on the grounds that such apportionment ensures parity of treatment for tax purposes with donors who are not members of a close company. However, he thought that it would be worth considering removing the limit completely. There would however need to be strict rules to ensure that money convenanted reached genuine public charities or was clearly spent on charitable objects.

Official in lead:	C STEWART	2541-7414
Official in support:	MRS E FLETCHER	2541-7784
FP contact:	M D R HAIGH	233-5757

PAGE NO:

CONFIDENTIAL

BUDGET SECRET

ITEM: STAMP DUTY: STOCK EXCHANGE RELIEFS

STARTERS NUMBER: 121 **CLASSIFICATION:** B2

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
NIL	NEG	No	2½ pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
EST	4.12.85		20.12.85	

BACKGROUND AND COMMENTS

Reliefs for market-makers need to be redrawn before the Stock Exchange reforms take effect in the autumn of 1986. (Also see starters 114 and 143.) An announcement is needed this autumn to enable the Stock Exchange to plan for the Big Bang (computer systems need to be redesigned). Issues are:

(i) whether relief should be given to broker/dealers when dealing as market-makers;

(ii) whether relief should <u>not</u> be given to broker/dealers in respect of other transactions;

(iii) If not, whether the relief for sub-sales which is exploited by off-market dealers should be withdrawn; and

(iv) treatment of off-market dealers generally.

Official in lead: D G DRAPER 2541-6646

Official in support: MISS A M RHODES 2541-6605

FP contact: M HAIGH 233-5757

CONFIDENTIAL

41/1e

BUDGET SECRET

ITEM: CTT RELIEFS FOR EMPLOYEE OWNERSHIP

STARTERS NUMBER: 122

CLASSIFICATION: B2

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Cost very difficult to quantify, but probably negligible	NIL	No	2 pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	29.11.85			

BACKGROUND AND COMMENTS

Proposal - pressed by Job Ownership Limited - to extend the existing exemption from CTT for transfers of shares in a company to an employee trust so as to make it apply in any case where the transfer results in the employee trust gaining control of the company, even though the trust does not take the shares directly. FST undertook at Committee Stage last year to hold discussions with officials, with a view to legislation to 1986, but without commitment.

Official in lead:	H B THOMPSON	2541-6334
Official in support:	B K LAKHANPAUL	2541-6567
FP contact:	M HAIGH	233-5757

PAGE NO:

BUDGET SECRET

ITEM: CAPITAL GAINS TAX: RELIEF FOR VENTURE CAPITAL COMPANIES

STARTERS NUMBER: 123

CLASSIFICATION: B2

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
NEG	NIL	NO	8 to 10*

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	17.12.84			

BACKGROUND AND COMMENTS

Ministers have agreed to consider providing CGT exemption for companies providing venture capital. This has been pressed by DTI Ministers and FST has discussed with the British Venture Capital Association. Further information is awaited from them to enable submission to be made to Ministers.

Present stumbling blocks are (possible) length of legislation, scale of managers' remuneration (sought primarily in capital form) and precise definition of qualifying investments (BVCA wish to invest part overseas).

* Possibility of this being shortened by regulations to be considered.

Official in lead: J P B BRYCE 2541-6247

Official in support: V J BAKER 2541-6739

FP contact: M HAIGH 233-5757

CONFIDENTIAL

BUDGET SECRET

ITEM: BUSINESS EXPANSION SCHEME

STARTERS NUMBER: 124

CLASSIFICATION: B2

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Cost/saving, length of legisation, etc depend on the nature and extent of any changes made.		No	Present legislation runs to about 10 pages.

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	19.11.85	16.12.85		

BACKGROUND AND COMMENTS

Longer term future of Scheme (which presently runs until April 1987) has been reviewed, taking account of results from a study by Peat Marwick into additionality. Chancellor has indicated Scheme will continue in some form, but this leaves wide range of options concerning possible changes to its main structure. Numerous other more technical modifications also possible and for consideration.

As yet, no public commitment to action in 1986. It is assumed Chancellor will want to announce plans for Scheme's future in 1986 Budget, but still for decision whether any legislative changes that are needed should be introduced in the 1986 or the 1987 Finance Bill.

Official in lead:	J H REED	2541-6442
Official in support:	D A CARR	2541-6390
FP contact:	M HAIGH	233-5757

CONFIDENTIAL

BUDGET SECRET

ITEM: TAX TREATMENT OF ENTERPRISE ALLOWANCE

STARTERS NUMBER: 125

CLASSIFICATION: B2

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
First year: -£5m Full year: -£25m	No effect	No	A few lines (but longer if transitional provisions needed to cater for those already receiving allowance).

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	15.7.85			

BACKGROUND AND COMMENTS

The Chancellor has asked us to consider exemption of this allowance as a Budget starter and possible lollipop.

Exemption would be a useful benefit for the unincorporated sector.

DTI and DoE Ministers have pressed for the allowance to be taxed under Case VI rather than Case I.

Official in lead:	M J G ELLIOTT	2541-6412
Official in support:	MISS R DYALL	2541-6304
FP contact:	M HAIGH	233-5757

CONFIDENTIAL

ITEM: PRT RELIEF FOR ONSHORE E&A

STARTERS NUMBER: 129

CLASSIFICATION: B2

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
See below	Nil	No	½ page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	15.1.86			

BACKGROUND AND COMMENTS

1985 Finance Act included a provision (Section 90(2)) withdrawing immediate PRT relief for onshore E&A. The smaller companies, led to BRINDEX, continue to press hard for this relief to be reinstated generally, and at a June 1985 lunch the FST agreed to consider any new evidence that onshore E&A activity would be damaged by the Section 90 change.

Some companies have also made the particular point that the change will bite especially hard in areas like the Minches which, though in deep water, are classified as "onshore" for this purpose. Prima facie this case commands some sympathy, and it should be possible - if Ministers so desired - to revise the definition of "onshore" to meet this point. The revenue cost of such a limited amendment is likely to be small.

Department of Energy, who acquiesced in last year's change only with reluctance, are now reviewing the economics of onshore fields in the light of this change. Though they have not yet declared their hand generally, Energy have already expressed some sympathy with the particular "Minches" problem. As with the industry itself, Energy are likely to be looking for any amendment to the Section 90 measure in the 1986 Finance Bill.

Official in lead:	M A HILL	2541-6018
Official in support:	M HAY	2541-7437
FP contact:	M HAIGH	233-5757

BUDGET SECRET

ITEM: BENEFITS IN KIND: THRESHOLD

STARTERS NUMBER: 133

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Depends on decisions		No	N/A

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	15.11.85	3.1.86	N/A	N/A

(secondary legislation to be used)

BACKGROUND AND COMMENTS

Maintenance of the Benefits in Kind income threshold at £8,500 pa increases the numbers of taxpayers chargeable on benefits each year. While increasing the revenue yield this also increases the staff cost for the Revenue and the compliance burden on employers.

Official in lead:	M PRESCOTT	2541 6303
Official in support:	P SAVAGE	2541 7764
FP contact:	M HAIGH	233 5757

CONFIDENTIAL

ITEM: RELIEF FOR OVERSEAS TRAVEL EXPENSES

STARTERS NUMBER: 134

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

	Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1986-87	- £m10	+10	Yes	2 to 4 pages
1987-88	- £m5	+20		
Full year	- £m5	+20		

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	15.7.85	27.11.85	20.12.85	

BACKGROUND AND COMMENTS

Following two consultative documents concerning the relaxation of foreign travel rules, Ministers need to decide the extent, if any, of further relief to be given for overseas travelling and subsistence expenses for UK residents working abroad and expatriates working in the UK; and for UK board and lodging expenses of expatriates and their families.

The high Revenue cost for 1986-87 and 1987-88 relative to full year costs reflect the commitment to backdate relief (but not restrictions) to 6 April 1984.

Official in lead: M PRESCOTT 2541 6303

Official in support: M SISK 2541 6708

FP contact: M HAIGH 233 5757

BUDGET SECRET

ITEM: EMPLOYEE SHARE SCHEMES: EXTENSION OF EMPLOYEES' RIGHTS UNDER SAVINGS-RELATED SHARE OPTION SCHEMES

STARTERS NUMBER: 135

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

	Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1986-87 and Full-Year:	Neg	Nil	Yes	Up to 1 page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	18.11.85	3.12.85		

BACKGROUND AND COMMENTS

Except in special circumstances employees participating in an approved SAYE-linked share option scheme can exercise their options early only if they have been held for at least three years. A number of companies (eg the Comp Air Ltd case represented recently by David Mudd MP) have complained that on a take-over employees can lose their rights if their employing company leaves a group operating such a scheme. This was the subject of a 1985 Budget Starter, when the Financial Secretary agreed that leglislation was warranted, but not in 1985.

(See also starters 118 and 119).

Official in lead: J D FARMER 2541 7652

Official in support: MISS D M GREEN 2541 6457

FP contact: M HAIGH 233 5757

CONFIDENTIAL

ITEM: PENSIONS: REFUND OF SURPLUSES

STARTERS NUMBER: 136

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
* 1986/87: + 150 rising to about +450 for next 3 years and declining to a steady level thereafter	Small staff cost likely	Yes	2-3 pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	25.07.85 (interim) 20.12.85	24.12.85		

BACKGROUND AND COMMENTS

Possible 'pensions package' to go with legislation on pensions arising from the Fowler Review postponed until FB 1987. This clause now restricted to legislation covering refunds of surpluses.

* Costings are tentative at this stage.

Official in lead: N C MUNRO 2541-6487

Official in support: C S McNICOL 2541-7237

FP contact: M HAIGH 233-5757

BUDGET SECRET

ITEM: STAMP DUTY: LOAN STOCK

STARTERS NUMBER: 138

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
+ £20m	Negligible	Yes	1

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
EST	4.12.85			

BACKGROUND AND COMMENTS

Ministers are considering as part of the stamp duty package the possibility of withdrawing the exemption for loan stock. Exemptions would remain for:

(i) gilts

(ii) borrowing in the euro-currency markets; and possibly

(iii) loans for less than 5 years.

Official in lead: D G DRAPER 2541-6646

Official in support: MISS A M RHODES 2541-6605

FP contact: M HAIGH 233-5757

CONFIDENTIAL

BUDGET SECRET

ITEM: TREATMENT OF VAT PENALTIES ETC FOR DIRECT TAX PURPOSES (IT & CT)

STARTERS NUMBER: 139

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Nil	Nil	No	1/3 page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	22.11.85	25.11.85	19.12.85	6.1.86

BACKGROUND AND COMMENTS

The 1985 Finance Act introduced penalties, interest and surcharges for certain VAT offences. We require a provision to make it clear beyond doubt that such items are not deductible for the purposes of Income Tax or Corporation Tax.

The Act also introduced repayment supplement on payments of VAT refunded to taxpayers. We require a brief provision to confirm that repayment supplement paid in these circumstances is not income for the purposes of Income Tax or Corporation Tax.

Official in lead:	T A SYMONS	2541-6300
Official in support:	MISS M A BARLOW	2541-7255
FP contact:	M HAIGH	233-5757

BUDGET SECRET

ITEM: CGT: DUAL RESIDENT TRUSTS

STARTERS NUMBER: 140

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Yield impossible to quantify at this stage, but could run to £m100s (see comments)	NIL	No	Perhaps ½ page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	20.12.85			

BACKGROUND AND COMMENTS

Proposal to prevent avoidance of CGT through trusts deliberately set up with one trustee resident abroad (typically in the Republic of Ireland). Evidence suggests that this device is widespread; in 2 actual cases, gains of nearly £m7 are involved.

An alternative to domestic legislation would be to seek amendment to our double taxation agreements with those treaty partners where we consider we are at risk. This would inevitably be a protracted and uncertain process. Such a solution is dependent upon the treaty partners' willingness to open negotiations, and of course provides them with an opportunity to seek unrelated and unwelcome changes.

* Forecast assumes no loss.

Official in lead:	H B THOMPSON	2541-6334
Official in support:	V J BAKER	2541-6739
FP contact:	M HAIGH	233-5757

PAGE NO:

BUDGET SECRET

ITEM: CAPITAL GAINS TAX: FUTURES AND TRADED OPTIONS IN GILTS

STARTERS NUMBER: 143

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1986/87: nil Full Year Could be significant loss of tax if no action taken	Small saving	No	½ to 1 page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
EST	4.7.85 10.1.86	14.1.86		

BACKGROUND AND COMMENTS

After 2 July 1986 (when disposals of gilts and qualifying corporate bonds will be exempt from CGT) an asymmetry could arise in futures and traded options in these instruments. Contracts showing losses will be "closed-out" and the loss taken, contracts showing gains will run to delivery and be exempt. Case for exempting such contracts from CGT has been put by Stock Exchange and London International Financial Futures Exchange, with whom discussions have been held.

If action is to be taken, early announcement desirable to remove uncertainty about tax treatment of contracts entered into before the Budget.

Official in lead:	J P B BRYCE	2541-7427
Official in support:	V J BAKER	2541-6739
FP contact:	M HAIGH	233-5757

CONFIDENTIAL

BUDGET SECRET

ITEM: **AMENDMENT TO SECTION 58, FINANCE ACT 1969 TO ALLOW THE DEPARTMENT OF EMPLOYMENT TO PASS ON TO LOCAL AUTHORITIES INFORMATION SUPPLIED FROM THE INLAND REVENUE EMPLOYERS' INDEX**

STARTERS NUMBER: 144

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
No effect	No effect	No	6 lines

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	24.7.85			

BACKGROUND AND COMMENTS

Section 58, Finance Act 1969 prevents the Department of Employment from disclosing employment information provided by the Inland Revenue other than to another Government Department for the purpose of a statistical survey. The Department of Employment are pressing to be able to pass on this information to local planning authorities and to local education authority careers services to meet a shortfall in the information they can already supply under their own powers.

Not likely to be controversial.

The FST is content (minute 29/7/85) for this item to be included in the list of starters, subject to developing priorities and the availability of legislative space.

Official in lead:	F W NEWCOMBE	2541-6544
Official in support:	J W BOYCE	2541-7333
FP contact:	M HAIGH	233-5757

CONFIDENTIAL

BUDGET SECRET

ITEM: SECTION 286 ICTA: LOANS TO PARTICIPATORS IN CLOSE COMPANIES

STARTERS NUMBER: 145

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Negligible cost	Some saving on staff increases that would otherwise result from implementation of Keith	No	Depends on which items included - but maximum 1 page.

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST				

BACKGROUND AND COMMENTS

Section 286 is designed to ensure (so far as the close company is concerned) that broadly comparable tax treatment applies when, instead of there being a straightforward distribution out of the company's profits, money is taken out by way of a loan or advance to its participators (broadly, its shareholders).

Implementation of the relevant Keith proposals will give more bite to the application of this charging provision - ie by imposing a specific obligation, with increased interest and penalty charges, to notify chargeability to tax when loans etc are made to participators. In view of this, and because there is a case on merits anyway, some narrowing in the coverage of Section 286 is also now desirable, in particular to exclude payments on account of directors' remuneration. Certain other minor changes - some relaxing, others tightening up - would be desirable at the same time.

Ministers have, however, already decided not to relax Section 286 in respect of loans made during the course of a management buy-out, as has been proposed in recent representations.

Official in lead: M PRESCOTT/J H REED 2541-6442

Official in support: M JARRETT 2541 6257

FP contact: M HAIGH 233-5757

BUDGET SECRET

ITEM: SECTION 252 ICTA: USE OF TAX LOSSES ON TRANSFER OF A TRADE BETWEEN COMPANIES IN COMMON OWNERSHIP

STARTERS NUMBER: 146

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Depends on solution adopted. But annual yield of up to £50m not unrealistic	Negligible	No	1 page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	26.11.85	24.12.85		

BACKGROUND AND COMMENTS

Any unused tax losses of a trade may be carried forward and set-off against future profits of that trade (S.177, ICTA). But such tax losses cease to be available either if the trade itself ceases or, generally speaking, if the trade is transferred from one trading entity to another (S.251, ICTA). Section 252, however, provides that where a trade is transferred between companies in substantially common ownership, any accumulated tax losses may also transfer.

Section 252 has various weaknesses, and these are being exploited - with the object, in each case, of enabling the accumulated tax losses to pass with the trade to an unrelated third party. Action to counter the worst of these abuses is desirable, and there are a number of alternative approaches that might be adopted. Of particular concern is the present ability of companies to hive down a trade (and with it the whole of the accumulated tax losses) to a subsidiary which is then sold to a third party, even though certain debts - eg trade creditors - are left stranded in the old company. (If eventually these debts have to be written-off by the creditors there would then also, effectively, have been double relief for the same loss).

Official in lead:	J M REED	2541-6442
Official in support:	M JARRETT	2541-6257
FP contact:	M HAIGH	233-5757

PAGE NO:

CONFIDENTIAL

ITEM: CAPITAL ALLOWANCES: TECHNICAL AMENDMENTS CONSEQUENT ON ABOLITION OF FIRST YEAR ALLOWANCES

STARTERS NUMBER: 147

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Nil	Nil	No	7 to 8 pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	27.11.85	2.12.85	11.12.85	

BACKGROUND AND COMMENTS

First Year Allowances will no longer be generally available for expenditure incurred on or after 1 April 1986. A number of provisions* in existing legislation have been identified as needing amendment - mostly of a technical nature - to allow parts of the capital allowances system to continue to operate satisfactorily in the post-FYA era.

* One example is the 1982 leasing legislation which provides a reduced writing down allowance (10 per cent) for machinery or plant leased to a non-resident. Without an amendment, the legislation will not operate as intended and such leased assets will attract the ordinary w.d.a of 25 per cent.

Official in lead: G H BUSH 2541-6287

Official in support: G A A ELMER 2541-7507

FP contact: M HAIGH 233-5757

ITEM: **FURTHER TAX MEASURES TO ENCOURAGE R&D: TREATING R&D AS A TRADE FOR TAX PURPOSES**

STARTERS NUMBER: 149

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
?	Negligible	No	2 or 3 pages (very provisional estimate but likely to be technically difficult to draft)

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST				

BACKGROUND AND COMMENTS

The Industrial Support Review said officials would consider further the practical possibility of giving relief for R&D expenditure at the time it is incurred (at present, relief for such expenditure cannot be given until a trade subsequently starts).

The cost would be much increased if relief extended to oil exploration expenditure.

Official in lead:	M J G ELLIOTT	2541-6412
Official in support:	MISS R DYALL	2541-6304
FP contact:	M HAIGH	233-5757

BUDGET 'SECRET

ITEM: GROSS PAYMENT OF FOREIGN DIVIDENDS, ETC TO RECOGNISED CLEARING SYSTEMS

STARTERS NUMBER: 151

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Nil ..	Nil	No	½ Page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	1.11.85	3.12.85	18.12.85	16.1.86

BACKGROUND AND COMMENTS

Clearing systems are used by financial concerns to facilitate transfers of stocks, etc without physical delivery. Under the present foreign dividends provisions a UK paying agent who wished to pay foreign dividends without deduction of tax has to be provided with the name and address of the beneficial owner of the dividend and be satisfied that he is not resident in the UK. The depositary banks holding the stocks for the clearing systems are unable to provide the required information and so the business goes to foreign rather than UK paying agents.

The legislation would permit UK paying agents to pay gross dividends to recognised clearing systems without the need for evidence of beneficial ownership. A similar provision was included in the Eurobond legislation - Section 35(2)(b) FA 1984.

Official in lead:	M F CAYLEY	2541-6372
Official in support:	G N ALPE	2541-6254
FP contact:	M HAIGH	233-5757

ITEM: **SECTION 8(3) OTA 1983: FIELDS IN COMMON OWNERSHIP: THIRD PARTY USE OF ASSETS**

STARTERS NUMBER: 153

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
See note 3	None	No	1 page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	5.12.85	9.12.85		

BACKGROUND AND COMMENTS

(1) Section 6 OTA 1983 imposes a charge on tariff receipts in respect of use of a qualifying asset. Section 8(3)(c) provides that where expenditure on a qualifying asset is allowable in more than one oil field (ie apportioned between fields in common ownership) then tariff receipts are chargeable in the field which received development consent first.

(2) Now most cluster developments are going ahead, where it is sensible for fields to be given development consent on the same day. So a further tie breaker is necessary to prevent difficulties in allocating the charge in those cases. (The alternative - to leave the decision in effect to the Secretary of State for Energy - is neither desirable nor wanted by Energy.)

(3) The revenue effects would depend on what would happen without this amendment, but the tax involved in such cases is some £10 million in 1986-87, and will be more in later years. Forecast assumes no loss.

Official in lead:	MRS C HUBBARD	2541-6576
Official in support:	Y S PANG	2541-6250
FP contact:	M HAIGH	233-5757

ITEM: OTA 1983: DISPOSAL RECEIPTS IN EXEMPT GAS FIELDS

STARTERS NUMBER: 154

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Negligible Cost	None	No	1 page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	21.11.85	3.12.85 5.12.85	20.12.85	

BACKGROUND AND COMMENTS

1. Sections 7 and 8 OTA bring into charge PRT tariff and disposal receipts arising from assets, the expenditure on which has been allowed for PRT. It also charges to PRT tariff and disposal receipts in exempt gas fields to avoid distorting commercial decisions where such fields are in competition with PRT fields fo the shared use of assets.

2. During discussions on OTA 1983 UKOITC requested a de minimis limit for disposals in exempt gas fields, to avoid raising assessments to PRT for very small amounts for fields otherwise exempt. No solution was then found, but representations on this front have been maintained, and we think there is a good case for doing something, either by a monetary threshold per field or a restriction of the charge to assets disposed for subsequent field use.

3. The cost would be negligible, and it would make for more efficient use of staff time.

4. The opportunity might be taken to make some other amendments on disposal receipts.

Official in lead:	MR C HUBBARD	2541-6576
Official in support:	Y S PANG	2541-6250
FP contact:	M HAIGH	233-5757

PAGE NO:

BUDGET SECRET

ITEM: PRT VALUATION OF LIGHT GASES

STARTERS NUMBER: 157

CLASSIFICATION: C (but see Starter No. 130 (BGC privatisation))

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Should have no effect on tax take	Nil	No	1 page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST				

BACKGROUND AND COMMENTS

Gas sold in non-arm's length deals is valued for PRT purposes under the rules of valuing oil - ie an arm's length price has to be established each month. Such an approach is arguably inappropriate for the lighter gases, which are almost invariably sold under contracts lasting 20 years or so. In recognition of this (and to protect the position of the Mossmorran project), an alternative basis for valuation of ethane for petrochemical purposes was introduced by Section 134 and Schedule 18 FA 82. Providing certain conditions are met, this enables such ethane to be valued according to the price formula in the contract concerned.

ICI are pursuing in the courts their quarrel with Section 134. If the Appeal Court (judgement expected shortly) should cast doubt onthe principal of the Section 134 approach to an arm's length valuation, we should have to reconsider Section 134 de novo.

Although the underlying facts are similar, Section 134 was not applied in 1982 to other light gas (eg methane) or to light gases when used as fuel (partly because of ICI's opposition). But we now have quantitites of methane to value, both for fuel and petrochemical uses. The biggest case involves BGC and the issue may have to be resolved by legislation before privatisation (so in Finance Bill 1986) though a very recent discussion suggests that if we cannot make the present law work, something more than simply extending Section 134 might be needed in their case.

Official in lead: M A HILL 2541-6018

Official in support: M HAY 2541-7437

FP contact: M HAIGH 233-5757

CONFIDENTIAL

BUDGET SECRET

ITEM: CTT: LIFETIME CHARGE

STARTERS NUMBER: 161

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
First Year Cost £40 million	Unlikely to be significant		Perhaps 30-50 pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST and Chancellor	5.12.85	21.12.85	10.1.86	

BACKGROUND AND COMMENTS

Chancellor's meeting of 6 December confirmed intention to abolish CTT charge on lifetime gifts to individuals, but retain for gifts into trusts. New provisions will be required to protect death charge.

Further work in hand on costs. If significant increases in lifetime giving, final cost could be substnatial eg £150 million if giving doubled. But this is very speculative and unlikely to be reaced before mid-1990's.

Official in lead:	B T HOUGHTON	438 7290
Official in support:	J P BATTERSBY (Non-trusts)	438 6459
FP contact:	H THOMPSON (Trusts)	438 6334

PAGE NO:

BUDGET SECRET

ITEM: TAX RELIEF FOR SAVINGS

STARTERS NUMBER: 162

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Possibly 1987-80 -£m40	Negligible addition	Yes	1-2 pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	9.1.86			

BACKGROUND AND COMMENTS

A new relief for investment (subject to an annual limit). Individuals would invest out of taxed income, but there would be no tax charge on disinvestment. Qualifying investments - which might be restricted to equities - would be held by banks, building societies, etc.

A relief on these lines would have similar aims as Loi Monory, Individual Retirement Accounts etc, but would not entail the same administrative and policing difficulties. And the Exchequer cost (much of which would be deadweight) would build up more slowly compared with other, front-end loaded, schemes.

Official in lead: M A HILL 2541-6018

Official in support: Y S PANG 2541-6250

FP contact: M HAIGH 233-5757

BUDGET SECRET

ITEM: CO-OPERATIVES' ACCESS TO APPROVED PROFIT SHARING SCHEMES

STARTERS NUMBER: 163

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1986-87: negligible cost Full year: perhaps up to -£m2	Nil	Yes	1 page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	20.12..85			

BACKGROUND AND COMMENTS

The shares which may be used in an approved profit sharing employee share scheme under the Finance Act 1978 must be irredeemable. Co-operatives' shares are usually redeemable and do not therefore qualify. Ministers considered the difficulties which this rule posed for co-operatives last year but decided that no action should be taken. The Financial Secretary has asked for the matter to be re-examined following a meeting in November with Mr Paul Derrick, the chief advocate of a change in the 1978 rules to allow access for co-operatives generally.

Official in lead:	M A HILL	2541-6018
Official in support:	Y S PANG	2541-6250
FP contact:	M HAIGH	233-5757

BUDGET SECRET

ITEM: BUILDING SOCIETIES: MINOR CONSEQUENTIAL AMENDMENTS

STARTERS NUMBER: 165 **CLASSIFICATION:** C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
NIL	NIL	YES	½ PAGE

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
EST	23.1.86	27.1.86		

BACKGROUND AND COMMENTS

Regulations necessary to operate a new "composite rate" scheme for bulding society interest due to take effect on 6 April 1986.

As a result, two minor amendments to current legislation are necessary. These will:

1. ensure that the special Schedule D Case III charging rules for a fresh source of income and a cessation of income can apply, where appropriate, to gross payments of building society interest

2. update two references to "arrangements" under Section 343 ICTA in present legislation.

Official in lead: N C MUNRO 438 6487

Official in support: C S McNICOL 438 7237

FP contact: M HAIGH 233 5757

PAGE NO:

BUDGET SECRET

ITEM: Relief for individuals for charitable donations through payroll deduction scheme

STARTERS NUMBER: 167

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million		Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1986/7	NIL	1987/8 + 50 (setting) (up cost)		not yet known
1987/8	-20	Full Yr + 30	Possibly future taxation Resolution	

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	29/1/86 17/2/86			

BACKGROUND AND COMMENTS

Proposal is for income tax relief for charitable donations up to £100 a year made by employees through payroll deduction schemes run by employers. No obligation on employers to run schemes, but no relief except through a scheme (eg for self-employed, or if employer is unwilling to run a scheme). Probable starting date April 1987 following legislation and regulations.

Official in lead: C Stewart 2541-7414

Official in support: Mrs E Fletcher 2541-7784

FP contact: M D R Haigh 233-5757

BUDGET SECRET

ITEM: Stokes v Costain and the Oil Industry

STARTERS NUMBER: 168 **CLASSIFICATION:** C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million		Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
1986/87	nil	NIL	NO	1
1987/88	nil			

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	12.2.86		21.2.86	

BACKGROUND AND COMMENTS

The Costain case produced the result that in certain circumstances no-one is entitled to capital allowances for expenditure on plant and machinery which becomes a "fixture". In general, allowances are only given to the person incurring the capital expenditure on the fixture provided he holds an interest in the land or buildings to which the fixture is attached (Section 59 and Schedule 17, Finance Act 1985).

In particular, UKOITC have raised the problem of an oil company which lends equipment to its customer, the service station dealer, often as part of the overall supply arrangements. The fixtures do not "belong" to the oil company who is buying and lending them while the borrowing dealer will not have incurred the capital expenditure on them and the new rules in FA 1985 cannot apply.

The FST has agreed that in order to avoid retrospection an election would be available to apply the old rules for expenditure up to Budget Day.

Official in lead: G H Bush 2541 - 6287

Official in support: G A A Elmer 2541 - 7507

FP contact: M D R Haigh 233 - 5757

PAGE NO:

BUDGET SECRET

ITEM: CTT: INTERACTION OF BUSINESS AND AGRICULTURAL RELIEFS AND PARTLY EXEMPT TRANSFERS

STARTERS NUMBER: 169 **CLASSIFICATION:** C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
See note below	Nil	No	2-3 pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	14/2/86			

BACKGROUND AND COMMENTS

The present rules give an unintended advantage to estates where there is both agricultural or business property and an exempt recipient - usually a spouse. This results in property passing CTT-free to chargeable beneficiaries up to the amount of the business or agricultural relief due (50 or 30 per cent depending on the property). The device has been described in the professional journals, and its use is increasing.

The full impact of the device has not yet come through to receipts, because it can be used up to two years after the death. So action to block it will prevent a future loss to receipts (perhaps of up to £10-20 million for deaths in 1986-87 on the basis of cases seen). But there may be relatively little yield in the short-term, as testators, with this device blocked, will probably leave more to the spouse, who is exempt - although there could ultimately be further CTT on the spouse's death.

Official in lead: J P BATTERSBY 2541 - 6459

Official in support: L E JAUNDOO 2541 - 7680

FP contact: M D R HAIGH 233 - 5757

BUDGET SECRET

ITEM: Section 16 OTA 1975; ACT: Restriction of set-off against ring fence profits

STARTERS NUMBER: 170

CLASSIFICATION: C

DEPARTMENT: Inland Revenue

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
*1986/7 - 5 to - 10	NIL	NO	1 page

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
FST	17/2/86			

BACKGROUND AND COMMENTS

Section 16 OTA 1975 protects the ring fence by restricting the set-off of ACT on intra-group dividends against ring fence corporation tax. Once dividends are paid to outside shareholders (including non-resident parent companies) ACT can then be surrendered to a ring-fence company for set-off against its CT. But this surrendered ACT cannot be carried back only forward. Depending on the circumstances (eg tax liabilities outside the ring fence) this can result in ACT becoming standard for some years. The industry has made representations for several years asking that S.16 should either be repealed or that they should be allowed to carry-back the surrendered ACT. The problem has now become a live one for at least two of the smaller groups, and may become so for some of the majors. Although the extent of the problem for the majors is difficult to estimate, the cost of any solution could be very significant.

*For the known problem of the smaller companies a solution would cost £m5 to 10 in 1986/87; but for the majors cost could be ten times that amount.

Official in lead: Mrs C B Hubbard 2541-6576

Official in support: Y S Pang 2541-6250

FP contact: M D R Haigh 233-5757

ITEM: **AMENDMENT OF 1981 BROADCASTING ACT: CHANGE OF IBA ARRANGEMENTS**

STARTERS NUMBER: 402

CLASSIFICATION: C

DEPARTMENT:

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Not yet clear (likely to be revenue-neutral)	None	No	Annex 2 pages

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
To be decided		Not yet available		

BACKGROUND AND COMMENTS

Treasury and Home Office officials produced a report in May 1985 recommending certain changes to the ITV and ILR levies.

These recommendations are now with Ministers; a decision is expected by the end of November. If changes are to be made, then the 1986 Fnance Bill might be the best vehicle, on grounds of expediency (there is no suitable Broadcasting legislation currently being planned); previous alterations to the levy has been made in this way (eg 1982). But we are proposing to check this procedure with Parliamentary Counsel. So for the time being, we are putting down a marker; we await a final decision both on the levy report, and on the most appropriate means of legislation.

Official in lead: T J BURR 233-8481

Official in support: N KAUFMANN 233-7200

FP contact: G McKENZIE 233-8974

BUDGET SECRET

ITEM: VED EXEMPTION FOR VISITING FORCES' VEHICLES

STARTERS NUMBER: 403

CLASSIFICATION: C

DEPARTMENT: Transport

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Nil	Nil	No	12 Lines

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST				

BACKGROUND AND COMMENTS

This item would give 12 months VED exemption to visiting forces' vehicles which have been granted relief from Customs duties; it is needed to make good a deficiency which has come to light in the legislation. The provision would come into force from 1 September 1986.

For many years, vehicles brought temporarily into UK by foreign residents have received 12 months VED exemption, subject to being exempt from Customs duties. However recent Customs legislation implementing an EC Directive on Customs duty exemptions for temporarily imported goods unintentionally had the effect of excluding vehicles of visiting forces from the VED exemption. There would be strong criticism if exemptions for visiting forces were withdrawn and exemption is continuing to be granted extra-statutorily for the present. There are also VED enforcement benefits in the proposed change, since vehicles would automatically have to be registered on arrival.

Official in lead: R Bird 2067-2430

Official in support: T Horton 2067-2000

FP contact: K M Romanski 233-5237

PAGE NO:

CONFIDENTIAL

ITEM: **REMOVE THE REQUIREMENT FOR A £2 FEE ON APPLICATION FOR A DUPLICATE VEHICLE REGISTRATION DOCUMENT (V62)**

STARTERS NUMBER: 405

CLASSIFICATION: B2

DEPARTMENT: Transport

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Negligible.	None	Yes	2 lines

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST				

BACKGROUND AND COMMENTS

Section 23(d) of the Vehicle Road Traffic Act 1971 requires an initial registration document (log book) to be issued free. Section 23 (1)(e) of the Vehicle Excise Act 1971 imposes a fee - presently £2 - for a duplicate registration document. Owners can avoid the fee by saying - truthfully or not - that the original document was lost in the post or - when buying second hand - the previous owner did not pass the document on. Eighty per cent of applicants for duplicate documents do this. It is proposed to stop charging the other 20 per cent on the grounds of equity. It will also simplify administration when the work of relicensing a vehicle where a duplicate registration documents is required is transferred to the Post Office.

This measure is unlikely to be controversial. The income foregone - about £250,000 a year - will be made up from increasing fees on other services.

Official in lead:	R Bird	2067-2430
Official in support:	T Horton	2067-2000
FP contact:	K M Romanski	233-5237

BUDGET SECRET

ITEM: CHANGES TO CLARIFY AND SIMPLIFY TRADE LICENSING ARRANGEMENTS

STARTERS NUMBER: 406

CLASSIFICATION: B2

DEPARTMENT: Transport

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Neutral	Small saving Not quantifiable	No	Likely to be 2 or 3 clauses (Guess)

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST				

BACKGROUND AND COMMENTS

The 'trade licensing facility' is designed to enable motor dealers and traders to use on the road vehicles which are temporarily in their possession without the need to register and license them. The proposed changes are designed to bring the facility up to date to cover additional uses, which have come into existence since the present legislation came into force in 1971, and to simplify the procedures in qualifying for plates. The fee is also to be increased.

Official in lead:	R Bird	2067-2430
Official in support:	T Horton	2067-2000
FP contact:	K M Romanski	233-5237

CONFIDENTIAL

BUDGET SECRET

ITEM: DATE TO END OF MONTH FIRST LICENSING

STARTERS NUMBER: 407

CLASSIFICATION: B2

DEPARTMENT: Transport

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
Negligible - probably slightly negative	None	No	3 lines (Guess)

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST				

BACKGROUND AND COMMENTS

At present motor vehicle licences start at the beginning of a month and run for a 6 or 12 month period. The motor trade have been pressing for some time for more flexibility in licensing periods and in particular for the licensing period to start on any day of the month. Such a system would lead to substantial revenue loss, but instead Ministers have promised the trade that they would consider a much more limited scheme which would allow licences for new vehicles only to start on one of four dates in the month and run to the end of the month and then for the full 6 or 12 month period. A special rate of duty would be charged on these licences to reflect their longer validity. A possible system has been investigated and it could be introduced without serious operational difficulties.

It is difficult to provide an estimate of the cost as much will depend on the number of motorists who will take advantage of the scheme. We estimate that any loss will be negligible. The legislation required will be one additional paragraph to Schedule 7 of the Vehicles (Excise) Act 1971.

Official in lead:	R Bird	2067-2430
Official in support:	T Horton	2067-2000
FP contact:	K M Romanski	233-5237

BUDGET SECRET.

ITEM: **INCREASED PENALTIES FOR VED EVASION**

STARTERS NUMBER: 410

CLASSIFICATION: C

DEPARTMENT: Transport

Revenue cost (-) or yield (+) £ million	Staff addition (+) or saving (-)	PCTA or equivalent Resolution required	Length of legislation (lines or pages)
£3-5 million (see below) .	Nil	No	5-6 lines

Minister in lead	Submission made (date)	Approval to draft (date)	Instructions sent (date)	Drafting completed
MST				

BACKGROUND AND COMMENTS

The proposal is to amend Section 9(2) of the Vehicles (Excise) Act 1971, so that, on conviction for keeping or using a vehicle without a valid vehicle excise licence, the courts would make orders for back duty at a specified multiple of the actual rate (1½ times or twice - Revenue yield would depend on which).

This would strengthen the punishment for VED evasion and would thus help meet the PAC's criticism of VED evasion and enforcement in a Report published in May 1984. The enhanced penalty would also encourage more offenders to accept the Department's offers to settle out-of-court, thus relieving resource pressures on the Department, Police and Courts. Discussions are in hand with the Home Office and Scottish Home and Heath Department, which it is hoped will enable a submission to be made to Ministers early in 1986.

Official in lead:	R Bird	2067-2430
Official in support:	J Palmer	2067-2485
FP contact:	K M Romanski	233-5237

BR/17

Rep No 13J

BUDGET SECRET

COPY NO 6 OF 6 .

PRIME MINISTER

I am writing to let you know what I have in mind for indirect taxes in the Budget.

I have reached the view that it would not be sensible to do more than revalorise the excise duties as a whole this year. There is no prospect of a major offsetting reduction in income tax. So I see little point in jeopardising the good prospect for a further significant reduction in inflation by adding unnecessarily to the RPI. But I think it is attractive to take the opportunity to reduce sharply the number of individual tax increases in the Budget, rather than simply uprating all the duties by the 5.7 per cent indexation factor.

As far as the motorist goes, I propose to put up petrol duty by 7½p a gallon and the duty on derv by 6½p a gallon. In each case this is about 2p a gallon more than revalorisation - but far less than most people are predicting. This will enable me to leave all the main VED rates unchanged.

Moreover, given the sharp fall in the oil price that has already occurred, and the slowness of the oil companies so far to reflect this in lower prices at the pump, there is no need for fuel duty increases of this order to be passed on to the consumer at all.

As Norman Fowler reminds me every year, there is considerable pressure on health grounds to increase the tax on cigarettes by appreciably more than revalorisation. I therefore propose an increase equivalent to approximately 11p on a typical packet of 20, with, as last year, no increase in the tax on pipe tobacco and cigars.

This will mean that there is no need for any increase at all in the duty on alcoholic drinks - for the first time since 1979. The prize here will be the absence of any increase in the tax on beer - which, you will recall, I had to put up by more than I would otherwise have done in 1984, to conform with the EC infraction judgement. The standstill on whisky will, of course, go down well in Scotland.

The overall impact of this package on the RPI, as conventionally calculated, will be to add about 0.5 per cent, entirely reflecting the effect of revalorisation. This is the same as last year's Budget, so there will be no change in the annual figure on this account.

I also propose to simplify the indirect tax system slightly by abolishing one or two of the minor oil duties and recouping the small loss of revenue from a 1½p increase in the duty on gas oil. This has been unchanged since 1980, leaving gas oil clearly under-taxed at the present time, relative to the rest of the EC. The duty on heavy fuel oil would once again remain unchanged.

So far as VAT is concerned, with the exception of one or two minor concessions to charities - relief on their newspaper advertising, and on medicinal products supplied to them - I am proposing to make no changes here, either to the rate or the base. However, I do intend to increase the VAT threshold to £20,500, in line with revalorisation, in spite of the Commission's contention (which we reject) that it is already higher than Community law allows.

I would be grateful to know if you would be content with these changes.

NL

N.L.

26 February 1986

pwp

This was what you dictated which - believe it or not - I did show to George!

DRAFT MINUTE TO PRIME MINISTER

INDIRECT TAXES

I am writing to let you know ~~my proposals~~ what I have in mind for ~~in the~~ indirect ~~tax~~ ~~field~~ taxes ~~for~~ in the ~~coming~~ Budget.

2. In view of the overall size of the Budget, and the need to keep the direct impact on the RPI to a minimum, I have concluded that it would not be sensible to do more than revalorise the excise duties. But I think it is attractive to take the opportunity to reduce sharply the number of changes made, not simply to up rate all the duties by the 5.7 per cent indexation factor.

3. I therefore propose to put up petrol duty by Xp and derv by Yp. In each case this is Xp and Yp a gallon more than revalorisation - but far less than most people are predicting. This will enable me to leave all the main VED rates unchanged.

4. There is considerable pressure on health grounds to increase the tax on cigarettes by appreciably more than revalorisation. I therefore propose an increase equivalent to approximately 11p on a packet of 20 (with, as last year, no increase in the tax on pipe tobacco and cigars).

5. This will mean that there is no need for any increase at all in the duty on alcoholic drinks - for the first time since [19...]. The prize here will be the absence of any increase in the tax on beer - which, you will recall, I had to put up by more than I would otherwise have done in 1984, to conform with the EC infraction judgement. The standstill on whisky will go down well in Scotland.

6. I also propose to abolish one or two of the minor oil duties, recouping the cost by increasing the duty on gas oil which is clearly under taxed at the present time, both in relation to the rest of Europe, and in comparison with 1980.

BR/17

Mr Rutter
I have amended it. N.

BUDGET SECRET

COPY NO OF .

PRIME MINISTER

I am writing to let you know what I have in mind for indirect taxes in the Budget.

I have reached the view that it would not be sensible to do more than revalorise the excise duties as a whole this year. There is no prospect of a major offsetting reduction in income tax. ~~Nor do I want to~~ So I see little point in ~~jeopardise~~ jeopardising the ~~very~~ good prospect for a further significant reduction in inflation by adding unnecessarily to the RPI. But I think it is attractive to take the opportunity to reduce sharply the number of ~~changes made, not simply to uprate all~~ individual tax increases in the Budget, rather than simply uprating all the duties by the 5.7 per cent indexation factor.

As far as the motorist goes, I propose to put up petrol duty by 7½p a gallon and the duty on derv by 6½p a gallon. In each case this is about 2p a gallon more than revalorisation - but far less than most people are predicting. This will enable me to leave all the main VED rates unchanged.

Moreover, given the sharp fall in the oil price that has already occurred, and the slowness of the oil companies so far to reflect this in lower prices at the pump, there is no need for ~~reason~~ ~~long~~ fuel duty increases of this order ~~must~~ to be passed on to the consumer at all.

These changes should leave pump prices well below the level of £2 a gallon which they reached after the last Budget, especially since the oil companies have not yet passed on the full benefit of the recent fall in oil prices. The effect of the Budget will be to leave much of the gain from lower oil prices with the consumer - where I am sure it should be.

Nick Ridley will also welcome this modest switch in the burden of tax from VED to petrol duty. And for most private motorists, especially pensioners (who drive fewer miles than the average) it will be better than across the board revalorisation. The standstill on lorry VED will be of particular benefit to our haulage industry, as well as to industrial costs generally.

As Norman Fowler reminds me every year, there is considerable pressure on health grounds to increase the tax on cigarettes by appreciably more than revalorisation. I therefore propose an increase equivalent to approximately 11p on a typical packet of 20, with, as last year, no increase in the tax on pipe tobacco and cigars.

This will mean that there is no need for any increase at all in the duty on alcoholic drinks - for the first time since 1979. The prize here will be the absence of any increase in the tax on beer - which, you will recall, I had to put up by more than I would otherwise have done in 1984, to conform with the EC infraction judgement. The standstill on whisky will, of course, go down well in Scotland.

simplify the indirect tax system slightly by abolishing

I also propose to ~~abolish~~ one or two of the minor oil duties and recouping ~~to recoup~~ the small loss of revenue from a 1½p increase in the duty on gas oil. This has been ~~remained~~ unchanged since 1980, leaving gas oil clearly under-taxed at the present time, relative to the rest of the EC. The duty on heavy fuel oil would once again remain unchanged. ~~I would have liked to reduce or even abolish it, but we would then have had to pay more to the Norwegians for Frigg gas, under the terms of our contract with them.~~

So far as VAT is concerned, with ~~Finally, VAT. With~~ the exception of one or two ~~a few~~ minor concessions ~~of particular interest~~ to charities - ~~including~~ relief on their newspaper advertising ~~by charities~~, and on medicinal products supplied to them - I am proposing to make no changes here, either to the rate or the base. However, I do intend to increase the VAT threshold to £20,500, in line with revalorisation, in spite of the Commission's contention (which we reject) ~~argument~~ that it is already higher than Community law ~~rules~~ allows.

I would be grateful to know if you would be content with these changes.

The overall impact ~~effect~~ of this package on the RPI, as conventionally calculated, will be to add about 0.5 per cent, entirely reflecting the effect of 'revalorisation'. This is the same as last year's Budget, so there ~~will~~ will be no change in the annual figure on this account.

N.L.

2153/57

08

FROM: N WILLIAMS
DATE: 17 April 1986

MR PRESCOTT IR

cc PS/Chancellor
PS/Chief Secretary
PS/Economic Secretary
PS/Minister of State
Mr Monger
Miss Sinclair
Mr Savage (Parly Section)
Mr Cropper
Mr Lord
PS/IR

CAR AND CAR FUEL BENEFIT SCALE CHARGES 1987/88: STATUTORY INSTRUMENTS

1. The Financial Secretary was grateful for your minute of 14 April.

2. He is content for the Orders to be tabled on Friday 18 April.

N Williams

NIGEL WILLIAMS
(Assistant Private Secretary)