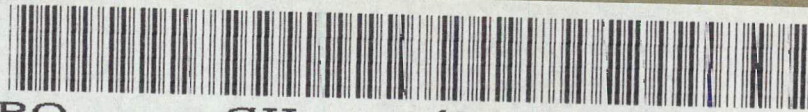


PO-CH/NL/0388
PART A

SECRET

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notify REGISTRY of movement)



PO -CH /NL/0388



PART A

1988 CAPITAL ALLOWANCE:
MORTGAGE INTEREST RELIEF
TAX TREATMENT OF PRIVATE
RENTING AND FRINGE
BENEFITS

DD's 25 years NAB 3 7-12-95

PO -CH /NL/0388

PART A

PART A

11-2-88

CLOSED
PAGE **B**

CONFIDENTIAL



FROM: J M G TAYLOR
 DATE: 4 January 1988

13/1
 BT

PS/FINANCIAL SECRETARY

cc PS/Chief Secretary
 PS/Paymaster General
 PS/Economic Secretary
 Sir P Middleton
 Mr Cassell
 Mr Byatt
 Mr Scholar
 Mr Culpin
 Miss Sinclair
 Mr Instone
 Mr Betenson
 Miss Hay
 Mr Cropper
 Mr Tyrie
 Mr Call
 Mr Jenkins (Parly Counsel)
 Mr Battishill - IR
 Mr Isaac - IR
 Mr Painter - IR
 Mr McGivern - IR
 Mr Elliott - IR
 Mr Reed - IR
 PS/IR

TAX TREATMENT OF PRIVATE RENTED ACCOMMODATION

The Chancellor has seen Mr McGivern's minute of 23 December, and the enclosed papers by Mr Reed and Mr Elliott.

2. He would be grateful for the Financial Secretary's views, as soon as possible. Provisionally, he is inclined to the 5 year BES scheme suggested in the last paragraph of Mr McGivern's minute, with half BES relief (in recognition, as it were, of the exemption from the property restriction) - and he would still have a ceiling on other BES ventures, even if there had to be a higher ceiling for these. But he would not rule out also going for a rent-a-room scheme, where the best variant would seem to be Option B, but with a restriction on the minimum length of tenancy. (He also wonders whether the Leeds Residential Property Association could not use the BES route.)

JMGT
 TO
 PS/FST
 4 JAN

JMGT

J M G TAYLOR



papers p. X pup

FROM: FINANCIAL SECRETARY
DATE: 8 January 1988

CHANCELLOR

Handwritten notes in red ink:
Thank you for the papers
I have seen the papers
PS: I think @ No
from how long
relief program

- cc Chief Secretary
- Paymaster General
- Economic Secretary
- Sir P Middleton
- Mr Cassell
- Mr Byatt
- Mr Scholar
- Mr Culpin
- Miss Sinclair
- Mr Instone
- Mr Betenson
- Miss Hay
- Mr Cropper
- Mr Tyrie
- Mr Call
- Mr Jenkins OPC
- Mr Painter IR
- Mr McGivern IR
- Mr Elliott IR
- Mr Reed IR
- PS/IR

Handwritten notes in red ink:
PS psc have
X max 2/16
all in
man for 5)

TAX TREATMENT OF PRIVATE RENTED ACCOMMODATION

I have considered Mr McGivern's minute of 23 December covering papers from Mr Reed and Mr Elliott.

BES Relief

2. As you know I was not attracted to the BES route when this was originally suggested. Having looked at the proposal in more detail I have not changed my mind. Indeed I really do question whether the BES relief will attack the objective we have set ourselves.

3. To my mind, the central problem is that in general the rate of return on investments in rented accommodation is expected to be "too low" post-deregulation. Thus the objective must be to raise, across-the-board, the post-tax rate of return on rented accommodation by introducing a modest tax relief. I do not see the BES relief as having this across-the-board effect. It is difficult to know whether it will be ineffective (or effective only at the

FST
TO
CX
8 JAN

CONFIDENTIAL

margin), or whether it will be very successful indeed. But if it does turn out to be successful it will be extremely expensive. The provision of 100,000 dwellings, for example, would cost over a billion pounds if we went for a full BES relief - and even 100,000 new rented dwellings would be a fairly limited objective in the face of the supply gap that DOE have identified.

4. My own view, (though others disagree) is that the BES relief might prove very attractive indeed, and thus we might well be confronted with a spiralling cost. We would have given the new housing policy a substantial kick-start - but at a significant exchequer cost.

5. Others argue that what we are looking for is a "high-profile token" - a measure which will give a psychological boost to the rented sector, without having a major across-the-board impact on rates of return or upon the supply gap. I did not think that this was the objective and I doubt whether Nicholas Ridley is looking for just a token measure. But even if this is the objective I am still not sure that the BES relief is the appropriate measure. I suspect it will prove to be very expensive per dwelling.

6. In order to minimise the potential costs I would strongly favour both:

- (i) A limit on the proportion of an investment that is eligible for relief. For simplicity perhaps we should have a "half-BES";
- (ii) A cap - set at a higher level than for other BES companies. We will have to decide the precise level for the ceiling at a later stage.

7. I would prefer the Writing Down Allowance which we originally rejected on the grounds that it implied the paradox of providing a Writing Down Allowance for an asset which invariably tends to appreciate. Despite this, I believe that if we have to introduce a tax relief, the Writing Down Allowance is the least bad, precisely because it is an across-the-board relief which does

CONFIDENTIAL

something to boost the rate of return on all investment in private rented accommodation. But all this depends on what you see as the objective of the exercise.

8. On the assumption that you wish to press ahead with the BES relief, I have considered the detailed points in Mr Reed's paper. My conclusions are highly tentative. I suggest that officials discuss them with the DoE at the appropriate time.

- (i) **General:** I agree with officials that the relief should be based on BES itself to avoid unnecessary legislative duplications. I also believe that the relief should be restricted to companies specialising in residential lets. In addition, as I said above, I favour "half-BES" and a ceiling;
- (ii) **Qualifying Let Residential Accommodation:** I think that the relief should cover new buildings and also properties which have been substantially re-furnished. The relief should not be available for property already let when acquired by the company. I am less sure about empty property. There is an argument for getting this empty property back into use by offering the BES relief. In order to reduce deadweight, one might perhaps restrict the relief to properties which have been empty for some time. On the other hand this would provide an incentive for people to leave their properties vacant for the minimum period - which would have a perverse effect on housing supply. I am agnostic on this issue. I do not think that local authority dwellings taken over by private landlords should be within the scope of the relief, not least because there will be sitting tenants involved and a substantial deadweight cost.
- (iii) **Multiple Dwellings:** I am content with the 20% let out rule (paragraph 11).

CONFIDENTIAL

- (iv) **Time Limit on Selling Property:** Under the general BES rules there would be nothing to stop a rented dwelling being sold to another company after the qualifying three-year period. This company too would be eligible for the new BES relief when it acquired the rented property. But this opens up the prospect of a property qualifying for BES relief more than once - a prospect which I find unattractive. I think we may have to consider having a period of perhaps 10 years before which a property could not be sold (or could not be sold without becoming ineligible for relief). This would bring other difficulties, however, if the original BES investors had sold out after their minimum period of 5 years. I think this needs to be looked at.
- (v) **Types of Letting:** I think the BES relief should be restricted to the new-style assured tenancies but not including shorthold tenancies.
- (vi) **Expensive Properties:** I think these should be excluded, which could simply be done by confining the relief to assured tenancies. There is an argument that by including expensive properties one would be maximising the chances of expanding the supply of rented accommodation albeit only at the top end of the market. But I see little attraction in encouraging BES investment in palatial rented suites.
- (vii) **Sub-Standard Properties:** I think we should consult DOE on this.
- (viii) **Connections Between Investors/Directors and Tenants :** I think that we should exclude letting to the BES investor.
- (ix) **Tied Accommodation/Holiday Homes/Lodgings and Hotels:** I would exclude all these.

CONFIDENTIAL

- (x) Letting to Students: I think this should be included.
- (xi) Assured Agricultural Occupancies: We need to consult DOE on this.
- (xii) Housing Associations: Although I can imagine we will come under pressure on this, I think we should exclude these.
- (xiii) Time Limit: I favour a time limit of 5 years.

Rent a Room

9. I am even more opposed to the rent-a-room scheme than I am to the BES relief. My opposition rests on three main considerations:

- (i) I think the introduction of such an exemption would look very bizarre in the context of this year's Budget.
- (ii) It would also lead to renewed pressure from other groups for their income to be exempted - there are plenty of other deserving cases.
- (iii) Parliamentary Counsel reports that this together with the BES relief and other measures may well prove impossible to draft in the limited time available.

10. If the decision is taken to press ahead with the new relief I would favour Option A. This would exempt rental income up to a monetary ceiling under fairly restrictive circumstances: the recipient of the income would have to be an owner-occupier; only a small number of rooms could be let (perhaps up to 3); these rooms would have to be furnished; and the rooms would have to be let for more than some minimum period (perhaps 30 days). This is the narrowest option of the three proposed and these restrictions would do something to reduce the deadweight costs of the scheme.

CONFIDENTIAL

11. But any of the options would inevitably lead to strong pressure from other interest groups for extensions and I doubt whether there will be much "additionality". The whole "rent-a-room" scheme has, in Peter Cropper's words, the flavour of "a measure which might have been introduced in 1943!"

Q. R.

61. **NORMAN LAMONT**



COPY NO. 16 OF 16.

FROM: J M G TAYLOR

DATE: 13 January 1988

PS/FINANCIAL SECRETARY

cc PS/Chief Secretary

PS/Paymaster General
PS/Economic Secretary
Mr Scholar
Mr Culpin
Miss Sinclair
Mr Michie
Mr Cropper
Mr Tyrie

Mr Isaac - IR
Mr Lewis - IR
Mr Prescott - IR
PS/IR

FRINGE BENEFITS TAX:**AMBIT AND DE MINIMIS LIMIT FOR SMALL PROVIDERS**

The Chancellor has seen Mr Prescott's minute of 12 January.

2. He would be grateful for the views of all Ministers (and would welcome suggestions from other copy recipients) on the name of this tax.

A handwritten signature in black ink, appearing to be 'J M G Taylor'.

J M G TAYLOR



COPY NO. 12 OF 12.

FROM: A C S ALLAN

DATE: 25 January 1988

PS/FINANCIAL SECRETARY

cc Sir P Middleton
Mr Scholar
Mr Culpin
Mr Michie
Mr Cropper
Mr Tyrie

Mr Lewis - IR
Mr Prescott - IR
PS/IR

**FRINGE BENEFITS TAX: AMBIT AND DE MINIMIS LIMIT FOR
SMALL PROVIDERS**

The Chancellor has seen your minute of 20 January to Mr Prescott. He agrees that we certainly need a de minimis rule, but he is not sure that the Revenue's is sufficient. We may also need to exclude employers with fewer than a given (small) number of employees. Quite apart from the corner shop, he feels we do not, surely, want to catch the domestic employer with one or two resident staff. He would be most grateful if the Financial Secretary could look at this.

A handwritten signature in black ink, appearing to read 'ACSA', with a long horizontal stroke underneath.

A C S ALLAN

BUDGET SECRET: TASK FORCE LIST



COPY NO. 22 OF 23.

FROM: A C S ALLAN

DATE: 19 January 1988

MR P LEWIS - IR

cc PS/Chief Secretary
 PS/Financial Secretary
 PS/Paymaster General
 PS/Economic Secretary
 Sir P Middleton
 Sir T Burns
 Sir G Littler
 Mr Anson
 Mr Monck
 Mr Scholar
 Mr Culpin
 Miss Sinclair
 Mr Michie
 Mr Cropper
 Mr Tyrie
 Mr Call
 PS/IR
 Mr Prescott IR
 Miss Rhodes IR

FRINGE BENEFITS

The Chancellor would be grateful if a further option could be considered as part of what we might do if we did not introduce an FBT. There will surely be very few company cars given to those below the PlLD limit - since, as he understands it, the £8500 pa includes the value of the perk. Could we not therefore abolish the PlLD limit entirely. Where this caused administrative or other difficulties for perks given to lower-paid employees (eg work place nurseries), we could exempt these benefits from tax in the hands of the employees, while offsetting that by disallowing the cost as a business expense in the hands of the provider. This could also be extended to other benefits which are, in practice, currently exempt in the hands of the employee - eg canteens and sports facilities.

2. I should be grateful for a note on this by Thursday evening, for discussion at the overview meeting next Monday, together with the further note on car scales if we do not proceed with an FBT.

A handwritten signature in black ink that reads 'ACSA'.

A C S ALLAN



COPY NO 7 OF 7

FROM: A P HUDSON

DATE: 20 January 1988

MISS SINCLAIR

cc Mr Culpin
Mr Riley
Mr Michie**FBT: OUTLINE PRESENTATION**

Thank you for sending me a copy of your 20 January minute. My views on the general points in your paragraph 4 are as follows:

- (i) I am a bit nervous of too much moralizing about fringe benefits. The Government keeps saying it believes in free markets, and that employers must decide what they can afford to pay their staff. The logic of this is that, if they choose to pay fringe benefits, that is up to them.
- (ii) Scrapping P11Ds sounds a good idea.
- (iii) I think we have to present the new arrangements as a simplification, albeit a simplification all round - ie. simpler for employees, simpler for the Revenue, and no worse for employers. Otherwise it is very difficult to explain what we are achieving through FBT that could not have been achieved by other means.
- (iv) Consultation sounds sensible to me, but, as you say, it is mainly for the Revenue to advise.

2. On the outline, my only suggestion is for a different approach ... to the first couple of sections. I attach a draft.

A handwritten signature in black ink, appearing to be 'A P HUDSON'.

A P HUDSON

BUDGET SECRET: TASK FORCE LIST

COPY NO. OF .

FBT: DRAFT REVISED OPENING

Introduction

Government proposes to reform taxation of fringe benefits, to make system simpler, fairer, and more comprehensive.

The problem

- Under present regime, fringe benefits are proliferating, and administration increasingly cumbersome.
- Benefits are proliferating mainly because they are under-taxed relative to earnings. Unfair on those who do not get benefits. And divisive, because encourages "them and us" attitude in businesses. Fringe benefits principally a UK phenomenon [if true].
- Administration is cumbersome: employers have to return P11D form for every employee earning over £8,500, whether he/she receives benefits or not; Revenue have to examine them; employee then has to pay tax.
- If no action taken, problem likely to get worse.
- Government has therefore decided on major reform.



COPY NO. 23 OF 23 .

FROM: J M G TAYLOR

DATE: 25 January 1988

MR LEWIS - Inland Revenue

- cc PS/Chief Secretary
- PS/Financial Secretary
- PS/Paymaster General
- PS/Economic Secretary
- Sir P Middleton
- Sir T Burns
- Mr Anson
- Sir G Littler
- Mr Monck
- Mr Scholar
- Mr Culpin
- Miss Sinclair
- Miss C Evans
- Mr Cropper
- Mr Tyrie
- Mr Call

- Mr Battishill - IR
- Mr Isaac - IR
- Mr Painter - IR
- PS/IR

FRINGE BENEFITS

The Chancellor has seen and noted your submission of 22 January. He awaits the separate submission on the general question of increasing the car scales under the present benefits system.

A handwritten signature in black ink, appearing to be 'J M G Taylor'.

J M G TAYLOR

COPY NO 1 OF 8 COPIES

FROM: MISS M HAY
DATE: 25 JANUARY 1988

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Economic Secretary
Sir Peter Middleton
Sir Terence Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Riley
Miss Sinclair
Mr Cropper
Mr Tyrie
Mr Call

Mr McGivern - IR
Mr Johns - IR
PS/IR**PRIVATE RENTING: BRIEF FOR MEETING WITH MR RIDLEY**

You are meeting Mr Ridley tomorrow to discuss the possibility of tax relief for private rented accommodation. You may also wish to tell him about your proposal to abolish mortgage interest relief (MIR) on home improvements. This brief covers both issues.

Possible tax relief for private rented accommodation

2. Following your exchange of correspondence with Mr Ridley last summer you agreed to consider the case for modest tax measures which would give a boost to the private rented sector and would be good value for money. An interdepartmental group under the chairmanship of Mr Cassell reported to you and Mr Ridley on 19 November.

3. The report concluded that even after deregulation, it seems unlikely that the rents obtainable will provide a sufficiently attractive return to landlords to call forth a supply what would meet the expected housing needs of those seeking to rent. There is

HAY
→
CHEX
25/1

therefore a case for considering methods of providing investors with a rate of return which would encourage the building of housing for rent without driving rents up beyond a reasonable affordable level for potential tenants. The report identified four possible forms of tax relief designed to boost the rate of return to the investors:

- BES relief for investment in company providing accommodation for let;
- writing down allowances for new or refurbished accommodation for let;
- sideways relief for interest costs;
- exemption of proportion of rental income from letting a room in one's own house.

4. You have concluded that tax relief alone can do little to bridge any significant gap between supply and demand for rented housing. Nevertheless given that one reason why deregulation may prove insufficient to bring forward an adequate supply of rented accommodation over the next 5 years or so is because it will take time to change attitudes to political risk, there might be some merit in introducing a temporary tax measure designed to underline the Government's commitment to deregulation and the private rented sector generally and which would make some direct contribution to supply (ie a "kick start" relief).

5. With that consideration in mind, you will wish to put to Mr Ridley your view that BES relief for investment in companies providing let accommodation is the best of the tax options (we do not know his views). The relief has the advantage of being front-end loaded and so would have immediate effect and therefore the maximum impact in the short-term. (See Annex A for outline of BES.)

6. You will want to point out that a full BES relief would be very generous. As indicated in the report (see table attached at Annex B) BES relief boosts the rate of return to a 50 per cent taxpayer holding his investments for five years to 15.3 per cent compared with a 4 per cent rate of return if no such relief existed. You will want to explain to Mr Ridley that you therefore consider that "half-BES" relief would be more appropriate for private renting. Rather than giving relief on the whole of an investment by an individual in a

company offering accommodation for let, you would offer tax relief on half such an investment. This would give a 50 per cent taxpayer a rate of return of the order of $8\frac{1}{2}$ -9 per cent rather than the 15 per cent offered by full BES relief. Although less generous, this $8\frac{1}{2}$ per cent is around the required rate of return suggested in the indepartmental report.

7. As a tax relief is seen essentially as something to give private renting a kick-start after deregulation, there is a strong case for time-limiting the BES relief. The Financial Secretary has recommended a 5 year limit.

8. If Mr Ridley presses for a different option, or an additional measure, you will wish to point out that any new relief would be contrary to the general thrust of Government tax policy.

- sideways relief for interest would further enhance the already favourable treatment of interest on borrowing for investment in housing vis a vis equities
- extending the availability of capital allowances for new or refurbished rented properties would be a step backwards from the 1984 corporation tax reforms involving giving a writing down allowance over 25 years for an asset which would be likely to appreciate over such a period.

An extension of BES, which is an existing relief, would not present as large a problem.

9. You will wish to explain to Mr Ridley that you would want to focus the relief on the sort of accommodation most needed. To this end it would be helpful if your officials could meet with his as soon as possible to discuss how the relief can be targeted effectively. Your provisional view is that relief might be targeted on new style assured tenancies with some restrictions to exclude more expensive properties.

Abolition of mortgage interest relief on home improvements

10. You may wish to take this opportunity to tell Mr Ridley about your proposals for curtailing mortgage interest relief on loans for

home improvements. This of course will not be welcomed by Mr Ridley, particularly against the background of the Government's recent White Paper which stated the Government's commitment to the improvement of the housing stock in inner cities. The position of private landlords will not be affected. They will continue to get relief on expenditure on improvements including interest costs.

11. Recent evidence suggests that the bulk of the relief goes not to those undertaking major works, such as building additional rooms, but rather subsidises the cost of patios, double glazing and other features scarcely distinguishable from general consumer spending. So the effect on the improvement of the housing fabric should be limited.

12. In explaining your reasons for withdrawing this relief, you will want to highlight the recent PAC criticisms of the level of abuse of MIR for home improvements. In evidence to the Select Committee the Revenue have indicated that up to 20 per cent of relief for loans for home improvements is obtained fraudulently. The PAC have put very strong pressure on the Revenue to try to clamp down on this abuse of the relief. The Revenue have taken measures to do so but it is very difficult to police the relief without deploying large additional administrative resources. The change will however have to be publicly presented in terms of concentrating relief on home buyers.



MISS M HAY

Main features of BES relief

The relief applies to investment in new shares in any company not connected with the investor which:

- (i) carries on a qualifying trade
- (ii) is not quoted on the Stock Exchange or the USM

The investor receives tax relief at his marginal rate on the amount invested up to an annual ceiling of £40,000. (The proposed "half-BES" relief would apply to only half the amount invested.)

When the investor sells his shares the proceeds are not charged to capital gains tax.

To obtain full relief the investor must hold his shares for 5 years or more.

The main exclusions from BES are banking, dealing in shares and land, leasing or hiring, investment in eg wine, whisky, accountancy services. There is also a restriction on companies with substantial property backing.

EFFECT ON RATES OF RETURN OF DIFFERENT TAX POLICIES

Assumptions: 3% inflation) Baseline
 1.5% real rent growth)
 6% real interest rate

TABLE 5

Four and a half per cent net rental yield

Real pre tax and post tax rates of return (%)

	individuals		companies	
	pre tax	post tax	pre tax	post tax
baseline (3% inflation 1.5% rent growth)	5.2	4.0	5.2	4.3
Sideways Relief	n/a	4.7	n/a	
BES scheme (30 year holding period)	n/a	7.0	n/a	
BES scheme (5 year holding period)	n/a	15.3	n/a	
4% writing down allowance	n/a	6.8	n/a	6.5

TABLE 6

Seven and a half per cent net rental yield

Real pre tax and post tax rates of return (%)

	individuals		companies	
	pre tax	post tax	pre tax	post tax
baseline (3% inflation 1.5% rent growth)	11.9	8.7	11.9	9.5
Sideways Relief	n/a	8.7	n/a	
BES scheme (30 year holding period)	n/a	14.1	n/a	
BES scheme (5 year holding period)	n/a	25.3	n/a	
4% writing down allowance	n/a	13.5	n/a	12.7

n/a = not applicable

TYRIE
CHÉX
26/1

CHANCELLOR

FROM: A G TYRIE

DATE: 26 JANUARY 1988

cc Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Riley
Ms Sinclair
Ms Hay
Mr Cropper
Mr Call

PRIVATE RENTING: MEETING WITH MR RIDLEY

I have just seen Ms Hay's brief for this meeting.

I am slightly concerned that paragraph 6, on 50% BES, digs our heels in too firmly. Ms Hay says that full BES relief would be very generous. She uses figures to illustrate this, based on the same method of calculation as the figures in the original private rented sector paper (which Mr Ridley will have), and on a 50% top rate. As we all know, these so-called 'rate of return' are pretty spurious calculations.

Mr Ridley will probably argue, rightly I think, that we don't want this scheme to be a flop like all our other attempts to revive the private rented sector (shorthold, old style assured tenancy etc). It would be a pity if we put 'half-BES' to Mr Ridley in a way which sealed off the possibility of anything more generous.

AGT.

A G TYRIE

BUDGET SECRET : TASK FORCE LIST

COPY NO 1 OF 12

FROM: MISS M HAY

DATE: 26 January 1988

CHANCELLOR

cc The Chief Secretary
 Financial Secretary
 Mr Scholar
 Mr Culpin
 Mr Riley
 Miss Sinclair
 Mr Cropper
 Mr Tyrie
 Mr McGiven IR
 PS/IR

Ch See also Mr Tyrie's
 minute, behind.

26/11

PRIVATE RENTING : TODAY'S MEETING WITH MR RIDDLEY

It is possible that Mr Riddley may raise the issue of the existing tax relief for properties let under the current assured tenancies scheme at this afternoon's meeting.

2. Writing down allowances (4% on a straightline basis) are available for certain properties for let under the existing assured tenancies scheme. The relief is temporary, being available only for expenditure incurred before 31 March 1992.

3. The current housing bill will convert old style assured tenancies to new style and will disapply the provisions of the 1980 Housing Act so that properties currently eligible for relief will cease to be "qualifying" properties. If no action were taken those properties would get no further relief and if, as is likely, the housing had increased in value the writing down (depreciation) allowances they had already received would be clawed back.

Line to Take

4. If Mr Ridley raises this issue you may wish to tell him that you intend to take steps to ensure that relief already given is not clawed back, and that writing down allowances will continue to run on expenditure already incurred. Treasury Ministers are currently considering the extent and nature of the necessary transitional provisions.

MARY HAY



COPY NO. 18 OF 19 COPIES

ppp

FROM: J M G TAYLOR
DATE: 27 January 1988

MISS M HAY

cc PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Riley
Miss Sinclair
Mr Cropper
Mr Tyrie
Mr Call

Mr McGivern - IR
Mr Johns - IR
PS/IR

PRIVATE RENTING: MEETING WITH MR RIDLEY

The Chancellor was grateful for the briefing for this meeting.

2. The Chancellor saw Mr Ridley alone. He has reported that he told Mr Ridley about his proposal to abolish MIR on home improvements. Mr Ridley did not flinch from this. He hoped, however, that it might be possible to retain MIR for those cases where an individual purchased an uninhabitable building and converted it into living accommodation. The Chancellor undertook to look further at the possibility of retaining MIR for this category of home improvement.

3. On encouraging the private rented sector, Mr Ridley's favoured option was to treat letting as trading for tax purposes. The Chancellor said that he thought that the cost of this option would be prohibitive. There might also be demarcation difficulties. But he undertook to look at this further and to report to Mr Ridley on the results of his investigations. It was agreed that, if this

BUDGET SECRET: TASK FORCE LIST



option did not run, the half BES relief should become the lead option. Mr Ridley agreed that discussions between officials should now take place - his nominee for this was Mr Philip Fletcher.

mpw

pp

J M G TAYLOR



COPY NO. 19 OF 20 .

FROM: J M G TAYLOR

DATE: 5 February 1988

bf
17/2
(for speaking to ...)
(initials)

JMGT
PS/ST
5/2

PS/FINANCIAL SECRETARY

- cc PS/Chief Secretary
- PS/Economic Secretary
- Sir P Middleton
- Sir T Burns
- Mr Scholar
- Mr Odling-Smee
- Mr Culpin
- Miss Sinclair
- Mr Riley
- Mr Cropper
- Mr Tyrie
- Mr Jenkins - OPC
- Mr Battishill - IR
- Mr Isaac - IR
- Mr Painter - IR
- Mr O'Connor - IR
- PS/IR

**MORTGAGE INTEREST RELIEF: IMPROVEMENT LOANS
STARTER NO.115**

The Chancellor has seen your minute of 3 February. He agrees with the Financial Secretary's conclusion that we should reject the proposal that improvement loan relief might be retained in circumstances where an individual purchased an uninhabitable building and converted it into living accommodation.

J M G TAYLOR



**MINUTES OF A MEETING HELD IN THE CHANCELLOR'S ROOM,
HM TREASURY, AT 2.00PM ON FRIDAY, 29 JANUARY 1988**

Those present

Chancellor of the Exchequer
Financial Secretary
Sir P Middleton
Sir T Burns
Mr Monck
Mr Scholar
Mr Culpin
Miss Sinclair
Miss G C Evans
Mr Michie
Mr Cropper
Mr Tyrie
Mr Call

Mr Battishill - IR
Mr Isaac - IR
Mr Prescott - IR
Ms Rhodes - IR

TAXATION OF FRINGE BENEFITS

Papers: Mr Lewis's minute and enclosures of 28 January;
Mr Monck's minute of 28 January; Financial Secretary's
minute of 25 January; previous papers.

The Chancellor was grateful for the papers submitted for the meeting. He had reflected carefully on the issues raised both in these and in earlier papers. The time had come to reach a conclusion on the direction of work relating to the taxation of fringe benefits. As work on the proposed FBT had developed, the net advantage of introducing it had become more and more marginal, to the point where it seemed too small to justify the necessary upheaval. He had therefore concluded, with some regret but with no hesitation, that it would not be right to pursue the FBT further in this Budget. He was most grateful for all the work that had been done.

BUDGET SECRET: TASK FORCE LIST



2. The Chancellor proposed that the meeting should concentrate on options for maximising the take from conventional taxation of cars. He had two preliminary questions. First, was it possible to make the new scale charges effective from 1988-89? This would mean that higher receipts would be available from year 1 rather than year 2; and the increase in taxation of cars could be matched with the reductions elsewhere in the package. Mr Cropper noted a third advantage: it would be easier to introduce this increase at a time when company profits were buoyant.

3. Mr Lewis said it would be possible to make this change in 1988-89. There would be an administrative cost: the Statutory Instrument for 1988-89 had been laid, and the increases coded out in individual tax assessments. These would need to be revised. Mr Battishill said that legislative procedures might mean that the increase could not be implemented until the Finance Bill received Royal Assent. These points would need to be examined further.

4. The Chancellor said that, subject to further examination of the administrative costs, we should proceed on the basis that the increase would take place in 1988-89. Earlier statements, at the time the 10 per cent increase in 1988-89 was announced, should also be examined to ensure that nothing was said which could be held to contradict this action.

5. The Chancellor's second question related to the P11D limit. If that were raised to £10,000, it might permit a larger increase in the car scales. Could this increase the revenue take in comparison to maintaining the threshold at £8,500? An increase in the P11D limit would, of course, need to apply to all benefits. The Chancellor invited the Financial Secretary to look further at this.

6. The meeting considered the issues in Mr Lewis's paper of 28 January ("Cars - income tax options"). On the main options, the



Chancellor said that further work should concentrate only on options 2 and 3, and only on increases of 75 per cent and 100 per cent in the scale charges. Table B of Mr Lewis's paper should be re-calculated on the basis of implementing the changes in 1988-89. Variants should be examined, and a range of changes around the averages. The further work should identify who the losers would be, and what levels of income they enjoyed. The Chancellor invited the Financial Secretary to take this forward.

7. On the longer-term, the Chancellor said planning should assume an increase of 10 per cent in 1989-90. This figure should not be revealed unless pressed.

8. On special cases, it was agreed to leave the taxation of second business cars on the present basis. It was noted that the "2,500 business miles" limit was virtually unenforceable, and moreover, that the rule was itself curious since it was the private use of the car whence the benefit was derived. There was a case for increasing the mileage limit; but such an increase would also give rise to threshold problems. It was, therefore, agreed to leave taxation of these cars on the present basis. It was also agreed not to alter the taxation for "tool of the trade" cars.

9. On the taxation of expensive cars, the Chancellor noted that the taxing of the benefit should be reviewed in conjunction with the capital allowance rule for such cars. There was a case for combining a larger increase in the taxation of the benefit of these cars with some easing of the capital allowance rules. Some raising of the capital allowance ceiling might be appropriate. The Chancellor invited the Financial Secretary to consider this further.


10. The Chancellor said that he did not think the industrial considerations in Mr Monck's minute of 28 January pointed clearly against an increase in the taxation of company cars. The numbers



might turn out to be rather pessimistic. Moreover, he had told Lord Young of his intention to make a swingeing increase in the taxation of cars and Lord Young had not demurred. There was no need to check the figures further with the Department of Trade and Industry.

11. The meeting considered briefly the taxation of other benefits. The Chancellor was minded to retain the exemption for canteens, but remove it for luncheon vouchers and directors' dining rooms. A scale charge might be a possibility for taxing the benefit of directors' dining rooms. The Financial Secretary was invited to consider this further, in conjunction with the Paymaster General.

12. The Chancellor also invited the Financial Secretary to look further at the taxation of other benefits. The Financial Secretary noted that it had been agreed to exempt entirely car parking and sports grounds.


J M G TAYLOR

2 February 1988

Distribution

Those present
Chief Secretary
Paymaster General

Copy No. 1 of 16

FROM: FINANCIAL SECRETARY
DATE: 5 February 1988

CHANCELLOR

cc Chief Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Mr Scholar
Mr Culpin
Mr Michie
Mr Cropper
Mr Tyrie
Mr Call
Mr Isaac IR
Mr Prescott IR
Miss Rhodes IR
PS/IR

*CVs & Michie's work
LWS*

BENEFITS IN KIND: COVERAGE

You asked me to look at the residual coverage questions now that the decision has been taken to drop the Fringe Benefits Tax.

2. I would suggest that this minute be put on the agenda for Monday's Overview, because the Revenue need early decisions on certain of the issues covered below.

EXEMPTIONS ETC.

3. I would make the following recommendations:

- (i) **Sports and Recreation Facilities:** should be exempt. In theory these are currently taxable so we would need specifically to exempt. The presumption must be that we would publish an ESC although Mr Isaac will look at the possibility of issuing a Statement of Practice instead of an ESC (more generally, I have asked for a note on the difference between these two possible options).

BUDGET SECRET: TASK FORCE LIST

- (ii) **Workplace Nurseries:** these should remain taxable.
- (iii) **Car Parking:** should be exempted (by ESC) if on "own premises" and taxed if not on own premises.
- (iv) **Third Party Entertainment:** should be exempted by legislation, as already agreed and announced.
- (v) **Third Party Gifts:** should continue to be exempt.
- (vi) **Employer Provided Gifts and Entertainment:** should continue to be taxed.
- (vii) **Removal Expenses:** should continue to be exempt pending post-Budget review.
- (viii) **Lower Paid Agricultural Workers' and Clergymen's Concessions:** should continue to be exempt.
- (ix) **Miners' Free Coal:** should continue to be exempt.

4. I would also continue with all the other existing minor concessions and exemptions listed in Mr Prescott's minute of 28 January.

on folder, behind

5. There is not much logic in this list of recommendations. But I think the objective must be to maintain the status quo except insofar as that is leading to problems with the increasing numbers of "higher paid" employees.

6. Two groups of "benefits" not considered above are, in my view, more difficult:

- (i) Accommodation;
- (ii) Canteens, Luncheon Vouchers (LVs) and Directors' Dining Rooms.

ACCOMMODATION

7. The questions for decision here are two-fold:

(i) Is the existing coverage right?

(ii) Do we need to legislate to change the basis of valuation of these benefits in 1988 or would it be better to put this off until 1989?

8. As far as (i) is concerned, I think that the existing position is satisfactory and I see no case for changing it.

9. The second question is more tricky. Since we would be moving from valuations based on 1973 rateable values to a system based on current capital valuations, the change will inevitably create some substantial losers amongst the estimated 90-100,000 recipients of non-exempt provided accommodation. Thus there is an argument that we should begin the move towards more realistic valuations in a year when people will be receiving tax cuts. (I am convinced that we cannot move straight to the new valuations: I think we do need a phasing-in period). This, of course, points to legislation in 1988 and implementation in 1988/89.

10. The counter argument is that since the need for a new valuation system arises from the abolition of domestic rates, we should defer the introduction of the new system until 1989 (when Scottish rates will go). The transitional period would then commence in 1989/90 and would be presentationally linked to the abolition of rates. I think it would be quite difficult to use this defence if we started the transitional period before we needed to.

11. There are arguments both ways but I would recommend putting off this legislation until 1989, not least because I am not convinced that we have focussed clearly enough on how the new valuation rules would work. Certainly if we decided to legislate in 1988 we would need to do a lot of quick and detailed thinking about the new system to be introduced.

CANTEENS, LUNCHEON VOUCHERS AND DIRECTORS' DINING ROOMS

12. As you know the only change we definitely need to make this year is to remove the absurdity (in a rider to an unpublished concession) that Directors' Dining Rooms become taxable if the company gives those of its other employees for whom staff canteens are not available LVs worth more than 15p per day. I think that we all agree that this rider, which is unevenly enforced anyway, is untenable and it could simply be omitted when this concession is formally published. Without the rider, companies could then at least give their employees LVs of more reasonable amounts without thereby triggering a tax charge in respect of the Director's Dining Room.

13. There are strong arguments for stopping there and making no further changes, and these arguments become stronger when one considers all the other possible changes one might devise. I think the Paymaster would probably support this 'do nothing option'; it would not cause difficulties for the Revenue; and it would be the option most consistent with the rest of the recommendations I am making in this note. On balance, I think this option would generate the least political flak in the House.

14. Nevertheless, there are arguments against this minimal option, the strongest being that:

- (i) LVs are virtually indistinguishable from cash and are precisely the sort of benefit which should be taxed, particularly in a Budget which is aimed at removing shelters and anomalous exemptions as a quid pro quo for reducing tax rates;
- (ii) LVs are readily assessable for tax in contrast to many of the other 'benefits in kind' which are or will be exempt;
- (iii) Even without the rider to the Dining Room concession, there would still be the anomaly that the directors could eat well and tax free while the other staff were taxed on all but 15p of their LVs;

BUDGET SECRET: TASK FORCE LIST

(iv) The 15p exemption has been withering on the vine for years and is now so de minimis that it could be removed altogether without any hardship (extra tax bill for a basic rate taxpayer of less than 20p per week!);

(v) The removal of the exemption would - after a large row - put a stop to the annual time-wasting ritual of representations in favour of increasing the 15p limit.

15. I think that the Paymaster takes the view - as I do - that if we taxed LVs without taxing any other of the 'anomalous' benefits we would run into a major storm and would find it very difficult to explain why LVs uniquely had been singled out for punishment. He could live with taxing LVs if miners' coal were taxed too. My own view is that miners' coal leads us straight back to clergymen and agricultural workers.

16. A better route, I think, would be to couple the taxation of LVs with the taxation of Directors' Dining Rooms ((iii) above). Thus the only exemption would be for canteens generally available to all the staff. Even if LVs were given and even if there were a canteen available to all, an exclusive Directors' canteen would be a taxable benefit. This was, in fact, the option you yourself favoured at our meeting last week.

17. Of course, this option is not without its own problems:

(i) Although some of the heat would be taken out of the opposition from the LV Lobby by the decision to tax exclusive canteens, there would still be a row and, in addition, we would get the more muted grumbling from Directors too;

(ii) Although Directors' Dining Rooms are currently taxable and (sometimes) taxed if LVs or canteens are not provided for the staff generally, the Revenue advise that a generalised taxation of this benefit, with far more taxed than at present, would be administratively very difficult under the present employee-based system;

BUDGET SECRET: TASK FORCE LIST

(iii) There would therefore need to be some sort of compounding arrangement under which the employer paid the tax - ie. we would be right back into FBT territory. We would also need to decide how to value the benefit (indirect as well as direct costs?); how to define a Directors' Dining Room; how to distinguish the perk lunch from the business lunch with exempt third parties etc?

18. Despite these difficulties, I think this more radical option is marginally preferable. It does get rid of the LV exemption and does so, in my view, in the least controversial context possible (given that we have ruled out taxing canteens).

g.h.

|| 'NORMAN LAMONT'

BUDGET SECRET: TASK FORCE LIST

py

copy sent



FROM: A C S ALLAN
DATE: 5 February 1988

MR MACE

cc PS/Financial Secretary
Sir P Middleton
Sir T Burns
Mr Scholar
Mr Culpin
Mr Cropper

Mr Isaac - IR
PS/IR

ACSA

Sp. ('X' below)

Jf

ADDITIONAL PERSONAL ALLOWANCE

The Chancellor would be grateful for advice on one additional option on the APA, as soon as possible. This is to withdraw the APA over the same range of incomes as the MCA is to be withdrawn. The objective would be to reduce another tax penalty on marriage, accepting that it would also hit rich single parents, and that two earner co-habiting couples could make sure that the lower earner claimed the APA. The number of people affected would presumably be small, but so should the additional cost to the Revenue.

X1

ACSA

A C S ALLAN



Inland Revenue

The Board Room
Somerset House
London WC2R 1LB

FROM: A J G ISAAC

DATE: 11 FEBRUARY 1988

CHANCELLOR OF THE EXCHEQUER

BENEFITS IN KIND : DIRECTORS' DINING ROOMS

1. Mr Prescott's note below responds to the remit that you gave us at last Monday's Overview. May I try to draw out a few general points.

2. First, I was among those who recognised in the context of the FBT a possible option of enforcing the tax charge on directors' dining rooms (the present exemption is largely by Extra Statutory Concession). Whatever the tax system, there are potentially difficult technical or political issues to be decided on, for example

What is a "directors'" dining room? and
How to define and measure the subsidy?

These difficulties could have been decisive, even in an FBT. A good deal could have depended on whether the answers were broad or narrow, simple or complex. At least, however, the whole point of the FBT was that any tax charge fell on the employer: it was not necessary, in addition, to address a third area of difficulty and identify the benefit enjoyed by individual employees.

3. When we discussed this with the Financial Secretary before last Monday's Overview, we suggested that if Ministers felt it necessary to pursue this possible charge within the present tax system, the most promising approach would be to begin by

establishing the employer's subsidy (as under FBT). One possibility was that the tax might then be paid by the employer at some more or less arbitrary flat rate (a 'mini' FBT, or - more precisely - an arbitrary form of 'compounding' the employee's income tax liabilities). The Overview meeting ruled that out.

4. In theory, a possible variant might be to allow employers to apportion the actual subsidy between the eligible employees on some just and reasonable basis⁽ⁱ⁾ and tax the employees accordingly. Given the obvious scope for argument between employees - would there be a right of appeal against the employer's apportionment? If so, to whom? And would all employees have to join in? - I doubt if that is practicable and indeed I would expect most employers to prefer the "mini FBT".

5. A further possible and more practicable variant⁽ⁱⁱ⁾ might be to apportion the subsidy between eligible employees on a more arbitrary "formula" basis. For example, the legislation could

(a) divide the annual subsidy by the number of eligible employees, and treat each individual employee as having enjoyed his pro rata share of the subsidy; or

(b) multiply the subsidy per meal by the number of meals each individual employee has taken, and treat the individual employee as having enjoyed his (more fine-tuned) benefit accordingly.

(i) Subject to a reasonable split between basic and higher rate taxpayers, the apportionment would be a zero-sum game between the employers and the individual employees, in which the tax office would not need to concern itself unduly.

(ii) A possible sub-variant of this might be to have banded scale charges, so that employees enjoying a subsidy of less than £x (for example £50 a year) were exempt from charge; employees enjoying a subsidy of more than £x but less than £y (for example £100 a year) were treated as enjoying a benefit of £n: and so forth. There is more than one view here whether this sub-variant would help - or add yet further to the complexity.

6. The alternative approaches in (a) and (b) of paragraph 5 above illustrate the basic choice which has to be made, if the objective is to impose a charge to tax not on the employer (subsidising the canteen) but the employees (enjoying the subsidy):

- to the extent that legislation imposes a flat rate charge on every employee with access to a subsidised "directors'" dining room - without modifying the charge in answer to questions: How often does he use the dining room? How much does he eat? How much does he pay? - the tax is open to criticism as being too unfair in too many cases. (In what we tend to think of as "directors'" dining rooms, a realistic charge would need to run well into three, and probably four, figures per annum; but there will be meals for directors and senior staff, provided separately, costing much less than this);
- to the extent that the legislation requires employers or employees to record detailed information - for example how often does each employee use the dining room? How much does he eat and drink? How much does he pay? - it is open to the opposite criticism, of seeking equity at the cost of unacceptable bureaucracy.

7. These arguments seem to me clearly to rule out the two extremes: a universal flat rate scale charge applying to all employees; or (as the Overview meeting recognised) a charge on each employee according to the subsidy which he actually enjoys. There is a question whether there is a viable middle course: something which is admittedly pretty arbitrary and rough justice for individual employees and admittedly a significant additional compliance burden on employers - but neither to an intolerable degree. There are obvious interactions between the mechanics and the scope and size of the charge. ⁽ⁱⁱⁱ⁾ In our earlier discussions with the Financial Secretary some of us suggested that, at least in the absence of the FBT, there were serious

reasons for doubting whether the game was worth the candle. But I cannot see that the answer can lie in a flat scale charge.

C L O R

A J G ISAAC

(iii) It was mentioned in the course of the Overview meeting that there must be some directors' dining rooms which even now are not exempt under the terms of the present ESC. In so far as tax is in practice now charged in these cases (we have no central information on this and no published guidelines), it will be by ad hoc negotiation between the local tax office and local employer and his accountant. Our guess is that the numbers are probably relatively few, and the amount charged on this informal basis relatively small (this is certainly consistent with Mr Scholar's experience of employment with a business that was charged at 15p a day - the value of a tax free luncheon voucher). It is, thus, one of the areas of the benefit system where no great difficulty has arisen, in part because nothing much has changed over 40 years. I very much doubt that continuing 'benign neglect' on the essential details is a realistic precedent, if Ministers are looking for a tax strategy withdrawing the 1948 ESC, and seeking a substantial new tax charge on large numbers of "directors'" dining rooms throughout industry and commerce. In the present day both taxpayers and tax offices would - rightly - demand clear published guidance on the principles under which their new tax liability would be charged, and the way it would be allocated. Whether or not there was new primary legislation (and a scale charge would of course require new primary legislation) it would be necessary for Ministers to address the three main sets of questions - Which dining rooms? What costs? How allocated? - and to publish clear answers of a kind that both taxpayers and tax offices could use in negotiations and any subsequent appeal proceedings.

BUDGET SECRET: TASK FORCE LIST

Copy 1 No of 9 Copies

FROM: P J CROPPER
DATE: 10 February 1988

CHANCELLOR

cc Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Mr Tyrie
Mr Call

1. £20 a month is a round number.
*2. Hester, I attach good importance to the advan-
tge-in, & we must papers for this week
make sure the proposals of consist, Ashwell, M.*

PAYROLL GIVING

You said yesterday that you would like to double the Payroll Giving limit from £120 to £240.

2. Does anybody share my view that we should round up to £250 or £300? People find figures like £240 (£420 for the unit trust element in PEPs) a little mystifying. The £250 would be "a round number", while £300 would provide headroom for £5 a week in any foreseeable leap year.

3. While on the subject I draw your attention to a letter I received from one of the CAF team after the Home Secretary's recent seminar, setting out the case for Treasury/Home Office expenditure on publicising the Payroll Giving Scheme.

4. Your Lollipop idea, with accompanying publicity expenditure, meets the present need in a very constructive way, but I think it will be helpful if I can say to Andrew Phillips, and Brophy himself, that Treasury Ministers have been appraised of the point.

P J CROPPER

20 Old Bailey,
London EC4M 7EP
Telephone: 01-236-9081
Telex: 887284 Parlex G.
Fax: 01-236-7458
DX: 46703 (Old Bailey)

and at: Sudbury, Suffolk
Tel. 74433 and Ipswich Tel. 219282

Your Ref:

Our Ref: AWP/KP/

Bates, Wells & Braithwaite

Solicitors

25th January, 1988

Peter Cropper, Esq.,
H.M. Treasury,
Westminster,
London, S.W.1.

Dear Mr. Cropper,

Further to the meeting chaired by the Home Secretary this morning and our discussion after it, you invited me to drop you a line summarising the argument for the Chancellor making available the funds necessary to promote his payroll giving scheme through television (and possibly other advertising) via the COI. The argument, it seems to me, runs as follows:

- (i) The payroll giving scheme is potentially revolutionary. It is intended to be a lever by which the charitable impulse, well established in our culture, is encouraged to show itself amongst wage and salary earners in a much more active and generous form.
- (ii) Although the major charities, and the handful of agencies (CAF to the fore), have made strenuous efforts to use this instrument of giving placed in their hands by the 1976 Finance Act, the results so far have been, not to beat about the bush, disillusioning. CAF tell me that they have firms which have signed up with a potential employee/donor base of well in excess of five million people, but that only 35,000 or so employees have actually signed on the dotted line.
- (iii) All this despite the fact that tremendous efforts have been made all round. I have first hand experience of one consortium of charities which have banded together to persuade as many as possible of these 5½ million to give, and to give to their consortium (which, through the agency, then distributes to each of the charities in the consortium). Their ability to go on financing

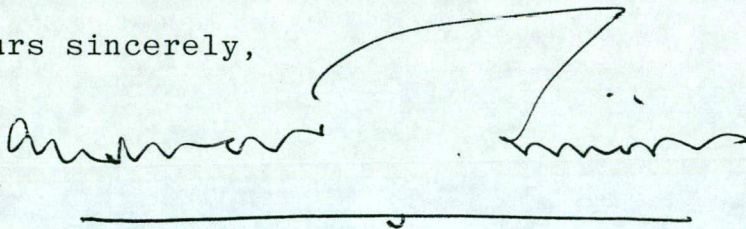
.../...

this marketing operation is strictly related to the returns, which frankly do not warrant it.

- (iv) In effect, everyone has under-estimated the cultural hurdle which needs to be leaped in order to cash in on the potential. Like many things which should be simple, the gap between the idea and the act of signing up is much bigger and more difficult to bridge than all of us who are enthused by the scheme have expected.
- (v) The fear now is that those who have invested substantial sums and manpower in getting the scheme off the ground will gradually withdraw from the effort, and that, far from the scheme taking off gradually, it will die gradually.
- (vi) There is the additional problem that trustees of charities have to take an extremely cautious, prudential view of the way they spend funds, particularly in the public relations area. There is no doubt that many of them are unwilling to invest in major advertising (least of all television advertising) on the legally proper grounds that much of the benefit of their advertising will accrue generally to the charity sector, and not to their charity particularly.
- (vii) Given that when he spoke at the CAF Conference Nigel Lawson was expecting that he would be yielding £20m. in "lost" tax, and given that he is now going to give away far less, one would like to see him breathing real life into his brainchild by financing a COI attack to kickstart the scheme into real life.
- (viii) This is not, I would submit, a case where the charities have been idle or half-hearted. Both the government and the charity sector share an excitement as to the permanent change in the sourcing of voluntary effort which the scheme could effect, but without this major promotion it could merely limp along.

Is there any chance do you think that something could be done about this as a matter of urgency?

Yours sincerely,



A handwritten signature in cursive script, appearing to read 'Andrew Phillips', is written over a horizontal line.

ANDREW PHILLIPS

BUDGET CONFIDENTIAL



FROM: P D P BARNES
DATE: 11 February 1988

PS/CHANCELLOR

cc PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
Mr Cropper
Mr Tyrie
Mr Call

*Chy see also PM's note,
behind. 28/11/2*

PAYROLL GIVING

The Economic Secretary has seen Mr Cropper's minute to the Chancellor of 10 February.

2. The Economic Secretary thinks there is quite a lot to be said for a Government funded publicity blitz, not least politically. He thinks it would help to put across the idea that tax cuts are not purely selfish but an opportunity for personal generosity.

*Business @
payors. I agree with
the EST. AS for the sum,
Spoke to 7240 (720 = mark).
M:-*

RB

P D P BARNES
Private Secretary

** altho' cautious
minutes, I understand*

Jonathan



FROM: S P JUDGE
DATE: 11 February 1988

PS/CHANCELLOR

cc PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
Mr Cropper
Mr Tyrie
Mr Call

PAYROLL GIVING

The Paymaster General has seen Mr Cropper's (TFL) minute of 10 February.

2. He would go for £300, which (unlike £250) has the virtue of being readily divisible by 12.

S P JUDGE
Private Secretary



COPY NO 29 OF 29

FROM: J M G TAYLOR

DATE: 11 February 1988

MR CAYLEY - INLAND REVENUE

cc PS/Chief Secretary
 PS/Financial Secretary
 PS/Economic Secretary
 PS/Paymaster General
 Sir P Middleton
 Sir T Burns
 Sir G Littler
 Mr J Anson
 Sir A Wilson
 Mr M C Scholar
 Mr Culpin
 Mr Sedgwick
 Mr Odling-Smee
 Miss C Evans
 Mr Michie
 Miss Sinclair
 Mr Riley
 Mr Cropper
 Mr Tyrie
 Mr Call
 Mr Unwin - C&E
 Mr Battishill - IR
 Mr Isaac - IR
 Mr Painter - IR
 Mr Pitts - IR
 PS/IR

CAPITAL GAINS TAX: REBASING AND ABOLISHING INDEXATION

The Chancellor was grateful for your note of 10 February. He has concluded that this option need not be pursued further.

A handwritten signature in dark ink, appearing to be 'JMG'.

J M G TAYLOR



COPY NO. 12 OF 13. *pm*

FROM: J M G TAYLOR

DATE: 11 February 1988

MR MACE

1. ~~Alex~~
To note for
overview agenda.
2. ~~Put in review folder.~~

cc PS/Financial Secretary
Sir P Middleton
Sir T Burns
Mr Scholar
Mr Culpin
Mr Cropper
Mr Battishill - IR
Mr Isaac - IR
Mr Painter - IR
PS/IR

INDEPENDENT TAXATION:

WITHDRAWAL OF MCA AND ADDITIONAL PERSONAL ALLOWANCE

The Chancellor was grateful for your submission of 9 February. He would like to discuss this at the next Overview meeting.

JG

J M G TAYLOR



COPY NO. 9 OF 9 .

FROM: J M G TAYLOR

DATE: 11 February 1988

MR CROPPER

cc PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Tyrie
Mr Call**PAYROLL GIVING**

The Chancellor has seen your minute of 10 February.

2. He has commented that £20 a month is a round number. However, he attaches great importance to the advertising tie-in, and we must prepare for this without delay, making sure that the proprieties, of course, are observed.

A handwritten signature in dark ink, appearing to be 'J M T'.

J M T TAYLOR

pr

COPY NO. 2 OF 34

FROM: C J RILEY
DATE: 11 FEBRUARY 1988

CHANCELLOR

cc PPS

Chief Secretary	Miss Sinclair
Financial Secretary	Miss C Evans
Paymaster General	Ms Munro
Economic Secretary	Mr A Hudson
Sir P Middleton	Mr Cropper
Sir T Burns	Mr Tyrie
Sir G Littler	Mr Call
Mr Anson	<u>Inland Revenue</u>
Sir A Wilson	Mr Battishill
Mr Byatt	Mr Isaac
Mr Scholar	Mr Painter
Mr Culpin	Mr Lewis
Mr Odling-Smee	<u>Customs and Excise</u>
Mr Sedgwick	Mr Unwin
	Mr Knox

SUBSIDISED MORTGAGES: IMPLICATIONS OF WITHDRAWING MIR

I attach a paper which Alison Munro and I have prepared. It should be read in conjunction with Mr Lewis's paper, also circulated today.

2. Our paper concludes that any general supply side gains, through effects on house prices, are likely to be very small. There could be some beneficial effects in cases where employees are currently locked in by cheap mortgages, but the effects could be perverse if the charge applied only to new loans.

3. If subsidised mortgages were effectively discouraged by a new charge, there is every chance that employers would resort to other means of locking-in their employees should they wish to do so. They might opt to provide other benefits, or perhaps annual bonuses which avoid employee NICs. My conclusion is that while action to prevent the wider spread of benefits is desirable, action on (smaller) subsidised mortgages alone is less easy to justify.



C J RILEY

SUBSIDISED MORTGAGES: IMPLICATIONS OF WITHDRAWING MIRIntroduction

This paper considers the implications of a tax charge which effectively withdraws the MIR available on subsidised mortgages. It assumes that MIR is withdrawn from the subsidy element only, not from the interest actually paid.

2. It also assumes that income tax is applied to the gross interest subsidy on such mortgages. An alternative would be to tax the net value of the subsidy to the employee, after allowing for the reduction in MIR, which would imply a somewhat lower effective tax rate on the subsidy. There is an argument for this in principle - the effective tax rate would then be closer to the combined rate of NICs payable on salaries* - but it would be somewhat more complicated in practice. This option is not pursued further; it would have similar but smaller effects than the main option.

3. The issue of whether to apply the charge to existing mortgages or only to new mortgages is discussed in Mr Lewis' paper. In the long run this would make very little difference to the overall effect, but the short run effects would be different. The implications for locking-in, for example, would be very different. For the most part this paper assumes that the change applies to all existing mortgages.

4. There are a number of forms of interest qualifying for relief where the same question arises - ie whether they should be taxed if subsidised by the employer. The arguments for and against their inclusion are considered in Mr Lewis's paper. We would not expect many employers actually to subsidise such loans (though information is lacking) so the issues are mainly presentational and administrative rather than of substance.

* Charging basic rate tax on the net subsidy implies a rate of 19% (75% of 25%) on the gross subsidy, which is almost exactly equal to the combined rate of NICs below the UEL.

5. The effects of acting on mortgage interest are discussed in the sections which follow. They include:

- a reduction in the scale of subsidised mortgages, or a slower build up - it is difficult to see what incentives would remain for mortgages less than £30,000;
- upward pressure on pay, especially in the financial sector and the southeast, and/or increased growth of other benefits;
- some reduction in the upward pressure on house prices at the lower end of the market, though not necessarily more in the southeast than elsewhere;
- possibly, but by no means certainly, some improvement in labour mobility.

General background

6. Although information is limited, we think that subsidised mortgages are provided mainly in the financial sector. There are no general rules, but eligibility is frequently restricted to employees above some minimum age (often 21 or 23 years), subject to a minimum length of service (often 1 or 2 years). We estimate that about 2/3 of those eligible for subsidised mortgages actually take them up - around 260,000 in banking, insurance and other financial institutions. The average size of subsidised mortgages is around £24,000.

7. We do not have any detailed figures on the breakdown of subsidised mortgages by salary or by region. They are likely to be available to employees of banks and building societies throughout the country, as well as other financial companies. But the financial sector looms largest in the southeast - 15% of all employees at the end of 1986 on a wide definition, compared with only 8% nationally - where pay levels are typically higher than elsewhere in the economy. Growth in this sector has also been particularly large in the southeast over the last two years, with some very large salaries and very large loans offered to attract staff.

8. In some cases individuals can negotiate a remuneration package involving both salary and subsidised mortgage, with some trade-off between the two. But eligibility for subsidised mortgages is probably an add-on to salary for most employees affected. Individual pay levels for employees of banks and building societies are not normally dependent on whether they actually take up a subsidised mortgage or not. But again, this is an area on which we have little statistical information.

9. Subsidised mortgages provide a number of advantages compared with higher salaries, for both employees and employers. For employees they provide a way of avoiding NICs, and perhaps of acquiring larger loans than would otherwise be available to them. Employers do not pay NICs on mortgage subsidies, and may regard them as a way of locking-in their employees. In addition employers may regard such loans as less risky than loans to the general public.

10. In any event there seems every likelihood that subsidised mortgages would continue to spread, both within and outside the financial sector, in the absence of action to redress the NIC advantage. Rapid growth of house prices, especially in the southeast, puts a premium on this method of attracting and retaining staff.

Effects on Mortgages and Pay

11. This is where the most immediate effects will arise.

(a) If MIR were withdrawn from all subsidised mortgages

There are various possible responses:

(i) Do Nothing

The cost of the additional tax would be borne entirely by employees.

- (ii) Retain existing subsidised mortgages, but raise pay
The cost of the additional tax would be borne at least in part by employers. Full compensation of the employee might require an average pay increase of around 2-3%.
- (iii) Cash out mortgages
Full compensation of the employee would increase the cost to the employer because of the NIC charges. The most likely outcome is perhaps a sharing of the additional cost between employer and employee. The required pay increase might be in the region of 7-8% on average.
- (iv) Replace subsidised mortgages by alternative benefits in kind
This would yield the same advantage to the employee, with the same cost to the employer, as subsidised mortgages do now (ie no NICs paid). A variant on this option might be an annual bonus or housing allowance, which would attract employers' NIC but largely escape employee NIC.

12. Annex A illustrates the effects of options (i) to (iii) for a typical subsidised mortgage. Estimates of the overall effects on revenue if all employers made the same response are shown in the table below. Note that they do not allow for the spreading of pay increases/alternative benefits to other employees, and ^{increase in} any consequent tax/NIC revenue.

Overall effect on tax/NIC revenue (£million)

	<u>IT</u>	<u>NIC</u>	<u>CT</u>	<u>Total</u>
(i) Do nothing	90	0	0	90
(ii) Raise pay, keep loan	130	20	-50	100
(iii) Cash out (to fully compensate employee)	5	50	-20	35
(iv) a) Alternative benefit in kind	0	0	0	0
b) Annual bonus	0	30	-10	20

13. Option (i) - doing nothing - may not be a very realistic option even in the short run. Many employees, particularly at the lower end of the salary scale would probably find it very difficult to meet the extra tax liability. There would almost certainly be strong pressure on employers to renegotiate remuneration packages quickly.

14. Option (ii) - continuing the cheap loan but increasing pay - would not be a sensible response for mortgages below £30,000, since cashing out would allow the employee to be at least as well off, at lower cost to the employer. This is because the employee would get additional MIR by cashing out, so the necessary compensation from the employer would be less. This is illustrated in Annex A. There is an even stronger incentive for cashing out such mortgages for higher rate employees.

15. For cheap loans above about £55,000 (for basic rate taxpayers and assuming an average subsidised interest rate of 5%) the additional employers NIC charge that would be incurred by cashing out would be greater than the cost to the employer of fully compensating the employee for the "tax" on the cheap loan; so in these cases cheap loans might continue. But the more rational response would be to "cash out" the part of the mortgage below £30,000, and offer a cheap "top up" loan.

16. In the longer run we would expect almost all existing cheap loans below £30,000 to be either cashed out or replaced by other benefits. If the subsidised loan had been a pure add-on, the employer might be unwilling to cash out because he would probably have to extend higher pay to other employees. In this case some other form of extra remuneration seems more likely.

17. The employer could substitute alternative benefits for cheap mortgages. If employees already receive the more common benefits, such as cars, it may be possible for employers to devise new benefits which do not incur high administrative costs. Another quite attractive possibility for employees below the UEL is some form of annual bonus or housing allowance, which could be targeted on those having their mortgage subsidy withdrawn. This might

largely avoid employee NICs, because in the month of payment it could take cash remuneration above the UEL, but would be liable to employer NICs.

18. If this analysis is accepted, our figures suggest that the increase in tax/NIC revenue is likely to be in the range £0-40 million, given the present scale of cheap mortgages. A reasonable central figure might be £20 million, which corresponds to the case where the annual bonus/allowance is paid. But to the extent that cheap mortgages could be expected to spread further through the economy in the absence of action, the increase in revenue could well be greater.

(b) If applied to new mortgages only

19. Subsidised mortgages below £30,000 would no longer be attractive, and hence would tend not to be offered by employers. Larger loans or "top-up" loans above £30,000 might continue to be offered at cheap rates in order to attract staff. And there would be a tendency for pay and/or other benefits to rise.

20. But there would almost certainly be some impact on the pay and benefits of existing employees as well. It would be difficult to restrict pay increases or alternative benefits to new employees; at the very least existing employees without cheap loans would demand the increase. It is anyway unlikely that employers would wish to operate a two-tier pay system; so they might offer to "buy out" existing cheap loans in one way or another.

21. The revenue yield if MIR were withdrawn only from new loans would depend mainly on what happened to existing employees. The yield from new employees will be very small - slightly higher NIC if they receive pay or a bonus rather than a cheap loan. If increased remuneration spread to all employees, the longer term revenue yield would be similar to the figures given above for withdrawing MIR from existing loans.

Effects on house prices

22. Where higher salaries are given in place of cheap loans, some of the increase - perhaps only a small part - may leak outside the housing market. With additional benefits rather than salaries, there would probably be rather greater leakage. This would tend to reduce the upward pressure on house prices, especially at the lower end of the market.

But the impact on house prices is unlikely to be very large, given the small numbers affected. And at the upper end the effect would probably be negligible, both because MIR is proportionately less important and because there would still be some incentive to provide cheap loans above £30,000.

23. One might expect the effects on house prices to be concentrated more on the southeast, since subsidised loans tend to be concentrated there. But the average building society mortgage in the Greater London area is more than £37,000; and the bulk of very large loans will tend to be in the southeast. So it is not clear that a reduction in the upward pressure on prices will be larger (proportionately) in the southeast than elsewhere. Regional differentials could even widen, but in any case the effects are likely to be small.

Wider effects on labour market(a) Pay

24. Pay increases in the financial sector could not easily be confined to those who had cheap loans. The average pay increase necessary to compensate the latter would be around 8%, but even with some spreading to other employees it is most unlikely that average pay levels in the financial sector would rise by anything like this amount. They already reflect the fact that on average about 1/3 of employers do not take up the offer of a cheap loan; and there would be a clear incentive to employers to provide extra remuneration in the form of benefits and bonuses rather than regular pay. At most one might expect pay to rise by 2 or 3 percent on average.

25. Upward pressure on pay need not necessarily be confined to the financial sector; other sectors may feel constrained to make higher pay settlements in order to keep pace. But this would probably not be a very widespread tendency. The other sectors would not be affected by the phasing out of cheap mortgages, and there would be no need for them to alter pay and benefit levels in order to attract or retain staff. The effect on average pay levels in the economy as a whole would thus almost certainly be very small indeed - at the very most, say, 0.2%.

(b) Labour mobility

26. It is necessary to distinguish two separate effects:

- direct effects of subsidised mortgages, including locking-in effects;
- indirect effects through regional pay and house price differentials.

We consider these in turn.

27. The scale of any direct effect on labour mobility is unclear. Locking-in effects are likely to be confined largely to those cases where an employee is granted a loan which is significantly larger than he or she could obtain elsewhere; normal sized loans would not greatly inhibit mobility, they would simply be aggregated with income in assessing incentives to move jobs.

28. Subsidised loans below £30,000 would be hardest hit by the charge, and such loans may be greater than employees on relatively low incomes could obtain elsewhere. The degree of locking-in might therefore be somewhat reduced for these people. But on very large loans, well above the £30,000 ceiling, the loss of tax relief would be small in relation to the total interest paid. And individuals with sufficiently high salaries currently have little difficulty in obtaining very large mortgages. Any locking-in associated with very large mortgages is therefore unlikely to be much reduced by the charge.

29. Taxing subsidised mortgages would probably cause firms who wished to lock in their employees to seek other ways of doing so. Higher pay would be the obvious way, though they would have to pay higher employer NICs. A more cost effective way would be to increase the scale of other benefits - eg cars, medical insurance - which would continue to have the same NIC advantage as currently enjoyed by subsidised mortgages.

30. It is therefore rather doubtful whether withdrawing MIR on subsidised loans would lead to a very substantial improvement in labour mobility by reducing the extent of locking-in. Indeed, one could argue the reverse: discouraging subsidised mortgages may make moving between jobs more difficult for those affected. This would be very likely to occur if the withdrawal of MIR applied to new loans only. Those with subsidised loans at present would be strongly discouraged from moving jobs or locations - probably a stronger locking-in effect than anything inherent in the current system.

31. The indirect effects are most likely to affect those who do not have access to subsidised mortgages. Insofar as house prices fall (or rise less) in the southeast relative to those elsewhere in the country, this will make it easier to attract labour to the southeast without widening pay differentials. By the same token, labour will be less inhibited from moving out of the southeast for fear of being unable to return. But, as already noted, our view is that any effects on regional house price differentials is likely to be small - possibly even perverse - so it is difficult to see any great improvement in labour mobility from this source.

Conclusion

32. Withdrawing MIR from subsidised mortgages could produce some supply side gains by improving labour mobility. But it is impossible to quantify them. They may be significant in some fairly narrow areas - eg bank clerks and those they compete with - but we cannot be certain of this. And if the charge was applied only to new cheap loans, the effects on the mobility of those who already have them

could well be perverse. We almost certainly cannot look to any very significant effect on house price levels or regional differentials. So overall, any supply side gain seems unlikely to be very great.

BUDGET SECRET: TASK FORCE LIST

ANNEX A: EFFECTS ON EMPLOYEE, EMPLOYER AND TAX/NIC RECEIPTS OF DIFFERENT BEHAVIOURAL RESPONSES, FOR A TYPICAL CHEAP LOAN

Option	Received by employee	Cost to employer	Tax/NIC receipts
Existing situation	Gross subsidy = £1200	Subsidy = £1200	0
(i) Do nothing	Gross subsidy = £1200 Tax on subsidy = -£300 <u>£900</u>	Subsidy = £1200 <u>£1200</u>	Tax on subsidy = £300 <u>£300</u>
(ii) Continue with loan, salary increase to fully compensate employee	<u>Below UEL:</u> Gross subsidy = £1200 Tax on subsidy = -£300 Gross salary = £455 IT = -£114 NIC = -£41 <u>£1200</u>	Subsidy = £1200 Gross salary = £455 Employer NIC = £48 Reduction in CT = -£176 <u>£1527</u>	Tax on subsidy = £300 IT = £114 NIC = £89 CT = -£176 <u>£327</u>
	<u>Above UEL</u> Gross subsidy = £1200 Tax on subsidy = -£300 Gross salary = £400 IT = -£100 <u>£1200</u>	Subsidy = £1200 Gross salary = £400 Employer NIC = £42 Reduction in CT = -£155 <u>£1487</u>	Tax on subsidy = £300 IT = £100 NIC = £42 CT = -£155 <u>£287</u>

- Assumptions:
1. Basic rate taxpayer
 2. Mortgage is £24,000 at interest rate of 5% compared with market rate of 10%; so gross subsidy is £1200 pa.
 3. Employee NIC = 9%, employer NIC = 10.45%, employee is contracted in.
 4. Employer is full CT-paying.

BUDGET SECRET: TASK FORCE LIST

Option	Received by employee	Cost to employer	Tax/NIC receipts
(iii) Cashing out			
a) Employee no worse off	<u>Below UEL</u>	<u>Below UEL</u>	<u>Below UEL</u>
	Gross salary = £1364 IT = -£341 MIR = £300 NIC = -£123 <u>£1200</u>	Gross salary = £1364 Employer NIC = £143 Reduction in CT = -£107 <u>£1400</u>	IT net of MIR = £41 NIC = £266 CT = -£107 <u>£200</u>
	<u>Above UEL</u>	<u>Above UEL</u>	<u>Above UEL</u>
	Gross salary = £1200 IT = -£300 MIR = £300 <u>£1200</u>	Gross salary = £1200 Employer NIC = £125 Reduction in CT = -£44 <u>£1281</u>	IT net of MIR = 0 NIC = £125 CT = -£44 <u>£81</u>
b) Employer no worse off	<u>Below UEL</u>	<u>Below UEL</u>	<u>Below UEL</u>
	Gross salary = £1086 IT = -£272 MIR = £300 NIC = -£98 <u>£1016</u>	Gross salary = £1086 Employer NIC = £114 Reduction in CT = 0 <u>£1200</u>	IT net of MIR = -£28 NIC = £212 <u>£184</u>
	<u>Above UEL</u>	<u>Above UEL</u>	<u>Above UEL</u>
	Gross salary = £1086 IT = -£272 MIR = £300 <u>£1114</u>	Gross salary = £1086 Employer NIC = £114 Reduction in CT = 0 <u>£1200</u>	IT net of MIR = -£28 NIC = £114 <u>£86</u>

Note: With cashing out, it is assumed that employee continues with the same size loan, at the market interest rate of 10%.



Inland Revenue

The Board Room
Somerset House
London WC2R 1LB

COPY NO. 2 OF 37.

FROM: T J PAINTER

DATE: 11 February 1988

CHANCELLOR OF THE EXCHEQUER

TAX RELIEF FOR THE PRIVATE RENTED SECTOR

The attached papers which have been agreed by FP, make a guess at the range of costs of the proposed new BES relief and give a costing for extending trading status to residential landlords. Again there has to be a lot of judgement and guess work - particularly as regards the scope for sideways relief for losses.

cc Principal Private Secretary

Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Anson
Sir A Wilson
Mr Byatt
Mr Scholar
Mr Culpin
Mr Sedgwick
Mr Odling-Smee
Miss Sinclair
Mr Instone
Mr Riley
Miss C Evans
Mr A Hudson
Mr Cropper
Mr Tyrie
Mr Call
Mr Jenkins (OPC)
Mr Unwin (Customs)
Mr Knox (Customs)

Chairman

Mr Isaac
Mr Painter
Mr McGivern
Mr Beighton
Mr Calder
Mr Deacon
Mr Elliott
Mr Reed
PS/IR

2. These are the figures which form the basis of what appears in this week's scorecard.

3. The estimate in the paper of the cost of a half-BES scheme nationwide (£m10 to £m15 a year from 1989/90) is small. When the BES proposal was mooted my own guess was that it could prove a good deal more attractive than mainstream BES and generate a significant cost in its own right as well as eroding mainstream BES.

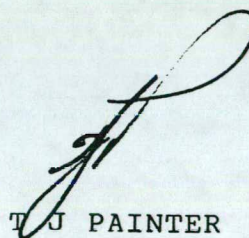
4. This is clearly very much a matter of judgement and, not surprisingly, there is more than one judgement in the Revenue. I have no grounds for substituting different figures for those in the paper but perhaps I should record that I see a number of factors which could, in combination, push the cost - and success - of the scheme up rather than down:

- it must be axiomatic that the scheme will be heavily, and effectively, marketed by Government (the DOE and those responsible for coordinating the inner-cities initiative, with Revenue support);
- prima facie it is easier to promote than existing BES: a single and familiar product; no built-in tension as with BES the father between the need on the Government side to highlight its high-risk nature so as to justify the scheme and the pressure on promoters to talk up the security of their investments; and, tentatively,
- although effectively much BES investment has had the security of asset backing there is a more secure ring to bricks and mortar in the form of houses than to say fine wines, ship hulls, or even secured contracting; if so,

- the new scheme might appeal to a wider range of investors than present BES (there will still be over a million higher rate taxpayers post-Budget) whereas a crucial assumption in the note is that the pool of potential investors is unlikely to expand as a result of the new relief.

5. Clearly I am not qualified to comment on the weight to be attached to the political risk potential investors will perceive beyond noting that I would expect DOE officials to have talked it up rather than down for understandable tactical reasons in the Cassell Working Group and that events could make it much clearer, for better or worse, quite early in the life of the scheme.

6. Full relief for the inner cities pushes up the estimate of cost in the paper substantially - perhaps to £50 million. This underlines the likely sensitivity of take-up to the rate at which relief is given. It would of course be easier to vary the terms of a relatively free-standing BES scheme in the light of experience than the various structural changes to the tax system considered by Mr Cassell's group. Indeed, you could take regulation-making powers to vary the rate of relief in-year.



T. J. PAINTER

BUDGET SECRET: TASK FORCE LIST

BES: LIKELY TAKE UP AND COST OF NEW SCHEME

We have very little to go on in costing the proposed new BES relief. The crucial question is how attractive the relief will prove and, therefore, what will be the take-up. Neither we nor DOE are able to answer this question with any confidence. But set out below are possible costings on the basis of some very tentative assumptions.

BES: Background

2. The total annual amount raised through BES since its introduction in 1983 has been roughly:

1983-84	£105 million
1984-85	£150 million
1985-86	£160 million (estimate)
1986-87	£160 million (estimate)

3. BES is a relief aimed at high risk investment but in practice BES investors have sought relatively safe investments. Initially property development offered such an investment, but this was excluded from BES in 1985. Land-backed schemes and investment in wine and antiques also offered a high degree of security, but the 1986 Budget closed off these avenues. Latest evidence suggest that secured contracting has become a (relatively) safe haven. Also of note is the growing trend toward large public issues - 56% of total investment put in to issues of over £1 million in 1985-86 compared with 44% in 1984-85. The average prospectus issue in 1986-87 was £2.5 million, compared with £1.6 million in 1985-86.

4. The above suggests that investors, given a choice, will tend to choose the safest investments; and despite the restrictions imposed in 1985 and again in 1986, investors have managed to find new relatively safe havens. Many current BES investments are promoted as being relatively safe and asset-backed (for example, about 70 per cent of the

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amount sought through public offers so far in 1987-88 is for secured contracting, hotels, pubs, restaurants and shops - all in amounts of over £1 million).

5. We do not have statistics which show how many individuals make a BES investment each year. We carried out an exercise for the first year of BES (1983-84) which indicated that between 15,000 and 20,000 individuals invested in BES. It seems likely that the number of investors now would not be very different and would anyway still be small in relation to the total number of higher rate taxpayers (over 1 million). The average marginal tax rate (and therefore the rate of relief) is about 50 per cent.

Implications of Budget Package for BES

6. The Budget proposals with the most significant potential impact on BES are

- the proposed reduction in the higher rates of income tax;
- the proposed ceiling on BES relief for total annual investment in any one company (front runners here are £1 million, £500,000 or £250,000); this ceiling will not apply to companies investing in housing for rent (it is an open question whether there should be a higher ceiling or no ceiling for these);
- (less directly) the proposed change in the tax treatment of forestry - currently an important shelter.

7. The reduction in the highest rate of income tax to 40% will diminish the attractiveness of BES. It will reduce the post-tax rate of return to a top rate taxpayer. Some investors will almost certainly be discouraged.

8. The introduction of the ceiling on the amount of investment in any one company could have a large effect on the level of BES investment (depending on the amount of the ceiling). Public issues would be hit hard, and with a low ceiling, might virtually disappear. Some of the potential investment would no doubt go into BES funds or direct, local investment, but some would almost certainly not.

9. The impact of the changed regime for forestry will be more marginal. But by reducing the scope for sheltering income via this route, the Government will be enhancing the relative attractiveness of BES, despite reducing absolute returns. However, the effect is not likely to be great and cannot be quantified.

Proposed "Half-BES" for Renting

10. The level of BES investment in private renting will depend on the post-tax returns available and the perceived risk which will determine its attractiveness relative to other forms of investment. BES companies specialising in providing rented housing are unlikely to be seen as significantly safer than existing asset-backed BES investment (particularly given the political risk) and, with only half relief, the average rate of relief for investment in these companies will be only 20%. We think that BES schemes for private renting are therefore unlikely to attract those higher rate (or basic rate) taxpayers who currently regard BES investment as unacceptably risky. Furthermore, we do not expect the new relief to attract many people who currently make conventional BES investments but will be discouraged from doing so by the lower income tax rates.

11. This is a crucial assumption - we are saying that the pool of potential BES investors is unlikely to expand as a result of the new (half) relief for private renting. This is simply a judgment based on past experience of BES and our assessment of the relative attractiveness of investment in

BUDGET SECRET: TASK FORCE LIST

private renting. If the assumption proves wrong our costings will be too low.

12. The imposition of a ceiling on BES investment for each company will alter the relative risk and return on BES investments. Some investors who, but for the ceiling, would have chosen BES may be diverted into the new relief for private renting.

13. It is difficult to calculate the combined effect of the various influences. But, assuming half relief and no ceiling for investment in private renting, the following figures seem unlikely to prove too low:

	<u>Investment</u> <u>Existing BES</u>	<u>Private</u> <u>Renting</u>	<u>Total</u>	<u>Tax Cost</u>
i. Current regime	160	0	160	80
ii. New regime with no ceiling	120	10	130	50
iii. New regime with £1m ceiling	80	50	130	40
iv. New regime with £0.25m ceiling	40	70	110	30

14. These figures make some highly tentative assumptions, which are little more than guesses.

- a. First, they assume that the effect of the income tax changes will be a fall in conventional BES investment of £40 million to £120 million (row (ii) of the table), partly offset by £10 million investment in private renting. This assumption reflects the large amount of BES investment currently made by 60 per cent taxpayers (£130 million). It also assumes that conventional BES

BUDGET SECRET: TASK FORCE LIST

investment without a ceiling will be more attractive than investment in private renting (with only half relief).

- b. Second, they assume that a £1 million ceiling for conventional BES investment (but a high ceiling or no ceiling for investment in private renting) will reduce considerably the amount going into conventional public offers (currently about £115 million a year) but do little to discourage BES funds (currently raising about £30 million a year) or other BES investments (making up the balance of the £160 million a year BES investment). Comparing row (iii) and row (ii), the assumption is that all the conventional investment which is discouraged in this way goes into investment in private renting (this may be an over-estimate).
- c. Third, they assume that a £0.25 million ceiling would virtually eliminate conventional public offers and also adversely affect BES funds. Only part of the conventional investment which is discouraged by this low ceiling is assumed to go into investment in private renting (with half-rate relief).

15. On this basis the continuing tax cost of the new relief might be £10-£15 million a year - representing an investment of £50m to £70m a year. (At a cost of £40,000 per house, this would result in a further 1,200 to 1,700 dwellings per year - more if the companies also raised capital by borrowing.)

16. The DOE have approached the question from a completely different angle. Their view of potential take-up is based on the number of houses which may come into the rented market at a given rate of return. This in turn is based on their experience (which they admit is limited) of the returns available in the housing sector generally.

17. Using the assumptions in the joint working group's report of November last year, they have made adjustments to take account of the restriction to half BES, but not the reduction in the highest rates of income tax to 40 per cent. The rate of return varies according to the company's gearing, but is estimated to be of the order of 8.6 per cent for a 50 per cent taxpayer, (7.5 per cent to a 40 per cent taxpayer).

18. At a rate of return of 8.6 per cent, DOE believe that there could be additional investment in rented housing of £200 million in the first year, and £400 million thereafter. This would produce 5,000 dwellings in the first year and 10,000 in each subsequent year at an average price of £40,000 per dwelling. The resulting tax cost depends on the amount of borrowing assumed, but the first year tax cost would be of the order of £25-£40 million, with the second and subsequent year cost rising to £45-£80 million.

19. The DOE approach is quite as subjective as the assumptions underlying our costings; and it takes no account of the past take-up of BES, nor the (relatively) safe nature of most existing BES investments. Moreover, DOE are not aware that the value of BES relief will be reduced by income tax reductions in the Budget.

Possible Full Relief for Investment in rented housing in Inner Cities

18. The possibility of giving full BES relief for investment in private rented housing in inner cities has also been raised. On the working group's assumptions, the rate of return on such investment could be of the order of 13% as compared with 7.5% with half BES relief. This pushes up the attractiveness of investment in private renting relative to existing BES investments, and it is likely that more BES investors, or even some people currently not willing to invest in BES, might invest in private renting at these levels of return. We have no way of quantifying this

effect. But, it seems unlikely that investment in rented housing would exceed the levels achieved by BES in recent years when relief was available at 60 per cent and many of the investments were promoted as asset-backed. If, for example, £125 million were raised under the new scheme (and assuming full relief at 40%), the cost would be £50 million a year. This would represent about 3,000 to 5,000 dwellings per year, depending on the level of gearing.

CONCLUSION ON BES COSTS

19. On the basis of the above analysis, we would estimate the potential cost of the proposed half-BES scheme to be of the order of £10-£15 million (but with full BES relief for investment in inner cities the cost would be up to £50 million). This is lower than DOE's estimate: they put the annual cost at around £45-£80 million. But as explained, their basis for costing is no more certain than the Revenue/Treasury approach: and in the past DOE estimates of the take-up of the assured tenancy schemes have proved on the optimistic side. We cannot, however, be certain that the actual cost would not prove to be as high as the DOE suggests; or indeed, that the actual cost would not prove to be lower or higher than both of our ranges.

COST OF TRADING RELIEFS FOR RESIDENTIAL LANDLORDS

1. Our best estimate of the incidence of this cost is as follows:-

1988/89	1989/90	1990/91
-£m100	-£m55	-£m80 (continuing broadly at that level for subsequent years)

2. These figures assume that the population of landlords stays broadly as now (ie large numbers of new landlords are not brought forward by this relief). Trading treatment affects liability to different taxes - income tax, CT and CGT. This is discussed below.

3. Broad stability in the landlord population is consistent with the DoE view that this package of trading reliefs is essentially designed to reduce the flow of landlords out of the private rented sector (which they say is contracting at a rate of some 80,000 dwellings a year), rather than bringing in a large number of new landlords. But they cannot help us on the costings or in quantifying the impact of the relief in stemming this decline.

4. There are some elements of the package that in certain circumstances might encourage some landlords to remain in the private rented sector. For example, the CGT roll-over provision could enable a landlord to sell a "controlled" dwelling and plough the proceeds back into another property for letting at deregulated rents. But we cannot quantify this effect.

5. The only figure we have ourselves which might be of some help in answering this question, is that over the last 10 years the numbers of landlords (residential and others) on our books has declined by some 27%. So if these reliefs were successful in stopping the decline, it might be the case that, over a period of ten years, some 27% of the £80 million would not be deadweight.

6. The figure of £100 million for 1988/89 in paragraph 1 relates only to income tax (the lag between accrual of tax and payment means that there is no effect on receipts in the first year for either corporation tax or capital gains tax). The size of the figure is largely accounted for by the fact that giving trading treatment with effect from 1988/89 would mean that tax on rental income would become payable in two instalments so that half the tax payable for that year would not become due until 1 July 1989 (under present rules it would all be due on 1 January 1989).

7. The continuing cost of £80 million divides up as shown in the following paragraphs.

8. Income tax £30 million. This represents some £23 million for those components of a trading package for which the tax system provides us with some centrally held information ie

- changing to the preceding year basis of assessment;
- availability of retirement annuity relief; and
- availability of wife's earned income relief.

9. We have then rounded the figure (£23 million) up to £30 million to take account in a very broad way of those parts of the package for which no information is available (either centrally or, on some matters, even in local offices) eg

- sideways loss relief and interest relief;
- capital allowances on furniture and fittings.

10. We have no way of knowing whether this rounding adjustment is likely to be too high or too low, but it does not seem a wholly implausible figure. On relief for losses, for example, deregulated (ie market) rents should normally enable landlords to provide for repairs and operate at a profit, taking one year with another. Except perhaps in cases of high borrowing costs one would not expect significant excess expenditure in most years for relief sideways as losses. Landlords of controlled tenancies

should normally also operate at a profit, but here we would expect there to be some losses in years in which a larger amount of expenditure (out of low rents) has to be incurred on, in effect, deferred repairs. We have no information to help us to cost these cases.

11. Corporation tax £20 million. Here we have assumed that the corporation tax yield on this sort of income would be reduced by the same proportion as with income tax. Some of the trading reliefs will not be relevant to companies (eg retirement annuity relief) but against this we would expect larger capital allowances claims by companies and the estimated cost is not, we think, unreasonable.

12. Capital gains tax £30 million. This relates to roll-over relief and retirement annuity relief. The cost of giving these reliefs to landlords of furnished residential property was put at £10 million in 1985. The income tax yield on furnished lettings is roughly one third of the total income tax yield on all lettings; so we have increased the £10 million by a factor of 3.

~~PPH~~
RENTING (1)

M. Hay x 4918

APP Gen line

1. If we are to reduce V further, have to ensure people can move to where the jobs are.
 2. One obstacle at the moment: shortage of priv. rented accommodation.
- B. Already introduced leg'n in Hog Bill. Tax changes to allow complete the picture.

What is current proposal? BES and assured tenancies.

Attractions of BES

- front end loaded, immediate effect, behave drug'n in time will bring existing relief, understood etc. for the new housing.

Features of BES

- restricted to companies specialising in residential lets
- "half-BES" vs Full BES wd be v. generous
- restricted to new-style assured tenancies?
- time-limited

Discharge of patients criticised

By Peter Hildrew, Social Services Correspondent

Hospitals are criticised in the latest report of the health service ombudsman for discharging patients without taking their home circumstances into account.

In one case in the report by Mr Anthony Barrowclough, published yesterday, an elderly woman was taken home by ambulance after midnight when the registrar on duty decided that she did not need admission. She had been referred by her GP who thought she might need surgical treatment, and had been at the hospital since 5pm. An ambulance ordered at

10.38pm to take her home did not arrive until 12.14am.

The ombudsman found "no evidence that, despite the lateness of the hour, active consideration had been given to her admission for social reasons", although the hospital had a written policy to that effect.

In another case, "totally inadequate notice" was given that an elderly woman was being discharged. Her daughter received a phone call at work to say the ambulance was already taking her mother home, but she could not get there in time, and the crew had to take her back to hospital.

The mother was in a

distressed state when she finally got home, and was readmitted to hospital three days later.

The ombudsman found that the consultant had taken a clinical decision to discharge her "on the incorrect assumption that proper arrangements have been made for the woman's care at home". Nursing staff, the report says, should have told either the consultant or their nurse managers of their concern that the woman was not fit to be discharged.

Third Report of the Health Service Commissioner, Session 1987-88. HC 232, HMSO, £12.30.

Report suppressed, MP says

By Colin Brown
Political Correspondent

port in *The Independent* and expressed concern during the Bill's committee stage in the Commons about the powers for the Secretary of State to direct health authorities on ways of raising new forms of income.

Tony Newton, the Health Minister, said he envisaged the powers in the Bill would be used not to force hospitals to try new fund raising services, but to stop them making profits from services which were "inappropriate". He said this would apply to hospitals which wished to open direct lines to funeral directors. Mr Newton

HEALTH MINISTERS were accused last night of suppressing the annual report by the General Practitioners Finance Corporation because it criticised the Government's proposal to privatise it with the Health and Medicines Bill.

Harriet Harman, the Labour spokeswoman on health, told *The Independent* the report of the GPFC, which provides loans at below market rates for GPs to improve their surgeries, had been received by the Government last June and should have been published in July.

The Bill also enables hospitals to make a profit on their services for the first time. Ms Harman raised a leaked Government re-

also insisted the Government had demonstrated its commitment to the NHS by investing more money in new hospital buildings. He said it was hoped the Bill would enable them to raise £10-20m this year, but this could rise to £100m after three years.

In a separate attack, the Government was accused of "turning off the tap" on nurse training, which had led to delays in heart operations for children in the Midlands. Barry Sheerman, the Labour MP for Huddersfield, was told in a written answer that spending on nurse training fell from £498m in 1977-8 to £439m this year. "It is a deliberate policy by the Government to cut down on training," he said.

THE INDEPENDENT

Biffen demands £2.6bn package for NHS

By John Pienaar

JOHN BIFFEN, the former Tory Leader of the Commons, last night outstripped Labour demands for higher health spending with a call for extra NHS cash equal to tax cuts of between 1p and 2p.

Aid in the Chancellor's March Budget — equivalent to a package worth between £1.3bn and £2.6bn — was "absolutely essential for the short-term relief of the situation that now exists in the health service", he told the Commons.

Intervening in a debate on the Chancellor's autumn economic statement, Mr Biffen rejected the notion that the NHS or social services were "an overhead or an incubus on the national economy".

"It is a national partnership for an economy based on social market principles which have sustained this economy and this party so well."

Mr Biffen bluntly told his former ministerial colleagues: "There is no way that the public of this country will be convinced that bed closures, ward closures, hospital closures are consistent with an adequate

health service, even if numbers of operations are at record levels." There was no alternative "in the short term" but to further enhance NHS spending if there was to eventually be a political initiative on wider funding reforms.

"I hope at least the equivalent sum of between 1p and 2p in a change on the direct rate will be available for the health service — I believe that is the kind of sum necessary to restore an initiative in this situation."

The demand outstrips that recently delivered by Neil Kinnock, who called for £1.3bn in immediate extra support, the equivalent of a 1p reduction.

But Mr Biffen made clear his support for a general rethink of NHS funding in the longer term.

In particular, he questioned whether the increase in personal disposable income would clear the way for a look at "state

medical insurance as opposed to direct treasury funding". Restraint on the potentially massive financial demands of health care also had to be considered. "There is no way we can accept that the untrammelled operation of the NHS gives rise to intolerable expenditure."

Earlier, John Smith, the Shadow Chancellor said a significant shift in public spending was needed to boost the economy and welfare services.

Tax cuts would simply translate into extra consumer spending in the prosperous areas and overheated sections of the economy. Prudent and well directed increases in spending would improve services and tackle the looming problems of Britain's balance of payments.

"I hope that the Chancellor will heed the advice given him by his own advisers that to proceed with tax cuts would be highly irresponsible."

In a confident opening speech, however, Nigel Lawson the Chancellor of the Exchequer said the British economy was "well

placed to continue the excellent progress of recent years, in spite of the problems faced by other countries and the turbulence in the financial markets."

And he also dangled the prospects of tax cuts, by scornfully recalling the election campaign warnings of major increases in taxation by Roy Hattersley, Labour's economic spokesman.

"Whether he was right or wrong about taxation remains to be seen: but he will only have to wait another two months now, until March 15, for the massive increase in taxation he so confidently predicted, if indeed there is one."

As the state of the health service dominated another stormy question time session, Mrs Thatcher said the Government was seeking to increase the use of military hospital beds to cut treatment waiting lists.

"Health authorities are being encouraged to consider every possibility — including military hospitals — when putting in their bids for allocations from the waiting list fund."

RENTING (2)

Questions

1. What sort of hag are we trying to bring forth? Family hag?
2. ~~Assured tenancies where are we?~~

Assured tenancies

(Hag 26 Jan)

1. Specific problem.
2. WDAs available for certain properties let under assured tenancies scheme.
3. Hag Bill converting old-style ATs to new-style, so properties currently getting relief wd cease to, & cd be clawed back.
4. Hag's to avoid this.

new build or substantial renovation

1. After new supply, at reasonable rents (not Mayfair? linked to NS assured tenancy rules).
2. Dereg'n will bring this forth.
3. Case for bid start.
4. - decided to extend BES.
5. Estab'd relief, well understood.
6. Right characteristics - front-end loaded.

THE GUARDIAN

Biffen urges £2.6bn injection into NHS 6

HEALTH CASH

By Alan Travis.

The former Leader of the Commons, Mr John Biffen yesterday called for a short term injection of up to £2.6 billion into the National Health Service to give the Government the credibility to conduct long term reforms of its financing.

During a Commons debate on the Autumn Statement Mr Biffen looked forward to the Budget which will be on March 15 and argued that an amount of money equivalent to between one and two pence off the basic rate of income tax should be made available for the NHS.

"There is no way that the public of this country would be convinced that bed closures, ward closures and hospital closures are consistent with an adequate health service even if the number of operations are at a record level, even if the amount of expenditure is at a record level. There is no alternative but a further enhancement of spending," said Mr Biffen.

The call from Mr Biffen went further than the injection demanded by the Shadow Chancellor, Mr John Smith, during the debate. He repeated Labour demands for an extra £1.3 billion spending on the NHS.

The Chancellor, Mr Nigel Lawson, when he opened the debate left questions of public spending to the Chief Secretary to the Treasury, Mr John Major, who wound up.

Mr Lawson preferred to concentrate on arguing for a more managed approach to international co-operation on exchange rates to prevent the wild gyrations of recent years.

Mr Biffen cast his speech in terms of the current debate within Government over the future financing of the NHS. The injection of up to £2.6 billion was "absolutely essential for the short term relief of the situation in the health service and if we are to have the political initiative to conduct the other reforms that are essential then there has to be a clear consideration of extra monies."

Mr Biffen said whatever sum was chosen was bound to be related to the total sum available for tax cuts in the Budget



John Biffen:
"Will give credibility"

— reported to be around £3 billion.

"I hope that between one pence and two pence of the change in the tax rate being contemplated would be available for the health service," said Mr Biffen. "That is the kind of change needed."

He argued that the health service was not some overhead on top of the productive economy but a matter of partnership for an economy based on the social market principle.

The 40th anniversary of the NHS should not be an occasion for a memorial service but for a real consideration of the factors that affect the whole funding of the NHS.

He suggested there should be a wide-ranging debate on these factors which looked at the balance between state medical insurance and the direct Treasury funding in the light of the rise in personal disposable incomes; the changes in the age structure of the nation and in medical technology. It should examine the role of charges and take into account the growth of private medical insurance schemes.

Such a debate should lead to a discussion document and

changes but they had to precede the institutional changes being advocated by some Conservative MPs. There was no way the Government could escape the fact that the untrammelled expansion of the NHS would give rise to an intolerable level of spending.

Mr Smith agreed that enormous amounts of money could not be spent on the NHS but "we know that significantly more than the present Government spends needs to be spent."

So far ministers had only pledged to spend a further £100 million over and above the £700 million pledged in the Autumn Statement. "They have moved but it is nowhere near enough," said Mr Smith.

The Chancellor should heed the advice of his own advisers, namely Sir Terry Burns, that pursuing tax cuts once again in the March budget would be irresponsible. "Tax cuts would feed through to increased consumer expenditure, especially in the more prosperous areas, increasing the overheating in the economy and giving an extra twist to the balance of trade manufacturing deficit," warned Mr Smith.

But Mr Lawson was not in the mood to talk about public expenditure. Instead he took a tour d'horizon of the world economy. He argued that it was not public spending which created a successful economy but the performance of businesses and it had led to an upswing of unprecedented length, strength and steadiness.

The stock market crash was characterised by the Chancellor as a "correction" following the rapid rise of 1987 and the world economy was in fact markedly stronger before the crash than had previously been recognised.

"So any slowdown there may be this year will be from a pretty vigorous momentum of growth," said Mr Lawson.

He suggested that the G7 group, the world's biggest industrial countries, should build upon their agreement to cooperate to foster exchange rate stability.

A visible, measurable, objective of broad exchange rate stability within a framework of low inflation would provide clear advantages in preventing wild gyrations.



COPY NO. 8 OF 9 .

FROM: J M G TAYLOR

DATE: 11 February 1988

MR CROPPER

cc PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary
Mr Tyrie
Mr Call

PAYROLL GIVING

The Chancellor has seen your minute of 10 February.

2. He has commented that £20 a month is a round number. However, he attaches great importance to the advertising tie-in, and we must prepare for this without delay, making sure that the proprieties, of course, are observed.

A handwritten signature in black ink, appearing to be 'J M T'.

J M T TAYLOR



Inland Revenue

Policy Division
Somerset House

FROM: ANGELA RHODES
DATE: 11 FEBRUARY 1988

CHANCELLOR

CAR BENEFIT SCALES 1988/89: IMPLEMENTATION

1. At the Overview meeting on 8 February you said that the increases in the car benefit scales for 1988/89 should be included in the Finance Bill and the changes implemented as part of the Budget recoding exercise. This note looks at the options. As the Overview minutes record, any changes made once the recoding exercise is in progress put the implementation timetable for the whole package at risk.

The Budget Recoding Strategy

2. The present target is to bring in the revised PAYE codes in June. The date will be in the PCTA resolutions covering the rates and allowances changes. To achieve this the Budget recoding strategy requires

- an initial coding review to be carried out on 10/11 April. At this stage all the codes that need to be amended manually will be identified by computer and printed out for tax office attention
- 12 April - 13 May. All codes requiring manual revision will be reviewed and the computer record updated
- 14/15 May - the codes to be revised by computer will be amended; revised codes will be issued to employers and employees.
- mid June - implementation of new rates and allowances by employers. My note of 5 February explained that

Rhodes
CH &
BENEFIT
SCALE
11/2

employers require a long lead-in time this year because of the much larger number of code changes they will have to make on instruction from the Revenue (3 times as many as usual). PAYE codes not updated by the Revenue have to be updated by the employer who must ensure that all changes are made by the time the revised tax tables are operated

- end June - a sweep up review to "mop up" codes which have come up for revision (eg because the taxpayers circumstances have changed) since May.

3. There are two important points to note:

- WS- W
- (a) If this strategy is to be achieved decisions on what the changes are to be (in this case the increases in the car scales) are needed by 26 February (this is to allow time for the necessary computer programs to be written and tested before the initial coding review takes place in early April).
 - (b) If any of the decisions are changed once the coding review has begun the whole package is put in jeopardy. This is because once the process is in operation, any changes would mean we would have to unscramble the package probably delaying implementation.

4. Legislating to change the 1988/89 car scales and including them in the Budget recoding exercise runs up against much the same operational problems as making the changes by statutory instrument if the proposals are subsequently amended. There are additional - mainly legal - problems with the statutory route if the changes have been introduced under cover of a PCTA resolution.

PCTA Resolution

5. Parliamentary Counsel has confirmed that revised car scales could be introduced under the provisions of the Provisional Collection of Taxes Act. One of the requirements of that Act however is that the precise terms of a PCTA resolution must be reflected in legislation. If the provisions giving effect to the resolution are rejected during their passage through the House the resolution lapses and any tax deducted on the strength of it must be repaid. The distinction between the amendment of a provision and its rejection is not clear. However we understand that where for example a proposal is amended to substitute an increase lower than originally proposed (eg a 50% increase in place of a 100% increase) this amounts to a rejection of the difference between the amended and original proposals. The likely result is that the resolution lapses to the extent of the difference. Parliamentary Counsel has advised therefore that use of the PCTA procedure should be avoided where the provisions concerned are controversial or complicated (or both) because of the uncertain effects of subsequent amendments.

*Important !!!
(4/1984
As per
Kp return)*

The Options

6. The choice is between the PCTA route with a Budget recode (despite the risks) or introducing the new 1988/89 scales without PCTA cover leaving the coding changes until after Royal Assent.

The PCTA Route

7. The operational implications depend on whether the proposals are changed and if so when. There are a number of possibilities.

(a) No change

8. If the car scale changes are introduced by PCTA

resolution and passed without amendment there are no problems. There is no effect on the Budget recoding programme and the present timetable should be met.

(b) Proposals amended/rejected in Committee

*How these
sub-
steps*

9. If the PCTA route is used and the proposals are amended there are legal and operational problems. The major problem we would face is that all codes including car benefit would be wrong and it would very much depend on when the changes were made how we would deal with this.

10. If the proposals were amended before the new codes were issued (ie before 14 May) we should have to suspend the whole Budget recoding exercise - we could not tell employers to operate codes we know to be wrong - until we had unscrambled the codes. This would delay implementation of the whole Budget package and might require a new PCTA Resolution.

11. If the proposals were amended after the codes had been issued but before they were operated (effectively, if they were changed in Standing Committee or later) the problems would intensify. Clearly, disentangling the codes containing car benefit will take time. Some instruction to employers would be necessary and the choice would essentially be between asking them to

- revert to the pre-Budget codes until further notice. This effectively means three recoding jobs for employers
- continue to use the revised Budget codes until further notice. This means less work for employers but would be strictly wrong in law. Ministers and the Revenue could be open to criticism (in what would be likely to be a highly charged political atmosphere) for disregarding the expressed wish of Parliament and imposing unnecessarily high tax deductions in the

interim. It would also be open to those aggrieved by the Budget increases to require the code to be amended. The Revenue could not lawfully refuse to do this; but tax offices would face unmanageable problems if in unscrambling an already messy situation they had to cope with large numbers of individual appeals at the same time as they were preparing a general recode.

In the meantime, we should have to amend all codes containing car benefit to incorporate whatever revised car scales Parliament felt able to approve.

12. This is clearly an unattractive scenario. It involves the possibility of operating some codes that are not strictly legal, or the complication that we would be reliant on employers understanding and acting on revised instructions very quickly or (possibly) both. Almost inevitably this could go badly wrong.

13. We have therefore been exploring a third course of action. This also would involve coupling the PCTA route and the Budget recoding exercise. However if the car scales resolution is lost (or looks in danger of being lost) an amended PCTA resolution* would be introduced which would authorise the scales announced in the Budget to run until an appointed day (probably in September) when codes in line with revised proposals could be introduced. There is some precedent for this in the PAYE resolutions which set the date on which Budget changes are to be implemented. We are discussing this with Parliamentary Counsel and our legal advisers. There are detailed matters to sort out - for example PCTA resolutions fall at Royal Assent - but this route does not look impossible.

*As noted an amended PCTA resolution may be necessary in any event, if implementation of the Budget package has to be deferred beyond the date set in the original PCTA resolution.

Non-PCTA

14. The alternative is not to use PCTA. This would mean that although the changes in the Bill would take effect from 6 April, they would not be implemented until after Royal Assent. The Budget recode would not include car scales and could be implemented (assuming no changes in other areas) on time in June. But it results in an unusual pattern of an increased code plus refund closely followed by a decreased code (and higher deductions) for 1988/89 followed again by a further reduced code to collect an underpayment in 1989/90. In effect the car scale changes (which would mean significant reductions in codes) would not take effect until some time after the people concerned had received their refunds. As their codes would be reduced they would be operated on a non-cumulative basis and those affected (there are roughly one and a quarter million of them) would be faced with both higher deductions of tax for the remainder of 1988/89 and an underpayment to be collected in 1989/90. This is, of course very unattractive to taxpayers employers and the Exchequer - only around half the extra tax would be collected in year.

Operational Consequences

15. If the PCTA route is followed without amendment there are no operational consequences. If a PCTA resolution is amended or if the PCTA route is not used certain of the operational consequences are broadly similar:

- Two coding exercises would be necessary. The second, for car scales could not be started until the Budget recode had been completed - ie until July at the earliest, so it could not be implemented until August/September at the earliest.
- Recoding for cars is quite a big job involving up to 1.3 million cases. Most could be done automatically

though some would have to be done manually. There would therefore be extra costs - resources, postage etc.

- There are employers to consider. The Budget recode will be a big exercise for them too. A second large exercise within two or three months to cater for car scales would inevitably be extremely unpopular.

16. The PCTA route with amendments has additional disadvantages

- the original recode has to be unscrambled and implementation of the Budget package delayed accordingly
- unless an amended PCTA resolution is used for a period some codes would not have legal backing. It would be open to taxpayers to require them to be amended.

Conclusion

✓ 17. It would be possible to alter the 1988/89 car scales by means of a PCTA Resolution. There are difficulties if the original proposals have to be amended. These do not appear insurmountable but the main risks are

- the whole Budget package may have to be unscrambled and implementation delayed
- some PAYE codes may not be strictly within the law for some time if the amended PCTA device is not viable
- employers could be faced with two large recoding exercises in a short time.

18. If you decide to go for PCTA route and you think there is a chance of amendment the least damaging option may be to take

WML
Case 5-6
M 1/11/73

the clause in Committee of the Whole House. That way if changes are to be made the Budget recode operation could be suspended until the car cases have been taken out and put right.

19. We will continue to explore the amended PCTA route in case it does not prove possible or you do not wish to take this legislation on the floor of the House.

AR

A M RHODES



Inland Revenue

The Board Room
Somerset House
London WC2R 1LB

Red handwritten note:
Re x, what was felt 1985
and a few lines?

Red stamp:
PAINTER
CHECK
11/2

COPY NO. 1 OF 37

FROM: T J PAINTER

DATE: 11 February 1988

CHANCELLOR OF THE EXCHEQUER

TAX RELIEF FOR THE PRIVATE RENTED SECTOR

The attached papers which have been agreed by FP, make a guess at the range of costs of the proposed new BES relief and give a costing for extending trading status to residential landlords. Again there has to be a lot of judgement and guess work - particularly as regards the scope for sideways relief for losses.

- cc Principal Private Secretary
- Chief Secretary
- Financial Secretary
- Paymaster General
- Economic Secretary
- Sir P Middleton
- Sir T Burns
- Sir G Littler
- Mr Anson
- Sir A Wilson
- Mr Byatt
- Mr Scholar
- Mr Culpin
- Mr Sedgwick
- Mr Odling-Smee
- Miss Sinclair
- Mr Instone
- Mr Riley
- Miss C Evans
- Mr A Hudson
- Mr Cropper
- Mr Tyrie
- Mr Call
- Mr Jenkins (OPC)
- Mr Unwin (Customs)
- Mr Knox (Customs)

- Chairman
- Mr Isaac
- Mr Painter
- Mr McGivern
- Mr Beighton
- Mr Calder
- Mr Deacon
- Mr Elliott
- Mr Reed
- PS/IR

2. These are the figures which form the basis of what appears in this week's scorecard.

3. The estimate in the paper of the cost of a half-BES scheme nationwide (£m10 to £m15 a year from 1989/90) is small. When the BES proposal was mooted my own guess was that it could prove a good deal more attractive than mainstream BES and generate a significant cost in its own right as well as eroding mainstream BES. X

4. This is clearly very much a matter of judgement and, not surprisingly, there is more than one judgement in the Revenue. I have no grounds for substituting different figures for those in the paper but perhaps I should record that I see a number of factors which could, in combination, push the cost - and success - of the scheme up rather than down:

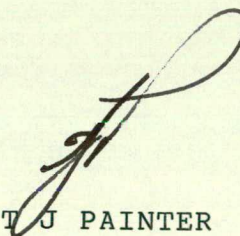
- it must be axiomatic that the scheme will be heavily, and effectively, marketed by Government (the DOE and those responsible for coordinating the inner-cities initiative, with Revenue support);
- prima facie it is easier to promote than existing BES: a single and familiar product; no built-in tension, as with BES the father, between the need on the Government side to highlight its high-risk nature so as to justify the scheme and the pressure on promoters to talk up the security of their investments; and, tentatively,
- although effectively much BES investment has had the security of asset backing there is a more secure ring to bricks and mortar in the form of houses than to say fine wines, ship hulls, or even secured contracting; if so,

We'll have BES the Holy Ghost next!

- the new scheme might appeal to a wider range of investors than present BES (there will still be over a million higher rate taxpayers post-Budget) whereas a crucial assumption in the note is that the pool of potential investors is unlikely to expand as a result of the new relief.

5. Clearly I am not qualified to comment on the weight to be attached to the political risk potential investors will perceive beyond noting that I would expect DOE officials to have talked it up rather than down for understandable tactical reasons in the Cassell Working Group and that events could make it much clearer, for better or worse, quite early in the life of the scheme.

6. Full relief for the inner cities pushes up the estimate of cost in the paper substantially - perhaps to £50 million. This underlines the likely sensitivity of take-up to the rate at which relief is given. It would of course be easier to vary the terms of a relatively free-standing BES scheme in the light of experience than the various structural changes to the tax system considered by Mr Cassell's group. Indeed, you could take regulation-making powers to vary the rate of relief in-year.



T J PAINTER

7 COST OF NEW SCHEME

BUDGET SECRET: TASK FORCE LIST

BES: LIKELY TAKE UP AND COST OF NEW SCHEME

We have very little to go on in costing the proposed new BES relief. The crucial question is how attractive the relief will prove and, therefore, what will be the take-up. Neither we nor DOE are able to answer this question with any confidence. But set out below are possible costings on the basis of some very tentative assumptions.

BES: Background

2. The total annual amount raised through BES since its introduction in 1983 has been roughly:

1983-84	£105 million
1984-85	£150 million
1985-86	£160 million (estimate)
1986-87	£160 million (estimate)

3. BES is a relief aimed at high risk investment but in practice BES investors have sought relatively safe investments. Initially property development offered such an investment, but this was excluded from BES in 1985. Land-backed schemes and investment in wine and antiques also offered a high degree of security, but the 1986 Budget closed off these avenues. Latest evidence suggest that secured contracting has become a (relatively) safe haven. Also of note is the growing trend toward large public issues - 56% of total investment put in to issues of over £1 million in 1985-86 compared with 44% in 1984-85. The average prospectus issue in 1986-87 was £2.5 million, compared with £1.6 million in 1985-86.

4. The above suggests that investors, given a choice, will tend to choose the safest investments; and despite the restrictions imposed in 1985 and again in 1986, investors have managed to find new relatively safe havens. Many current BES investments are promoted as being relatively safe and asset-backed (for example, about 70 per cent of the

amount sought through public offers so far in 1987-88 is for secured contracting, hotels, pubs, restaurants and shops - all in amounts of over £1 million).

5. We do not have statistics which show how many individuals make a BES investment each year. We carried out an exercise for the first year of BES (1983-84) which indicated that between 15,000 and 20,000 individuals invested in BES. It seems likely that the number of investors now would not be very different and would anyway still be small in relation to the total number of higher rate taxpayers (over 1 million). The average marginal tax rate (and therefore the rate of relief) is about 50 per cent.

Implications of Budget Package for BES

6. The Budget proposals with the most significant potential impact on BES are

- the proposed reduction in the higher rates of income tax;
- the proposed ceiling on BES relief for total annual investment in any one company (front runners here are £1 million, £500,000 or £250,000); this ceiling will not apply to companies investing in housing for rent (it is an open question whether there should be a higher ceiling or no ceiling for these);
- (less directly) the proposed change in the tax treatment of forestry - currently an important shelter.

7. The reduction in the highest rate of income tax to 40% will diminish the attractiveness of BES. It will reduce the post-tax rate of return to a top rate taxpayer. Some investors will almost certainly be discouraged.

8. The introduction of the ceiling on the amount of investment in any one company could have a large effect on the level of BES investment (depending on the amount of the ceiling). Public issues would be hit hard, and with a low ceiling, might virtually disappear. Some of the potential investment would no doubt go into BES funds or direct, local investment, but some would almost certainly not.

9. The impact of the changed regime for forestry will be more marginal. But by reducing the scope for sheltering income via this route, the Government will be enhancing the relative attractiveness of BES, despite reducing absolute returns. However, the effect is not likely to be great and cannot be quantified.

Proposed "Half-BES" for Renting

10. The level of BES investment in private renting will depend on the post-tax returns available and the perceived risk which will determine its attractiveness relative to other forms of investment. BES companies specialising in providing rented housing are unlikely to be seen as significantly safer than existing asset-backed BES investment (particularly given the political risk) and, with only half relief, the average rate of relief for investment in these companies will be only 20%. We think that BES schemes for private renting are therefore unlikely to attract those higher rate (or basic rate) taxpayers who currently regard BES investment as unacceptably risky. Furthermore, we do not expect the new relief to attract many people who currently make conventional BES investments but will be discouraged from doing so by the lower income tax rates.

11. This is a crucial assumption - we are saying that the pool of potential BES investors is unlikely to expand as a result of the new (half) relief for private renting. This is simply a judgment based on past experience of BES and our assessment of the relative attractiveness of investment in

BUDGET SECRET: TASK FORCE LIST

private renting. If the assumption proves wrong our costings will be too low.

12. The imposition of a ceiling on BES investment for each company will alter the relative risk and return on BES investments. Some investors who, but for the ceiling, would have chosen BES may be diverted into the new relief for private renting.

13. It is difficult to calculate the combined effect of the various influences. But, assuming half relief and no ceiling for investment in private renting, the following figures seem unlikely to prove too low:

	<u>Investment</u> <u>Existing BES</u>	<u>Private</u> <u>Renting</u>	<u>Total</u>	<u>Tax Cost</u>
i. Current regime	160	0	160	80
ii. New regime with no ceiling	120	10	130	50
iii. New regime with £1m ceiling	80	50	130	40
iv. New regime with £0.25m ceiling	40	70	110	30

14. These figures make some highly tentative assumptions, which are little more than guesses.

- a. First, they assume that the effect of the income tax changes will be a fall in conventional BES investment of £40 million to £120 million (row (ii) of the table), partly offset by £10 million investment in private renting. This assumption reflects the large amount of BES investment currently made by 60 per cent taxpayers (£130 million). It also assumes that conventional BES

investment without a ceiling will be more attractive than investment in private renting (with only half relief).

- b. Second, they assume that a £1 million ceiling for conventional BES investment (but a high ceiling or no ceiling for investment in private renting) will reduce considerably the amount going into conventional public offers (currently about £115 million a year) but do little to discourage BES funds (currently raising about £30 million a year) or other BES investments (making up the balance of the £160 million a year BES investment). Comparing row (iii) and row (ii), the assumption is that all the conventional investment which is discouraged in this way goes into investment in private renting (this may be an over-estimate).
- c. Third, they assume that a £0.25 million ceiling would virtually eliminate conventional public offers and also adversely affect BES funds. Only part of the conventional investment which is discouraged by this low ceiling is assumed to go into investment in private renting (with half-rate relief).

15. On this basis the continuing tax cost of the new relief might be £10-£15 million a year - representing an investment of £50m to £70m a year. (At a cost of £40,000 per house, this would result in a further 1,200 to 1,700 dwellings per year - more if the companies also raised capital by borrowing.)

16. The DOE have approached the question from a completely different angle. Their view of potential take-up is based on the number of houses which may come into the rented market at a given rate of return. This in turn is based on their experience (which they admit is limited) of the returns available in the housing sector generally.

17. Using the assumptions in the joint working group's report of November last year, they have made adjustments to take account of the restriction to half BES, but not the reduction in the highest rates of income tax to 40 per cent. The rate of return varies according to the company's gearing, but is estimated to be of the order of 8.6 per cent for a 50 per cent taxpayer, (7.5 per cent to a 40 per cent taxpayer).

18. At a rate of return of 8.6 per cent, DOE believe that there could be additional investment in rented housing of £200 million in the first year, and £400 million thereafter. This would produce 5,000 dwellings in the first year and 10,000 in each subsequent year at an average price of £40,000 per dwelling. The resulting tax cost depends on the amount of borrowing assumed, but the first year tax cost would be of the order of £25-£40 million, with the second and subsequent year cost rising to £45-£80 million.

19. The DOE approach is quite as subjective as the assumptions underlying our costings; and it takes no account of the past take-up of BES, nor the (relatively) safe nature of most existing BES investments. Moreover, DOE are not aware that the value of BES relief will be reduced by income tax reductions in the Budget.

Possible Full Relief for Investment in rented housing in Inner Cities

18. The possibility of giving full BES relief for investment in private rented housing in inner cities has also been raised. On the working group's assumptions, the rate of return on such investment could be of the order of 13% as compared with 7.5% with half BES relief. This pushes up the attractiveness of investment in private renting relative to existing BES investments, and it is likely that more BES investors, or even some people currently not willing to invest in BES, might invest in private renting at these levels of return. We have no way of quantifying this

effect. But, it seems unlikely that investment in rented housing would exceed the levels achieved by BES in recent years when relief was available at 60 per cent and many of the investments were promoted as asset-backed. If, for example, £125 million were raised under the new scheme (and assuming full relief at 40%), the cost would be £50 million a year. This would represent about 3,000 to 5,000 dwellings per year, depending on the level of gearing.

CONCLUSION ON BES COSTS

19. On the basis of the above analysis, we would estimate the potential cost of the proposed half-BES scheme to be of the order of £10-£15 million (but with full BES relief for investment in inner cities the cost would be up to £50 million). This is lower than DOE's estimate: they put the annual cost at around £45-£80 million. But as explained, their basis for costing is no more certain than the Revenue/Treasury approach: and in the past DOE estimates of the take-up of the assured tenancy schemes have proved on the optimistic side. We cannot, however, be certain that the actual cost would not prove to be as high as the DOE suggests; or indeed, that the actual cost would not prove to be lower or higher than both of our ranges.



Inland Revenue

Policy Division
Somerset House

*Spoke by Wilson
and PM*

*£20,000 limit
(limit to payee)*

FROM: P LEWIS

DATE: 11 FEBRUARY 1988

Chancellor

LEWIS
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CARS
11/2

CARS: BENEFITS IN KIND AND CAPITAL ALLOWANCES

1. This note analyses the options discussed at the last Overview meeting

- a doubling of the car scales for 1988/89, with the P11D threshold either at £8,500, £9,500 or £10,000
- a further 10% increase in car scales for 1989/90
- an increase in the capital allowances ceiling for expensive cars to £16,000.

2. Miss Rhodes' note looks at the legislative/parliamentary/operational implications of including the car scale changes in the Finance Bill rather than making them through a Treasury Order. A similar point arises on the capital allowance change (paragraph 11).

3. On the industrial implications, the Treasury have concluded that the effect of the additional changes since their last note cannot be assessed accurately and falls well within the margins of error of their original calculations. But the bringing forward of the changes to 1988/89 is important to the car industry because of the short notice, and they suggest that should be mentioned to Lord Young (if you have not already done so).

Losers

4. Table A analyses losers on a cash basis, and by reference to Option 3. As in the previous note, the number of losers and the average loss are derived from estimates of the actual distribution of company cars over various income bands; but the range of losses shows the maximum theoretically possible rather than the maximum loss which will necessarily occur.

Table A: CASH losers from doubling the scale charges in 1988/89

	<u>Losers</u>		<u>Tax loss (£)</u>	
	Number (thousands)	Percentage (of the 1.3 million company car holders)	Average	<u>Theoretical</u> Range (excluding cars with 50% surcharge and expensive cars)
P11D threshold £8,500				
above P11D limit	40	3	45 }	Up to £420
below P11D limit	30	2	330 }	
P11D threshold £9,500				
	30	2	65 }	Up to £400
P11D threshold £10,000				
	30	2	65 }	Up to £ 90

(larger cars, 160)

5. The 6 charts in the Annexes are specimen income tables showing, for each of the three main car bands, the income ranges over which losses could arise and their size. The first three (Annex A) compare the £9,500 threshold option with £8,500; the last three (Annex B) £9,500 with £10,000. As before, while the table covers all classes of cars, including those with a 50% surcharge and a 50% discount, and cars over 4 years old, the Annexes do not show the position of "perk" cars with a 50% surcharge which would produce larger losses.

Yield

6. The yield from these three options (ignoring behavioural changes) would be as follows:

Table B: Yield from doubling car scales in 1988/89

	1988/89	1989/90	1990/91	1991/92	£m
<u>Doubling of car scales combined with</u>					
a. £8,500 threshold	260	310	320	330	
b. £9,500 threshold	220	270	290	310	
c. £10,000 threshold	210	260	280	300	

Note: Scorecard figures are £30m less as the 10% increase for 1988/89 already announced is included in the base forecast.

Evaluation of the P11D options

7. Leaving the threshold unchanged produces more revenue, but it creates more losers and more large losers. It looks the least attractive of the three.

8. There is less to choose between £9,500 and £10,000. The lower limit would produce about £10m more revenue. Although the figures cannot be distinguished in Table A because the underlying data is not sufficiently detailed, there would clearly be some more losers with the lower limit; and as Annex B shows the range of losses could be higher (though the only big loser would be the odd case of the man earning just over £7,000 with a 2 litre car).

9. Given the relatively small difference in the revenue yield, we would on balance recommend the £10,000 option to give a lower number of losers and lower range of losses; and because it is safer in relation to the likely number of large losers. It also looks more attractive in the deregulation context.

Capital allowances for expensive cars

10. At your meeting last Monday you decided (provisionally) that the ceiling should be doubled - for new cars only - to £16,000. We suggest the new ceiling should apply to expenditure incurred

after Budget Day. Any later date would depress business car sales between the date of the announcement and the start of the more generous rules.

11. Like the car scale changes, this change could, if you wished, be made by statutory instrument. Alternatively, - and this seems the better course if the car scale changes are to be in the Finance Bill - it too could be included in the Bill to show the whole picture on car taxation changes, and to avoid any possibility of a separate debate on cars on the statutory instrument. Inclusion in the Finance Bill would also eliminate any possible procedural difficulty over laying an order to come into force immediately.

12. Without the change in the ceiling, about 400,000 cars purchased in 1988/89 would have been affected by the special capital allowance rules. This figure will now fall to about 30,000 - so, from a deregulation viewpoint, you will be able to claim that the burden has been lifted from more than 90% of the cars which would otherwise have been affected.

13. The cost of making this change would be:-

1988/89	1989/90	1990/91	1991/92	1992/93	£m
Negligible	50	110	130	100	

Overall yield from car taxation changes

14. You are proposing to announce this year a 10% increase in the car scales for 1989/90 as well as the doubling of the scales for 1988/89 and the capital allowance change. (The note of the last Overview meeting (paragraph 5(i)) suggests that you would be announcing the expectation that the scales would be increased by similar amounts in future years. Our understanding was that while this is your present intention, you would not announce anything about it in the Budget).

Amor

15. The following table brings together the net yield over a run of years from the package of car changes you are proposing to announce in the Budget.

Table C: Net yield from car taxation changes

		£m			
	1988/89	1989/90	1990/91	1991/92	
i. 100% increase in car scales charges for 1988/89 with £10,000 P11D limit*	+ 210	+ 260	+ 280	+ 300	
ii. 10% increase in car scale for 1989/90	-	+ 50	+ 60	+ 70	
iii. £16,000 capital allowances ceiling	negligible	- 50	- 110	- 130	
<u>Net total</u>	+ 210	+ 260	+ 230	+ 240	

* There would be an extra £10m yield with the P11D threshold at £9,500.

Note:

- i. There would be an additional yield in the last two years if further increases in the car scales were made for 1990/91 and 1991/92.
- ii. £30m of the total yield from the 100% increase is already in the forecast, and will not appear in the FSBR, as it has already been announced.

Handwritten note:
 Hacky - My.
 R. Strain

Break points for expensive car scales

16. Given that you have decided to take no special action on expensive cars, do you wish to leave the present starting points for the two ranges of expensive car charges unchanged at £19,250 and £29,000 respectively for both 1988/89 and 1989/90?

17. The arguments for doing so are

- these are the figures already announced for 1988/89
- these limits have been raised by a substantially greater amount than the increase in the index of new car prices since 1977/78. (At that point the break points were £6,000/£10,000. The new car price index has increased by 165% over the last 10 years; whereas the lower break point is now 220% higher and the upper one 190%).

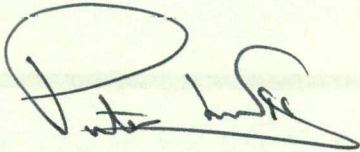
Points for decision

1. Is the doubling of the car scales for 1988/89 confirmed?
2. What should the P11D threshold be for 1988/89?
3. Is the 10% increase in car scales for 1989/90 also confirmed?
4. Should the break points for expensive cars remain at £19,250 and £29,000 for both years?
5. Is the doubling to £16,000 of the limit for capital allowances for expensive cars confirmed (subject to the cost being available in the final package)? Is it to be effective for cars purchased after Budget Day?

Yes
£10,000
yes
yes
yes
yes

(Mandy?)

6. Is there any further work you would like done at this stage, either generally or in connection with speaking to Lord Young again?



P LEWIS

The Board Room
Somerset House
London WC2R 1LB



Inland Revenue

Subsidy is defined by direct costs: comp on basis of approx 1/2 each employer equals (each) (more who share cost @ all)

FROM: A J G ISAAC

DATE: 11 FEBRUARY 1988

CHANCELLOR OF THE EXCHEQUER

Answer to para 4 of Prescott

Prescott's opinion

see also Prescott's para 5 (John Isaac @ x)

BENEFITS IN KIND : DIRECTORS' DINING ROOMS

1. Mr Prescott's note below responds to the remit that you gave us at last Monday's Overview. May I try to draw out a few general points.

2. First, I was among those who recognised in the context of the FBT a possible option of enforcing the tax charge on directors' dining rooms (the present exemption is largely by Extra Statutory Concession). Whatever the tax system, there are potentially difficult technical or political issues to be decided on, for example

- What is a "directors'" dining room? and
- How to define and measure the subsidy?

These difficulties could have been decisive, even in an FBT. A good deal could have depended on whether the answers were broad or narrow, simple or complex. At least, however, the whole point of the FBT was that any tax charge fell on the employer: it was not necessary, in addition, to address a third area of difficulty and identify the benefit enjoyed by individual employees.

3. When we discussed this with the Financial Secretary before last Monday's Overview, we suggested that if Ministers felt it necessary to pursue this possible charge within the present tax system, the most promising approach would be to begin by

ISAAC
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DINING
ROOMS
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establishing the employer's subsidy (as under FBT). One possibility was that the tax might then be paid by the employer at some more or less arbitrary flat rate (a 'mini' FBT, or - more precisely - an arbitrary form of 'compounding' the employee's income tax liabilities). The Overview meeting ruled that out.

4. In theory, a possible variant might be to allow employers to apportion the actual subsidy between the eligible employees on some just and reasonable basis⁽ⁱ⁾ and tax the employees accordingly. Given the obvious scope for argument between employees - would there be a right of appeal against the employer's apportionment? If so, to whom? And would all employees have to join in? - I doubt if that is practicable and indeed I would expect most employers to prefer the "mini FBT".

5. A further possible and more practicable variant⁽ⁱⁱ⁾ might be to apportion the subsidy between eligible employees on a more arbitrary "formula" basis. For example, the legislation could

(a) divide the annual subsidy by the number of eligible employees, and treat each individual employee as having enjoyed his pro rata share of the subsidy; or

(b) multiply the subsidy per meal by the number of meals each individual employee has taken, and treat the individual employee as having enjoyed his (more fine-tuned) benefit accordingly.

(i) Subject to a reasonable split between basic and higher rate taxpayers, the apportionment would be a zero-sum game between the employers and the individual employees, in which the tax office would not need to concern itself unduly.

(ii) A possible sub-variant of this might be to have banded scale charges, so that employees enjoying a subsidy of less than £x (for example £50 a year) were exempt from charge; employees enjoying a subsidy of more than £x but less than £y (for example £100 a year) were treated as enjoying a benefit of £n: and so forth. There is more than one view here whether this sub-variant would help - or add yet further to the complexity.

6. The alternative approaches in (a) and (b) of paragraph 5 above illustrate the basic choice which has to be made, if the objective is to impose a charge to tax not on the employer (subsidising the canteen) but the employees (enjoying the subsidy):

- to the extent that legislation imposes a flat rate charge on every employee with access to a subsidised "directors'" dining room - without modifying the charge in answer to questions: How often does he use the dining room? How much does he eat? How much does he pay? - the tax is open to criticism as being too unfair in too many cases. (In what we tend to think of as "directors'" dining rooms, a realistic charge would need to run well into three, and probably four, figures per annum; but there will be meals for directors and senior staff, provided separately, costing much less than this);
- to the extent that the legislation requires employers or employees to record detailed information - for example how often does each employee use the dining room? How much does he eat and drink? How much does he pay? - it is open to the opposite criticism, of seeking equity at the cost of unacceptable bureaucracy.

7. These arguments seem to me clearly to rule out the two extremes: a universal flat rate scale charge applying to all employees; or (as the Overview meeting recognised) a charge on each employee according to the subsidy which he actually enjoys. There is a question whether there is a viable middle course: something which is admittedly pretty arbitrary and rough justice for individual employees and admittedly a significant additional compliance burden on employers - but neither to an intolerable degree. There are obvious interactions between the mechanics and the scope and size of the charge.⁽ⁱⁱⁱ⁾ In our earlier discussions with the Financial Secretary some of us suggested that, at least in the absence of the FBT, there were serious

reasons for doubting whether the game was worth the candle. But I cannot see that the answer can lie in a flat scale charge.

C L O R

A J G ISAAC

(iii) It was mentioned in the course of the Overview meeting that there must be some directors' dining rooms which even now are not exempt under the terms of the present ESC. In so far as tax is in practice now charged in these cases (we have no central information on this and no published guidelines), it will be by ad hoc negotiation between the local tax office and local employer and his accountant. Our guess is that the numbers are probably relatively few, and the amount charged on this informal basis relatively small (this is certainly consistent with Mr Scholar's experience of employment with a business that was charged at 15p a day - the value of a tax free luncheon voucher). It is, thus, one of the areas of the benefit system where no great difficulty has arisen, in part because nothing much has changed over 40 years. I very much doubt that continuing 'benign neglect' on the essential details is a realistic precedent, if Ministers are looking for a tax strategy withdrawing the 1948 ESC, and seeking a substantial new tax charge on large numbers of "directors'" dining rooms throughout industry and commerce. In the present day both taxpayers and tax offices would - rightly - demand clear published guidance on the principles under which their new tax liability would be charged, and the way it would be allocated. Whether or not there was new primary legislation (and a scale charge would of course require new primary legislation) it would be necessary for Ministers to address the three main sets of questions - Which dining rooms? What costs? How allocated? - and to publish clear answers of a kind that both taxpayers and tax offices could use in negotiations and any subsequent appeal proceedings.



Inland Revenue

Policy Division
Somerset House

FROM: M PRESCOTT
DATE: 11 FEBRUARY 1988

CHANCELLOR

DIRECTORS' DINING ROOMS AND LUNCHEON VOUCHERS

1. At the Overview Meeting on 8 February, you asked us to explore further a possible package comprising
 - (i) withdrawal of the concessionary 15p a day exemption for luncheon vouchers
 - (ii) introduction of a new - statutory - charge on the benefit of subsidised meals in staff restaurants, directors' dining rooms etc that are not available to the staff generally, the benefit to be measured by reference to some sort of "scale charge".

PRELIMINARY POINTS

2. There are a number of preliminary points on which decisions would be needed but on which, for present purposes, we make the following assumptions
 - (a) The charge would apply to any canteen or dining room that was not available to the staff generally, even though those who were excluded got subsidised meals - perhaps of a similar kind - in a different canteen. Nor, therefore, would it be confined to dining rooms that were exclusively for, say, directors or senior staff.
 - (b) There would be no charge if there was no subsidy - ie where the dining room was for the exclusive use of, say, directors but where they nevertheless paid the full price for any meals consumed there. It follows from this that

PRESCOTT
CHIEF
DINING
ROOMS
LV 11/88

(c) even with a scale charge, it would still be necessary to specify which costs could and could not be subsidised (ie would the measure of the benefit include any subsidy towards indirect costs, or only direct costs?) And it would still be necessary for those employers who do not do so already to produce some kind of profit and loss account for the facility in question if they wanted to show that there was no subsidy and that the scale charge should not therefore apply.

3. One other point should be noted. The vouchers legislation applies to all employees, not just directors and the "higher paid" employees. Withdrawal of the LV concession would, therefore, mean that some "lower paid" employees were also affected. It would be for consideration whether, on grounds of symmetry, the new charge for exclusive dining rooms should similarly apply to directors and all employees; or whether it could be restricted to directors and "higher paid" employees on the grounds that there are in practice likely to be very few "lower paid" employees for whom there are exclusive canteens anyway.

WHICH DINING ROOMS?

4. The main target for the charge would be dining rooms that were for the exclusive use of directors and senior staff. But limiting it in this way would make avoidance relatively easy - eg by the simple expedient of allowing other staff occasional use of the facility. There would also be definitional difficulties - eg "senior staff". In practice, therefore, the provisions would probably need to be cast more generally in terms of a charge on subsidised meals provided by an employer in any canteen or dining room that was not available for the use of staff generally. This has the further merit that it is simply the obverse of the existing statutory exemption for canteens.

5. At this point, however, it is worth pausing to consider how the existing rules operate. In particular, the ambit of what we conveniently refer as the "director's dining room" ESC does in fact go rather wider than the title suggests, as will be seen from the following extract from Instructions to Tax Offices

"The exemption [ie the statutory exemption relating to canteens where meals are provided for the staff generally] should be regarded as covering the costs to the employer of providing lunches on a reasonable scale for directors and "higher paid" employees on the business premises of the employer if luncheon facilities are provided generally for staff working at the same place, notwithstanding that the provision for the staff is in separate accommodation or premises ...

... the exemption does not apply to facilities that are provided only for directors and "higher paid" employees, no corresponding facility being provided for employees generally".

*Is this
conjunction?*

6. Thus, we would already catch dining rooms that were exclusively for directors, or indeed for any other group or staff who were "higher paid" employees (which of course means anyone earning over £8,500, and not just "senior staff"), if there was no corresponding facilities provided for the other staff. However, while the provision must be on a "reasonable scale" where there are separate canteens, this can - and in practice - will still mean significant differences in the level of provision. Moreover, there is also the more fundamental anomaly under the present rules that the directors etc could eat well and tax-free on the premises in their exclusive dining room while the other staff got LVs that were taxable on anything above 15p.

7. The essential difference between the existing and the proposed new regime, therefore, is that under the latter we would also be catching

- (a) dining rooms that were exclusively for, say, directors even though other and perhaps even similar - but separate - canteen facilities were provided

for the other staff on the same premises. The justification for introducing such a change here would presumably be that exemption should nevertheless only be available where all the staff eat in the same canteen and on similar terms

- (b) any canteen exclusively for a particular group of staff (not necessarily "directors" or senior staff) where the other staff at present instead get luncheon vouchers.

8. On the face of it, a provision which applied to canteens that were not available to the staff generally (paragraph 4 above) would be wider in scope than one which applied to canteens that were exclusively for, say, directors and senior staff - ie because it would apply to any canteen that was for the exclusive use of a particular staff group and not just to those exclusively for directors etc. However, two points on this should be noted

- (i) companies with more than one site may have different canteens on different sites. But this would not be a problem provided that each canteen was available for use by staff from the other sites, even though in practice they only ever used the canteen at their own site. In some cases, however, this could be open to manipulation and it might be necessary to make the test of availability one that applied to all staff employed at a particular site or in a particular building
- (ii) a company might have different canteens for staff in different grades - eg shop floor, administrative, senior management, etc. Again, however, there would be a problem only if any of the canteens was not available to staff from the other grades. Thus, so long as the eg administrative and management staff could use the shop floor canteen, the latter would

not be chargeable. But if the shop floor staff were not allowed in to the administrators' canteen that would become taxable as would the managers' canteen if the shop floor and/or administrative staff were not allowed in.

In practice, therefore, though cast in general terms the new charge would still be likely to operate mainly on director's dining rooms.

SCALE CHARGE

9. The charge would apply to those employees and directors who did have access to the restricted canteen or dining room in question. However, instead of measuring the taxable benefit by reference to the actual cost to the employer of the subsidy provided for meals consumed in that canteen by each employee concerned, it would be measured by reference to some sort of scale or flat rate charge. The question, however, is what kind of scale charge is envisaged, to what would it relate and how exactly would it work.

What is being measured?

10. A major difficulty in seeking to apply a scale charge approach to subsidised meals in canteens and dining rooms is the lack of homogeneity. With cars, for example, a scale charge can be used as a convenient way of measuring the gross annual cost to the employer of providing the particular car in question - and that cost can in turn be determined by reference to independent external sources like the AA analysis. Moreover, for a car of a particular size and age etc, that cost will not normally vary much as between one employer and another. Broadly speaking, therefore, there is only one thing that is being measured. So, it is possible to arrive at a suitable figure for the scale charge, and then to apply it universally.

11. By contrast, with a facility like canteens and dining rooms there will be enormous differences in the level of provision between one employer and another, in terms both of the type and range of meals provided, and the level of the employer subsidy towards the cost of those meals. Similarly, there is no such thing as a standard meal - this could be anything from a glass of orange juice and a sandwich to a 5-course lunch.

12. In short, it is far from clear what exactly the scale charge would be measuring.

13. Perhaps the simplest approach would be to adopt an essentially arbitrary level for the scale, informed by what was known or guessed about the average level of subsidy for staff canteens and dining rooms generally but in no way purporting to be a measure of the actual benefit in individual cases. There might also be a second, higher scale for dining rooms that were exclusively for directors and senior staff on the rough and ready justification that the average level of subsidy in such dining rooms is probably higher than for canteens generally. The scale charge would then simply apply in respect of any "meal" consumed by an employee in an "exclusive" dining room, unless the company was able to show that there was no subsidy at all.

14. Neither we nor the Departments we have consulted (D/Employment, OME, etc) have any reliable information about the number of employees receiving subsidised meals generally - ie whether or not in "exclusive" canteens - or about the level of subsidies. All we have to go on are some figures produced by the company promoting luncheon vouchers (LV Ltd) and we cannot say how reliable those figures are. These suggest, however, that the average employer subsidy per "meal" may be about 60p, excluding any subsidy in respect of indirect costs like accommodation. (LV Ltd say the subsidy is much higher if indirect costs are included). But there are also enormous variations, as the attached figures quoted by the company

concerned suggests*. And, the level of subsidy in particular cases could theoretically be very high indeed - eg where a company provides a dining room in which the directors can eat a gourmet lunch every day, and drink the finest wines.

15. The appropriate daily level of subsidy on which to base it could under this approach be anything from say, 60p-£1 (average for all canteens, and allowing little or nothing for employer's subsidy in respect of indirect costs) to, say, £15-20 (a top-of-the-range director's dining room serving the best food and wines and including something for indirect as well as direct costs). On the assumption that the main target for the new provisions would be directors' and senior managers' dining rooms, and that the level of provision and therefore the level of subsidy is higher here than for other canteens, Ministers would presumably want to take a figure from somewhere in the middle to top end of this range, rather than from at the bottom of it. On this basis, the lowest figure to take for this purpose might be, say, £2 a working day. But it would clearly be possible to justify using a much higher figure - ie £5 or £7 a day, or even more.

16. There about 240 working days in the year, excluding weekends and assuming annual leave of 4 weeks. If the charge was to be an annual one relating to availability (see paragraph below), an assumed daily subsidy of £2 would (in round terms) imply an annual scale of about £500; a subsidy of £5 a scale of £1200; and a subsidy of £7 a scale of £1700.

17. Of course, none of this is very scientific and one could play around with all sorts of other figures.

*NB. The comparison being made in the Annex is with the estimated commercial cost of a comparable meal, not with the cost to the employer of providing it. This will presumably be lower than commercial cost and so too, therefore, would the level of the employer subsidy.

18. Clearly, however, a single universal scale charge of this kind would be a very crude measure indeed and would no doubt be strongly criticised as such. Because the amount of subsidy will in practice range enormously between employers, it would also imply overtaxing of the benefit (ie the subsidy) in some cases and undertaxing in others. Moreover, the same charge would have to apply regardless whether the "meal" in question comprised a quick snack or a 5-course meal.

19. In theory, a second approach would be to have some kind of scale that reflected, very broadly, different levels of subsidy. Amounts of up to (say) £1 a "meal" might be ignored, and there might be a top rate scale charge of (say) £10, with 2 or 3 bands in between. In practice, however, this would be virtually impossible to operate. There would have to be a "profit and loss" calculation for each dining room and canteen concerned, with every one of them then being graded according to the average level of subsidy per "average meal". The operational implications alone - both for us and companies - make this a non-starter.

Gross or net?

20. The discussion above assumes that the scale charge would be based on the net benefit involved - ie the employer's subsidy, as represented by the difference between the gross cost to him of the meals etc and the amount (if any) paid for them by the employee. This is different from the car scale charge which is a proxy for the gross measure of the benefit - ie the gross annual cost to the employer of providing the car, before allowing for any contribution towards that cost from the employee. It follows, therefore, that while the car scale charge is reduced by any contribution from the employee towards the car's cost, a canteen scale charge that was on a net basis would in effect already take account of anything paid towards the cost, and it would therefore be double counting to allow it to be further reduced by the amount if anything that the employee actually paid for the meals.

I entirely agree that X looks very formidable, and it may very well not be a "finisher". If it came to the point, however, we might need to consider whether it would be so much worse than the alternatives. (H.S.)

21. Alternatively, however, a canteen scale charge could be based on the gross cost to employers of the meal etc. (Again, it would be for decision whether this included indirect costs, or direct costs only).

22. Choosing the appropriate level for the charge would be largely a matter of judgment, with no very scientific basis or reliable information on which to proceed. Nor, again, would it purport to be a measure of the actual cost in any particular case. Clearly, however, if LV Ltd are right in saying that the average subsidy for canteen meals is at least 40% excluding anything for indirect costs, and upwards of 100% including indirect costs, then we would be talking about scale charges at least double the levels suggested at paragraph 15 above.

23. But because under this alternative the scale charge would be related to gross cost of provision, there should in theory then be a reduction in respect of anything paid by the employee for his meals etc in the canteen or dining room. Clearly, however, the compliance burden for employers would be intolerable if they had to keep records not only of the number of occasions on which the canteen was used by each employee, but also of the amount that he or she spent on each occasion. Realistically, therefore, this option could only be made to work if it was linked to payments by the employee of an amount at least equal to the standing charge. So, if the employee paid an amount equal to the whole of the scale charge (whether an annual one relating to availability, or a daily one relating to use) there would be no taxable benefit; otherwise, there would be a taxable benefit equal to the whole of the scale charge.

Availability or use?

24. There is in principle a further choice for consideration, between

- (a) an annual scale charge, relating to availability, and
- (b) a daily charge relating to actual use.

25. In theory, the scale charge could be an annual one relating to availability of the canteen, not actual use of it by the employee concerned. This would in some ways be analogous to the scale for cars and would be much simpler for employers and ourselves than a scale charge relating to use.

26. But there would be a number of difficulties

- there would probably have to be some let out for the director or employee who, for whatever reason (health, egalitarian beliefs, etc etc) opted never to use the facility in question and in fact did not do so. Monitoring the observance of such a self-denying ordinance would, of course, be virtually impossible.
- just as the car scale charges are reduced proportionately if the car is not actually available to the employee for part of the year, so too would there be pressure to allow a proportionate reduction for times when the employee was not in a position to avail himself of the facility even if he wanted to - ie absence from the office on business or sick leave. This would obviously complicate things both for the employer and ourselves. Moreover, while the scale charge would have been based on an assumed average working year of, say, 240 days, the actual length will vary from one employee to another and so there would be room for argument about the appropriate size of the numerator for the scaling down proportion.

- even with a reduction in the charge for times when the employee was not in a position to use the facility, a major difficulty with this approach is that the employee would incur the whole or substantially the whole of the scale charge even though he might actually use the facility only once or twice. This would no doubt be criticised strongly. Moreover, while with company cars - where similar criticisms might be made - it can be argued that there is a benefit simply in having a car available for private use in case it is needed (eg for emergencies), even if it is not used much in practice, that kind of consideration does not apply with a company canteen.

27. In practice, therefore, the scale charge would probably have to be one that related to actual use of the facility by the employee concerned, and not one relating to availability. Such a scale would obviously avoid the difficulties above, and would probably also be less controversial.

28. But this would in most cases involve a lot more compliance effort for the employer, and extra hassle for the employee - ie because of the need to record every occasion when the facility is used, rather than the - presumably much less frequent - occasions when the employee was not in a position to avail himself of it. This approach also reintroduces the problem that the same charge would have to apply irrespective of what the employee actually consumed on the day in question - ie whether he had a 5-course lunch, or only a cup of tea and a bun. Again, this would no doubt be strongly criticised.

OPERATIONAL ASPECTS

29. As mentioned earlier, the operational implications for both employers and ourselves would depend on what kind of scale was adopted. One relating to use would be

administratively much more difficult for employers than a simple annual charge relating to availability; it would also be operationally more difficult for us (though not as much for employers) eg because of the additional and more complex validation tasks that would be involved.

30. We do not at present have any information about which employers have subsidised canteens, which of them are exclusive, what meals are provided and which employees are benefiting. If Ministers wanted to start taxing these benefits immediately, therefore, we should need to mount a special exercise to obtain the necessary information so that coding adjustments could be made for 1988/89. Clearly, that would have a heavy resource cost, and probably out of all proportion to any additional yield. However, if liability did not start until 1989/90, it would be possible to make coding adjustments for that year as P11Ds came in after April 1989 in respect of 1988/89. There would still be some additional workload and it might take a year or two until this benefit was fully reflected in coding, but this would obviously be much more manageable.

LEGISLATION

31. Legislation would be needed for a scale charge and the length, coverage and complexity of this would depend on the kind of scale being introduced. Some - eg a simple annual charge relating to availability and with minimal exemption - would be easier to draft than others, but with all of them there would inevitably be various more detailed points concerning definitions, mechanics etc that needed to be covered.

CONCLUSION

32. Subsidised canteens - whether or not of the exclusive variety - are a good example of communally provided benefits where it is relatively easy to determine the aggregate amount

of the benefit provided by the employer (ie the total subsidy for the facility in question), but virtually impossible to determine the benefit - the share in that subsidy - enjoyed by any one individual using the facility. Apart from a special "mini FBT" system for taxing the employer, therefore, the only other possibility if there is to be any significant extension in the taxing of such benefits in the hands of employees would be the introduction of some kind of scale charge. But this would not be easy.

33. A major difficulty in seeking to apply a scale charge approach to canteens is the lack of homogeneity. Unlike say cars, there is with subsidised canteens no single thing that is being measured nor a single level of subsidy and so it is virtually impossible to apply the scale approach except in a very crude way that would no doubt be strongly criticised. Any such charge would inevitably result in the benefit being either undertaxed or overtaxed. It is unlikely that those being overtaxed would find comfort in being told that this was an averaging arrangement, and therefore that there were other employees who in compensation were being undertaxed.

34. If there was to be a scale charge for canteens, however, this could be one or two main kinds - an annual charge relating to availability, or a daily charge relating to use, in either case with a further choice between a charge based on gross or net cost of provision.

35. An annual charge relating to availability would be easier in terms of compliance for employers, and in terms of administration for the Revenue. But even if there was some kind of reduction for times when the employee was simply not in a position even to avail himself of the facility, such a charge would be open to the criticism that the employees would still be chargeable on the whole or substantially the whole amount even if in practice they used the facility only one or twice. A daily charge relating to actual use of the facility

would overcome that particular difficulty, but would involve a much greater compliance burden for employers and employees.

36. As for the choice between a gross or net basis for the charge, the ^{former} latter looks more difficult presentationally. This is partly because the level for the scale charge would by definition be considerably higher than under a net basis, and also because in practice - to avoid intolerable compliance burden on employers - the employee would either have to pay an amount equal to the whole of the scale charge, or be taxed on the whole of that amount.

37. The precise targeting and rationale for the proposed package perhaps also needs to be considered. The change would presumably be presented mainly on the grounds that in practice the level of subsidy in "top" dining rooms is likely to be much higher than anything provided for the other staff either in separate canteen or by way of LVs. But we would also be catching those cases - admittedly probably not many in practice - where there is an exclusive facility for, say, the directors but where there is also a similar - albeit separate - facility for other staff as well. The reason for the linkage between the proposed new charge and withdrawal of the LV concession would not be very clear in these cases.

Points for decision

- In view of the difficulties outlined above with adopting any kind of scale charge approach for canteens, do Ministers still wish to go ahead with the idea of a linked LV/dining rooms package?
- If so, how could the linkage between withdrawal of the LV concession and the introduction of a charge for "exclusive" canteens best be presented?

BUDGET SECRET: TASK FORCE LIST

- If there is to be a scale charge, should it be based on availability, or on use; should it be on a gross or net basis; and at what level should it be set?
- Should the new charge apply only to directors and "higher paid" employees, or to "lower paid" employees as well?

M PRESCOTT