

PO-CH/NL/0638 PTA

PO CH/NL/0638
PART A

PO CH/NL/0638
PART A

1987 BUDGET VEHICLE
EXCISE DUTY TAXATION
AND EXCISE DUTY ON
ALCOHOLIC DRINKS.

18-3-87

DDS 2575 NARS 7/11/96

THIS FOLDER HAS BEEN
REGISTERED ON THE
REGISTRY SYSTEM

Vehicle Excise Duty
Taxation + Excise duty
on Alcoholic drinks

1987- 638



DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

CONFIDENTIAL

31 July 1986

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
LONDON SW1P 3AG

See Nigel.

CH/EXCHEQUER	
REC.	01 AUG 1986
ACTION	MR ROMANSKI
COPIES TO	EST. FST. MST. EST SIR P MIDDLETON MR LITTLE MR SCHOLAR MR MONGER MISS SINCLAIR MR A EDWARDS PS/CTE

SS/DTP
TO
CH/EX
31/7

I am grateful for your letter of 2 June in reply to Nicholas Ridley's of 19 May about the international aspects of lorry taxation. Nicholas had warned you in his letter that he hoped to write soon about vehicle taxation policy generally. That is the subject of this letter.

In the Budget you were able to accede to Nicholas's request that more emphasis should be given to fuel duty and less to VED within the total of motoring taxation; VED was frozen, and the fuel duties increased by a little more than inflation to compensate. I recognise, of course, that you might have taken this measure irrespective of transport policy considerations, since the low price of oil made tax increases there comparatively painless.

However, the transport aspects are important and I would ask you to give very serious consideration to continuing the same trend in the next Budget. I need not dwell on the advantages for our international hauliers and for the reduction of VED evasion, which Nicholas covered at some length in his 18 December letter. (There is of course even more urgency about the enforcement problem than there was then, since the National Audit Office has recently attacked the level of evasion, and we can expect further criticism from the PAC on this point over the summer).

There is however one further advantage in shifting the emphasis of taxation which I might usefully draw to your attention. The fact that buses and coaches do not cover their track costs is becoming an irritant. British Rail and others are continually alleging unfair competition from long distance coaches and it is hard to demonstrate convincingly that this is not so. We do what we can about this by increasing these vehicles' VED; but in reality this can make very little impact on the problem since VED is such a small proportion of their motoring tax; and it tends to attract unfavourable comment in the Committee on Finance Bill each year, partly because of its incidental impact on taxis. By

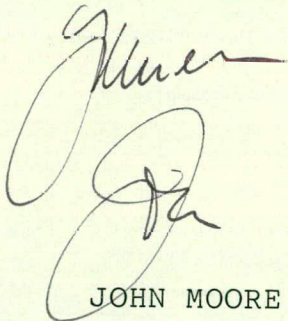
contrast an increase in derv duty would have a much larger impact on the revenue shortfall and yet should pass relatively uncriticised, particularly since some taxis are now entitled to fuel duty rebate.

I believe that a further shift in the balance between VED and fuel duty could also be popular politically. It was noticeable that the Budget change attracted, if anything, favourable publicity; and it is noteworthy that all the other main political parties appear to be espousing a "lower-VED policy. Of course, an overwhelming shift in balance could put up the cost of the proper business use of cars and would also bring the powerful rural motoring lobby into play. But this is not what I have in mind.

Y | Too great a shift would in fact cause difficulty for me over the relationship we seek to maintain between lorries' track costs and their motoring tax. To give you a broad indication, I have in mind an ultimate shift of no more than £100m for diesel vehicles (lorries, hackneys and cars) as a whole. Petrol vehicles are not subject to similar transport constraints (there are few petrol lorries), and, in order to get as much reduction as we reasonably can in VED revenue lost through evasion, I believe it important to maintain or even increase the differential between the rates of duty on the two fuels, thus providing the headroom to bring down car VED. | ??

Apropos of this, I understand from officials that you have been considering the idea of aligning the derv duty rate with the petrol rate, with a compensating reduction in VED rates for diesels. I recognise that giving some relief to our international hauliers was one of the objectives you had in mind, and I would value that, but not at the expense of losing advantages to be had from shifting the balance on petrol and VED, too. Hence my proposal that we should consider moving on both fuels.

How the shift can best be brought about is a practical problem which is bound to be influenced by the prevailing financial climate nearer the time of the next Budget. I suggest therefore that we should agree the principle with interested colleagues now, and address the means towards the end of this year.



JOHN MOORE



In the light of this, I am
preparing to amend my
proposal on these terms: to
increase, with effect, what is
the largest switch from 1987
to 1988 duty in the 1987
Budget (as with the important
point @ X) they can be
made to ~~be~~ when. The
argument for doing a major
switch for which there
agrees: that is clear.
But what is also clear
is that I cannot accept
Y in Mr Moore's letter:
even if I do make a
over

CONFIDENTIAL

The impact on the competitive position of UK hauliers vis-à-vis other EC hauliers is not likely to be very great. You will want to consider the wider implications in the light of this.

FROM: K M ROMANSKI

DATE: 31 July 1986

1. MISS SINCLAIR
2. CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Mr Monger
Mr Scholar
Mr Cropper
Mr McGuigan C & E
Mr Wilmott C & E
PS/C & E

*Ch/see also letter
(just in - below) from
the Transport Secretary
DJK 1/8*

TAXATION OF LORRIES: SHIFT IN BALANCE OF TAXATION FROM VEHICLE EXCISE DUTY TO DERV DUTY

Mr Kuczys' minute of 2 June asked officials to look at the idea of raising derv duty to the level of petrol duty and using the extra yield to reduce commercial vehicle VED. Using 1986-87 revenue forecasts, this minute has been agreed with Customs and Excise; we have also discussed the issues with Department of Transport officials.

Effect of switch

2. To bring derv duty into line with petrol duty at current rates would require a duty increase of 18.1 per cent, or 13.6p per gallon. This would yield £205m in a full year (allowing for the loss of £20m through the automatic increase in bus fuel grants). Lorry VED currently yields £450m, so that it would be almost halved if this proposal was implemented.

Earlier consideration

3. A shift in the balance of lorry taxation was suggested by Mr Ridley before the last Budget, although the maximum shift he was seeking, over a number of years, was £100m. As lorry VED was unchanged in the last Budget and derv duty increased by 2p per gallon more than revalorisation there was a small shift in the burden of taxation on lorries, amounting to about £25m. But the relativities between derv duty and petrol duty were unaltered.

ROMANSKI
TO
CH/EX
31/7

Advantages of a shift

4. The main arguments for a shift in taxation of lorries from VED to derv duty are generally perceived to be:

- (a) it would link total taxation more closely to mileage travelled;
- (b) it would provide an incentive to more efficient use of fuel;
- (c) the significance of VED evasion would be reduced;
- (d) it would help the international competitiveness of UK road hauliers; and
- (e) it would enable more revenue to be raised from foreign hauliers operating in the UK.

5. Of these, (a) and (b) seem likely to be true. But the effect of linking taxation more closely to mileage travelled would doubtless be to stimulate complaints from high-mileage hauliers, who would bear more tax as a result. And, although increasing the derv duty would lead to a more efficient use of derv, it would change the relativities between petrol and derv duty. This would encourage the use of petrol which is a more expensive fuel to refine, and more pollutant, so that this might be considered undesirable. It also raises the question of whether it would be right to shift the burden of taxation on lorries from VED to fuel duty without doing the same for cars - the first three arguments above apply to cars.

Evasion

6. So far as (c), VED evasion, is concerned, the latest DTp Survey of evasion indicates that some 4½ per cent of lorry VED revenue is lost - which represents about £20m. This compares with an overall rate of VED evasion of about 4%. Cutting lorry VED rates will automatically cut the cash loss from evasion; a large cut might also reduce the incentive to evade. But derv duty is also subject to evasion through unauthorised use of rebated fuel. Although this seems recently to have been tempered by the general fall in oil prices, it could increase if the price of derv were to go up as a result of the duty increase.

International competitiveness

7. On (d) I attach a table showing the latest information we have about other EC VED rates and derv prices and duty. Our lorry VED is at present the highest within the EC. Comparisons are difficult because of the multiplicity of different rates. But for a 38 tonne tractor unit with two axles, the UK duty rate is £3100, West Germany £2460 and Denmark £2000. Other Member States have rates of under £1000 (we do not have information for Spain and Portugal). This means that even cutting UK VED rates by half would leave them the third highest in the Community. Even so, a reduction of this order should benefit UK hauliers operating in Europe.

8. On (e), it seems unlikely that a switch from VED to derv duty would lead to much additional revenue from derv duty being secured from foreign lorries. The UK's long standing policy has been to reduce border formalities within the Community, particularly fuel checks and charges which affect our hauliers abroad. For that reason, we have been foremost in pressing for large duty-free allowances for fuel, and it is UK policy to allow duty- and VAT-free admission of all derv in the standard tanks of lorries entering the UK. This means that there are no delays or demands on Customs staff at the ports in checking fuel, of the kind that have caused delays and aggravation at continental frontiers. The standard tanks of a 38 tonne articulated lorry used in international haulage hold 160 to 200 gallons. At 5½ mpg this would enable a foreign lorry to cover about 1000 miles, which would be sufficient for the great bulk of their UK travel. The price of derv in the UK is the highest in the EC except for Ireland. At current factor prices it would be 18p per gallon cheaper at pump prices for a haulier to buy derv in France (the next most expensive) rather than the UK, if UK derv duty were equalised with petrol duty. The incentive for hauliers to arrive in the UK with full tanks is already there and would be increased by higher derv prices. Thus it is unlikely that a switch in the balance of taxation would have more than a marginal effect on the competitive position of UK hauliers as against foreign hauliers in the UK.

*This
Shows
No Link*

Road track cost implications

9. The proposal raises a number of other considerations. Department of Transport attach considerable importance is the effect on their policy that the pattern of total taxation for each class of lorry should match the pattern of road track costs. There is a built-in constraint on the amount of shift for lorries which would be consistent with this. A certain proportion of lorries' tax has to be fixed in relation to mileage but variable according to category (as VED is) in order to ensure that the pattern of tax roughly fits the pattern of cost. DTP calculations suggest that the largest cut in lorry VED revenue which would leave sufficient flexibility for the pattern of taxation to be matched to track costs is 25 per cent. Your suggestion, involving a 50 per cent reduction, therefore goes further than DTP Ministers would probably wish to go, although the new Secretary of State has not yet been consulted on this issue.

10. VED would need to all but disappear for certain categories of lorries. This is because the mileage which they travel means that the higher derv duty rates will result in their total derv duty bill exceeding their total track costs, without taking VED into account. Examples of the categories of lorries affected are (i) the lighter two-axle rigid vehicles, (ii) the lighter subclasses of three, four and five-axled articulated categories, and (iii) all six-axled vehicles. With fuel duty enhanced by 14p and VED on six-axle articulated lorries reduced to £100, there would be a surplus of tax over cost of nearly 100 per cent more than that of any other vehicle. Yet this is the vehicle DTP policy aims to encourage, because it does less damage - tonne km for tonne km - to the roads.

11. But road track cost policy is not an exact science anyway. About 10 per cent of fuel tax revenue (about £685 million in 1986-87) is not allocated to track costs because DTP are unable to say who bears it. This suggests a certain lack of precision both about the existing allocations and about the effects of changes in policy.

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12. There is one other aspect of the proposal which would concern Department of Transport. Aligning the derv duty rate with the petrol duty rate would mean that any shift in the burden of car taxation from VED to petrol duty, which is another of Department of Transport's objectives, would have implications for derv duty. This would add to the road track cost difficulties referred to above.

Effect on other diesel-driven vehicles

13. An increase in derv duty to the level of petrol duty would increase the burden of taxation on buses, coaches and taxis, because their VED rates are so small. For buses and coaches this might be considered reasonable since they are the only class of vehicle at present not covering their track costs. Stage passenger services would be protected from the derv duty increase by increased bus fuel grant. But the position of taxis would be harder to justify.

14. Cars and light vans which run on diesel fuel would suffer from the fuel duty increase, but it would be difficult to give them any corresponding reduction in VED. At present all cars and light vans bear the same duty rate. The creation of a new taxation class for diesel-driven vehicles would have implications for the administration and enforcement of VED. An increase in the tax burden on diesel-driven cars and vans would certainly slow the growth of diesel penetration, which is growing rapidly from a low base (at ^{the} end ^{of} 1985 diesel cars were 1 per cent of all cars, diesel vans 13.5 per cent of all vans, increasing at 53 per cent and 26 per cent a year respectively). It would look slightly odd in the light of publicity given recently to the new Rover diesel engine, likely to be introduced over the next year or so, which would concern DTI Ministers. There would also be an impact on small business distribution costs as a result of the effect on diesel-driven light vans.

15. There would also be implications for farmers' and showmen's lorries, whose VED rates are at present tied to the equivalent rate of duty for general lorries. The same ratios between

the rates could be maintained as at present, although this could cause difficulties with some very low duty rates. But because duty rates generally would be lower, the case for abolishing the concessions might be strengthened.

Timing and phasing

16. You would want to consider carefully the timing and phasing of any switch in the balance of lorry taxation. There are two aspects to this. First, large, sudden decreases in VED rates are bound to lead to complaints from persons who had just renewed their licences. They would be able to cash in their old licences and take out new ones at the lower rate, but that would cause a great deal of administrative effort for DVLC. It might be possible to phase in the VED and derv duty changes over a period, although this would have to be done carefully if the phasing were to be revenue-neutral. Customs and Excise also advise that advance warning of substantial increases in derv duty would lead to significant forestalling. Customs and Department of Transport would have to consider this further if a phased switch were to be undertaken.

17. The second aspect on timing concerns the price of derv. Both pump and bulk prices are at present some 14p to 16p below their level immediately before the 1986 Budget. If prices remain at their current levels, it would be possible to say that a shift in taxation in the 1987 Budget would still leave derv prices below pre-1986 Budget levels even if it were wholly passed on, which it need not be. So if a relatively sudden switch in the burden is to be made, the 1987 Budget might be a good time to do it.

Lead-free petrol

18. You are committed in next year's Budget to introducing a duty differential in favour of lead-free petrol. As derv is lead-free, a decision to narrow but not close the differential might point towards alignment of derv duty with the new unleaded

rate. Against this, derv is not unambiguously a "clean" fuel, given particulate emissions, and "offsetting higher production costs" (the reason for the unleaded petrol differential) does not apply, since derv is generally a cheaper fuel to refine than petrol. In addition, unleaded petrol will be of small revenue significance in the early years, and you may well wish to adjust the differential in the light of market pricing and uptake of the unleaded product. To maintain Budgetary flexibility, we would advise that the derv rate should not be formally tied to that on unleaded petrol, although, in the long term, that may be the more appropriate rate.

Conclusion

19. Raising derv duty to the level of petrol duty and making a corresponding reduction in lorry VED rates would have wideranging implications, and Ministers will want to consider the signal they would be sending, by ending the duty differential in favour of derv, to the motor and oils industries and consumers of diesel fuels, as well as the effects on VED. While the shift would link total lorry taxation more closely to mileage travelled, there would inevitably be losers as well as winners from the change. It should provide an incentive to more efficient use of fuel by lorries, although there would be disadvantages in environmental terms in reducing the present incentive to use diesel fuel rather than petrol. The switch would be marginally helpful in reducing the amount of VED evasion. It would help to improve the competitive position of UK hauliers in overseas markets, but would not help their position as against foreign hauliers in the UK market, because there is unlikely to be any significant increase in revenue from foreign hauliers. A switch as large as that implied by raising derv duty to the level of petrol duty would cause difficulties for the existing road track cost policy.

20. It seems unlikely that Department of Transport Ministers would support such a large shift from VED to derv duty as this proposal would involve. We understand that Mr Moore is likely to write to you about this after the recess.* If you wish this option to be pursued we would need to undertake a detailed

* In fact, he has just written - immediately below AWK

study of the pattern of lorry VED rates after the shift, and the transitional difficulties. Do you wish us to carry out this work?



K M ROMANSKI

PUMP
**EC DERV/PRICES (AT 23 JUNE 1986) AND VED RATES ON 38 TONNE,
 2 AXLE TRACTOR UNIT (JANUARY 1986)**

	Factor cost	DERV (pence)		VED
		Effective business tax burden	Total effective business price	£
Belgium	55	46	102	630
Denmark	58	29	87	2000
France	64	72	136	310
Germany	58	60	118	2460
Greece	46	17	63	520
Ireland	84	86	170	350
Italy	61	61	122	210
Luxembourg	55	28	83	330
Netherlands	52	24	76	960
Portugal	55	56	112	-
Spain	48	16	64	-
UK (current)	65	75	140	3100
UK (if derv duty aligned with petrol duty)	65	88	153	[1550]

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1. Alex
2. [Signature]

FROM: A W KUCZYS
DATE: 4 AUGUST 1986

AWK
TO
ROMANSKI

4/8

MR ROMANSKI

cc PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
PS/Minister of State
Sir P Middleton
Mr Monger
Mr Scholar
Miss Sinclair
Mr Cropper
PS/Customs & Excise

TAXATION OF LORRIES: SHIFT IN BALANCE OF TAXATION FROM VEHICLE EXCISE DUTY TO DERV DUTY

The Chancellor has seen your minute of 31 July, and the Transport Secretary's letter of the same date. In the light of this, he is prepared to amend his proposal in these terms:

To discuss, with Department of Transport, what is the largest switch from VED to derv duty in the 1987 Budget (and the Chancellor notes with approval your comment in paragraph 17 that the 1987 Budget might be a good time to make the switch) they can be made to wear? The arguments for doing a major switch far outweigh those against: that is clear. But what is also clear is that the Chancellor cannot accept Mr Moore's point that it is important to maintain or even increase the differential between the rates of duty on the two fuels, thus providing the headroom to bring down car VED. Even if the Chancellor were to make a switch from VED to petrol tax, it would inevitably be very much smaller than that for derv (probably a repetition of this year's manoeuvre), which means that the differential between derv duty and petrol tax is bound to diminish somewhat.


A W KUCZYS

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Pps

FROM: K M ROMANSKI

DATE: 20 August 1986

1. MISS SINCLAIR *M 20/8*
2. CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Mr Monger
Mr Scholar
Mr Cropper
Mr McGuigan C&E
Mr Wilmott C&E
PS/C&E

Ch
Letter to issue?

OK as per

AWK
22/8

TAXATION OF LORRIES: SHIFT IN BALANCE OF TAXATION FROM VEHICLE EXCISE DUTY TO DERV DUTY - LETTER FROM MR JOHN MOORE

Mr Moore wrote to you on 31 July seeking a shift in the balance of lorry taxation from VED to derv duty of about £100 million; and a similar shift in the balance of car taxation from VED to petrol duty.

2. Mr Kuczys' minute of 4 August recorded your interest in the former proposal. We are pursuing the ^{maximum} size of shift with Department of Transport officials as you requested, and will report further on this. But your view was that any shift from VED to petrol duty would have to be much smaller - probably no more than this year's.

3. A reply to Mr Moore on the general principles does not need to await the outcome of our investigations with DTp officials. I attach a draft letter for you to send at this stage.

4. There is one other issue which arises out of Mr Moore's letter, whether to consult ~~to~~ interested colleagues as he implies. Those primarily concerned would be the Secretaries of State for Trade and Industry (because of the effects on UK diesel vehicle production), Energy (energy policy implications of altering the differential between petrol and derv duties) and Environment (the pollution implications). The territorial Ministers might also have an interest. But their interests are secondary to the main issues, and we suggest that if

ROMANSKI
TO
CH/EX
20/8

you consider it necessary to consult them it would be better to do so at a later stage, when we have a firmer idea of the size of shift. The draft letter need not refer to consultation, as Mr Moore only mentions it in passing and is unlikely to be particularly concerned about it.



K M ROMANSKI

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

The Rt Hon John Moore MP
 Secretary of State
 Department of Transport
 2 Marsham Street
 LONDON
 SW1P 3EB

August 1986

Please type
 for C to send.

Thank you for your letter of 31 July about vehicle taxation.

So far as the taxation of lorries is concerned, I would agree that there are strong arguments for making a ^{major} shift from VED to derv duty, ^{including those} such as the ones which you mention. Depending on economic circumstances, notably the price of derv, at the time of the Budget, I would certainly be prepared to contemplate a ^{such a} large ^{significant} shift in the balance of the duties next year. I have asked my officials to look at this further with yours.

^{I do not believe it is politically possible to}
 On the taxation of cars, I ^{impliment a} think it would be more difficult to ^{major similar switch in the balance of taxation at one go.} carry out a large switch in the balance of taxation at one go, because of the political impact of a large increase in the petrol duty. But I would not rule out a ^{minor} switch, ^{along the lines of} perhaps like this year's, ~~and I shall bear your views in mind.~~

NIGEL LAWSON

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*PUP
Papers
Please*



FROM: M W Norgrove

DATE: 28 August 1986

MR ROMANSKI

cc PS/Chancellor
PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
Sir Peter Middleton
Mr Monger
Mr Scholar
Miss Sinclair
Mr Cropper
PS/Customs & Excise

TAXATION OF LORRIES: SHIFT IN BALANCE OF TAXATION FROM VEHICLE EXCISE DUTY TO DERV DUTY

The Minister of State has seen Mr Kuczys' minute to you of 4 August following your minute to the Chancellor and the Transport Secretary's letter of 31 July. He has commented that, as the theme of taxis runs through all these papers, it would seem worth having a little more knowledge of both their numbers and their fuel usage. The Minister recalls London taxis as being in excess of 10,000. He asks what the number is for the rest of the country, what fuel they use (variable?) and whether their fares are regulated outside London as they are by the Home Office in London. In either case, he would like to know how often they are regulated. His view is that London taxis must have been coining it latterly with lower petrol prices against fares fixed on higher prices.

A handwritten signature in black ink, appearing to be "M W Norgrove".

M W NORGROVE
Private Secretary

PS/MST
TO
ROMANSKI
28/8

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Treasury Chambers, Parliament Street, SW1
01-233 3000

cc CST
FST
MST
EST
Sir P Middleton
Mr Monger
Mr Scholar
Miss Sinclair
Mr Romanski
Mr Cropper
Mr McGuigan - C&E
Mr Wilmott - C&E
PS/C&E

28 August 1986

The Rt. Hon. John Moore MP
Secretary of State for Transport

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

Thank you for your letter of 31 July about vehicle taxation.

So far as the taxation of lorries is concerned, I would agree that there are strong arguments for making a major shift from VED to derv duty, including those you mention. Depending on economic circumstances, notably the price of derv, at the time of the Budget, I would certainly be prepared to contemplate such a shift in the balance of the duties next year. I have asked my officials to look at this further with yours.

On the taxation of cars, I do not believe it is politically possible to implement a similar switch in the balance of taxation at one go. But I would not rule out a minor switch, perhaps along the lines of this year's.

NIGEL LAWSON

CH/EX
TO
SS/DTP

28/8

pwj/p



*awaiting advice,
but might like
to be aware*

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

CR 11/9

JM/PSO/11150/86

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

8 September 1986

Dear Nigel,

I was grateful for your helpful letter of 28 August in reply to my earlier one about vehicle taxation. I recognise of course that any action on lorry taxation must also depend on other factors, most notably the price of derv, at the time of the Budget. Nevertheless, I am optimistic that some change will be possible and I am looking forward to seeing what your officials and mine come up with.

I am naturally a little disappointed that you think you will not be able to go as far on petrol as you might on derv, but I am encouraged to hear you are willing to contemplate a minor switch, along the lines of this year's.

I remain hopeful that nearer the Budget it may turn out that the political difficulties you envisage in going further are less daunting, and we may be able to do more.

John Moore
JM
11/9

JOHN MOORE

CH/EXCHEQUER	
REC.	10SEP1986
ACTION	MR ROMANSKI
COPIES TO	CST FST EST MST SIR P MIDDLETON MR LAVELLE MR SCHOLAR MISS SINCLAIR MR CROPPER PS/CtE

SS/DTP
TO
CH/EX
8/9

CONFIDENTIAL

The long wait for reply, but we need to go on here. I need further of 9(b), show no various options, with losses, RPI effects.

FROM: K M ROMANSKI
DATE: 5 November 1986

- 1. MISS SINCLAIR
- 2. CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
 Financial Secretary
 Minister of State
 Economic Secretary
 Sir P Middleton
 Mr Monger
 Mr Scholar
 Mr Cropper
 Mr McGuigan C&E
 Mr Wilmott C&E
 PS/C&E

*C/You are asked for your views in paragraphs 9 and 10 of cover note
 CR 7/11*

TAXATION OF LORRIES: SHIFT IN BALANCE OF TAXATION FROM VEHICLE EXCISE DUTY TO DERV DUTY

Mr Kuczys' minute of 4 August asked for advice on the maximum shift in lorry taxation from VED to derv duty which Department of Transport would be likely to accept. I attach a paper answering the question. The Annex to the paper addresses the MST's questions about taxis recorded in Mr Norgrove's minute of 28 August. The paper has been agreed with Department of Transport and Customs and Excise officials.

Size of shift

2. The paper's conclusion is that a £100 million shift in taxation is the maximum shift. There are two main reasons:

- a larger shift would lead to over-taxation of six-axled articulated lorries compared with five-axled vehicles of the same weight (perverse, since six-axled vehicles cause less damage);
- a larger shift would lead to a higher demand for refunds than DVLC could cope with, even taking on casuals, and would lead to unacceptable delays in processing all correspondence, not just refund applications.

ROMANSKI
 TO
 CH/EX
 5/11

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3. A shift of £100 million which was FSBR neutral would imply an increase in derv duty of about 7p per gallon, and varying reductions in lorries VED. The effect of such a switch would be to reduce the overall taxation borne by lorry compared with other motor vehicles. Overall, however, lorries would still pay more than enough in tax to cover their road track costs.

4. One of the difficulties with road track cost policy on lorries is that in some ways it cuts across other policy objectives. For example, trying to ensure that heavier lorries pay a larger excess over track costs than smaller ones does not sit easily with the relative treatment of lorries and private cars. The latter in fact pay a much larger excess over their track costs than the former in relative terms, but we presume that you would not want to increase the taxation on lorries substantially because of the implications for the industry. The disparity in treatment does, however, mean that a substantial reduction in the VED paid by a particular type of lorry could give rise to criticism.

Gainers and losers

5. Under the proposal for a £100 million shift described in the paper, the main gainers would be articulated lorries. All sizes of lorry would gain, but especially the larger ones. A 6-axled 38 tonne vehicle doing average mileage would pay £611 extra fuel duty per year, but have its VED reduced by £1140 - a gain of £529 per year. At £100, its VED rate would be the same as that on private cars.

6. The main losers would be:

- the larger rigid vehicles, which at present only just cover their track cost and underpay tax compared with articulated vehicles of similar weight;
- buses and coaches (although local bus services would be protected by the increase in bus fuel grant), but these

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do not at present cover their track costs and would still not do so even after the shift;

- **taxis**, which already cover their track costs, but whose VED cannot be reduced because it is tied to the rate for buses and coaches; there might be a case for reviewing the structure of VED on these vehicles, but Department of Transport Ministers do not wish even to consider this at present because of the state of flux in the bus industry at present; and
- **diesel-driven cars and vans**: reduction in their VED would involve the creation of a new taxation class which would create administrative and enforcement problems for DVLC.

7. If you consider that a VED rate of £100 for six-axled 38-tonne lorries is unacceptable, we can look at a higher figure - say £500 - in conjunction with Department of Transport. But this could mean either a smaller shift or that six-axled articulated lorries will have a higher excess over track costs than more damaging 5-axled ones.

Timing of shift

8. Our view is that a shift of £100 million should take place a single step and not be phased. DVLC can cope with the administrative effort of handling refunds with an additional 25 casual staff if the shift is limited to £100 million. Staging would not eliminate refunds, and some vehicles would apply for refunds at each stage. It would also cause extra administrative effort for DVLC in issuing revised tax tables during the year, and would lead to the danger of forestalling on derv as the duty increases would be known in advance.

Conclusions

9. Our conclusions are as follows:

- (a) We should accept that £100 million is the maximum shift;

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(b) The shift should be made on a ^PFSBR neutral basis (not a lorry neutral basis because this would require a larger increase in derv duty which would hit other diesel vehicles);

(c) We should not review the VED structure for buses, coaches and taxis;

(d) We should not introduce a differential VED in favour of diesel-driven cars and vans;

(e) The shift should take place in a single step and not be phased.

10. We would be grateful to know if you agree with these conclusions. We would also like to know whether you think a VED rate of £100 for six-axled articulated vehicles is acceptable; and if not, what figure you consider would be acceptable.

11. John Moore wrote to you about this on 8 September (copy attached). His letter does not specifically call for a reply, and we suggest that it would be better to await the outcome of the further work on six-axled 38-tonne lorries (if you want it to be done) before replying.



K M ROMANSKI

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TAXATION OF LORRIES: SHIFT IN BALANCE OF TAXATION FROM VEHICLES EXCISE DUTY TO DERV DUTY

This paper examines the implications of a shift in the taxation of lorries from vehicle excise duty to derv duty, and in particular the maximum shift which would be consistent with the policy which has been pursued on road track costs.

Road track cost policy

2. Road track costs include capital and current expenditure on national and local roads with the associated administrative expenditure, plus the costs of traffic policing and traffic wardens. Non-commercial vehicles are taxed on a surptuary basis - their taxation far exceeds their road track costs. But for commercial vehicles, policy is to keep the tax level much closer to the track costs, and to avoid tax-induced distortion of competition. For commercial vehicles the policy includes these three propositions:

- (a) fuel duty and VED paid for each category of vehicle should fully cover its track costs;
- (b) the surplus of taxation over track costs should be similar for vehicles of similar gross weights; and
- (c) the surplus should be larger for heavier vehicles.

Following the 1985 Budget, proposition (a) has been achieved for all main vehicle categories except the buses and coach group. Propositions (b) and (c) refer to the absolute size of the excess, and relate to the report of the Armitage Committee which recommended that any excesses should be concentrated on the heavier vehicles because of their greater environmental costs. These costs cannot be quantified, but do not necessarily relate to track costs - a given type of lorry could for instance do relatively little damage to the roads but be very noisy. Selective changes in VED rates in recent years have moved towards achieving (b) and (c) but they are not yet fully achieved.

Nature of shift

3. In order for the shift to be revenue-neutral in FSBR terms, the overall reduction in revenue on VED should be equal to the overall increase in derv duty less the increase in bus fuel grant which stage carriage service operators will receive automatically to compensate them for the higher fuel duty. On the assumption, which is discussed below, that VED rates for other diesel-powered vehicles - buses, coaches, taxis and cars - remain unchanged, a shift which was revenue-neutral overall would result in a reduction in lorry taxation equal to 20 per cent of the total shift. If lorry VED were reduced by £100 million, derv duty would need to be increased by £110 million, as bus fuel grant would offset £10 million of that increase. But derv duty paid by lorries would increase by only £80 million, the remaining £20 million net being borne by other diesel-driven vehicles.

4. A switch which was revenue-neutral for lorries would be possible, but it would require a larger increase in derv duty and would thus lead to bigger increases in the taxation of other diesel driven vehicles, unless reductions were made in their VED rates.

Size of switch

5. The underlying problem in any shift is a loss of flexibility as the element of taxation which can be varied according to the category of lorry is diminished. This flexibility is fundamental to a policy which aims to relate the total tax paid by different vehicles to track and other costs. At the moment the level of VED is sufficient to permit the achievement of track cost policies; and with a shift of £100m that would still be true. With a shift in excess of that, flexibility declines and it is no longer possible to relate the total tax paid by different types of lorry to the costs they impose on the infrastructure and environment.

6. Last July, when Department of Transport were considering the implications of the switch implied in the Chancellor's suggestion of raising derv duty to the level of petrol duty they foresaw difficulties for three broad vehicle groups:

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- a. Small rigid vehicles;
- b. Lighter articulated vehicles;
- c. Heavy six-axled articulated vehicles.

At the lower level of shift we are now considering, only the last poses serious problems. Small rigid vehicles could be accommodated within road track cost policy. There would be some anomalies for the lighter articulated vehicles, but there are very few vehicles in that category anyway.

7. So in determining the maximum size of switch it is the largest articulated vehicles (38-tonnes) which one has to look at. This group of vehicles is growing fast, frequently travels abroad, and is an increasingly vital element in road transport. Among 38-tonne lorries, the six-axled vehicles is assuming a growing importance. Because its weight is spread over more axles, it does less damage to the roads, and tax policy ought therefore to encourage its use. The difficulty is illustrated below. (We assume here that the switch is neutral in FSBR terms overall, which implies a reduction in total tax on lorries.)

A. Present position

<u>Axles</u>	<u>derv duty</u>	<u>VED</u>	<u>total tax</u>	<u>track cost</u>	<u>tax-cost surplus</u>
2+3	6877	3100	9977	8087	1890
3+2	7021	2730	9751	7802	1950
3+3	7021	1240	8261	6403	1858

In accordance with track cost policy, the surplus for the three types of vehicles are broadly equal. As costs reduce with the addition of axles, so the VED is reduced to balance.

B. Derv duty increased by £80m or 7p per gallon, VED reduced by £100m

<u>Axles</u>	<u>derv duty</u>	<u>VED</u>	<u>total tax</u>	<u>track cost</u>	<u>tax-cost surplus</u>
2+3	7475	1900	9375	8087	1289
3+2	7632	1460	9092	7802	1290
3+3	7632	100	7732	6403	1329

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Here again, the excess for all three types of vehicle is broadly equal. But this has necessitated bringing VED for the six-axle vehicle down to the private car rate - the irreducible minimum.

C. Derv duty increased by £110m or 10p per gallon, VED reduced by £140m

<u>Axles</u>	<u>derv duty</u>	<u>VED</u>	<u>total tax</u>	<u>track cost</u>	<u>tax-cost surplus</u>
2+3	7716	1650	9366	8087	1279
3+2	7878	1200	9078	7802	1276
3+3	7878	100	7978	6403	1575

The problem here is that derv duty paid by the 6-axle vehicle far exceeds track costs; this cannot be counterbalanced by a reduction in VED, since VED is already at its minimum level. It would be illogical and contrary to policy, to have a larger excess for the six-axle vehicle than for a five-axle vehicle of similar weight. A six-axle vehicle does less damage to the roads because its weight is spread more widely, so tax policy should not discourage its use.

8. We have considered whether a £140 million switch could not be accommodated by increasing the VED on 5-axles vehicles so that their surplus tax equalled that on 6-axled vehicles, with corresponding reductions elsewhere. But that would rectify one anomaly at the cost of introducing others, since it would mean that the excess on articulated vehicles was considerably greater than on rigid vehicles of a similar weight. It is also worth noting that many of the vehicles which take part in international traffic are five-axled thirty eight tonnes. As one of the aims of the shift is to help the international competitiveness of our vehicles, we would wish to keep VED on these vehicles as low as possible.

9. Even if the switch is limited to £100 million, the fact that the VED rate for 6-axled lorries would have to come down to the rate for private cars is a potential awkwardness. Although this can be justified in terms of the derv duty they pay, it would be a difficult argument to present to private motorists, since it would bring home

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to those not already aware of it the difference in their tax treatment, relative to their track costs, compared to that of lorries. If a rate of £100 for these lorries, particularly the heaviest ones, is unacceptable, it would be possible to impose a further constraint of a minimum VED rate for 38 tonne lorries of, say, £500. We would need to consider the implications of this with the Department of Transport. It could imply a smaller shift in the balance of taxation than £100 million, or else a worsening of the position of six-axled vehicles compared with 5-axled vehicles of the same weight, which would give the wrong signals to operators.

Gainers and losers

10. Since the heavier articulated lorry bears the biggest burden of excess taxation at present, that it is the group which would gain most; nearly all articulated lorries would benefit. The heavy rigid vehicles would be the main losers among the lorries - some of these only just cover their track costs at present. There would be some slight gainers and some slight losers among the lighter rigid vehicles.

Farmers' and showmen's vehicles

11. The shift in the balance of taxation away from VED to derv duty need not cause any change in the relationship between duty rates for these vehicles and ordinary lorries. Present plans are that the 1987 Budget should mark the third stage in aligning duty rates for farmers' vehicles over 7.5 tonnes at 60 per cent of the full rate; showmen's vehicles are already aligned at 25 per cent of the full rate. But in some cases higher rates than this implies would need to be levied to avoid obvious anomalies.

Buses and coaches

12. Buses and coaches would have to bear the increased derv duty. For stage carriage services this would be completely offset by the increased bus fuel grant. We see no case for reducing VED on buses and coaches as it is already very low, and they do not cover their road track costs at present. A £100 million switch would halve their

shortfall, to about £15 million (or 7 per cent of their track costs).

Taxis

13. The position of diesel taxis is more difficult (diesel taxis account for well over half the national fleet, and nearly all London taxis are diesel-powered). Taxis already cover their track costs, but as their VED rates are linked to those of buses and coaches, it would not be possible to reduce their VED to offset the derv duty increase. Although one possibility would be to review the structure of the buses, coaches and taxis class for VED, Department of Transport Ministers consider that in the present state of flux in the industry there is no case for deciding now whether to review it.

14. The increase in taxation of taxis would have to be defended on the grounds that taxis already have the lowest rates of VED except for motor cycles and agricultural tractors. In particular, they benefit from a lower rate than private motor cars.

15. The Minister of State asked some questions about taxis, which were set out in Mr Norgrove's minute of 28 August. These are answered in the Annex to this note.

Diesel cars and light vans

16. Diesel cars and light vans would also have to bear increased taxation unless a separate duty class was created for them. Assuming average annual mileage of 12,000 and 27 mpg on average a £100 million shift in taxation would imply a reduction of £30 in the car and light van VED rate for diesel vehicles if the derv duty increase were to be offset. However, introducing differential VED rates in the present private and light goods class would complicate the administration of the tax and create a new enforcement problem in stopping petrol vehicles using the cheaper diesel licence. The Department of Transport is strongly opposed to such a step. Without a special VED rate, a tax switch of the order contemplated would still leave diesel vehicles with a tax advantage, and DTp prefer this course.

VED refunds

17. The size of the switch affects the scale of the problem of VED refund problem. As VED rates for some categories of lorry will fall quite substantially, it is likely that it will pay lorry owners to apply for a refund on their old licences and then apply for a new licence at the lower rate. With a £100 million switch, some 240,000 lorries would have VED reductions. Of these, some 200,000 would benefit financially from obtaining a refund. Although in some cases the benefit might be too small to be worth the effort of claiming, the great majority can be expected to do so. To process these claims, DVLC would need 25 casual staff for about a month. The processing of all DVLC transactions (not just refunds) would be delayed by an average of two days, but these delays would be absorbed within 4 to 6 weeks. This would keep the problem within reasonable bounds.

18. Were there a switch of £140 million, the position would be very much worse. This is because the 290,000 vehicles below 7.5 tonnes which pay the £130 flat rate would have their duty reduced, in addition to the 200,000 who would benefit from a £100 million switch. This would mean that nearly 500,000 vehicles would benefit from a refund. To deal with such a demand would require more casual staff than DVLC could train or accommodate. Delays on all transactions would rise to an unacceptable level, from which it would take a long time to recover. There would be a considerable volume of complaints to Ministers about the delays. So practical considerations would also point to £100 million being the maximum level of switch.

19. We have considered whether staging of the switch might not give greater flexibility and permit a larger switch. But the difficulty is that although fewer vehicles might be involved in refunds, some vehicles would benefit from very large reductions, so their owners will be coming back for refunds several times. (Even if the reductions were staged at six-monthly intervals, they will probably find six-monthly licences unattractive because of the surcharge on them). The need to issue revised tax tables would be an added complication, so that the administrative effort for DVLC would not be eased by

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Staging. Customs and Excise also see considerable objections to staging the derv duty increase because of the danger of forestalling if the increases are announced in advance. They estimate that one week's forestalling of a 5p a gallon derv duty increase would cost around £2 million.

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TAXIS

1. Mr Norgrove's note of 28 August asked for information about taxis numbers and fuel usage, and also the position on fare regulation.
2. There were 32,700 licensed taxis in England and Wales at the end of 1985, of which 13,800 were in London. The DVLC census records 53,000 taxis in the United Kingdom. Apart from geographical coverage, the difference is accounted for by vehicles which do not ply for hire in the street and so do not require a taxi licence. It is estimated that about 30,000 of these taxis use diesel fuel and the remainder petrol. There is no comprehensive information available at present about mpgs and fuel, but some rather shaky figures can be deduced from local surveys. It is thought that taxis travel on average about 35 to 40,000 miles in a year. Diesel taxis average 30mpg and petrol taxis 25mpg. At current fuel duty rates, fuel duty per 1000 miles is about £25 for a diesel taxi and £35 for a petrol taxi. This contrasts with their track costs which are thought to be about £15 per 1000 miles. A £100 million increase in derv duty would leave diesel taxis slightly over £2 worse off per 1000 miles driven, or about £90 per year.
3. Ministerial responsibility for taxis and hire cars was transferred from the Home Secretary to the Secretary of State for Transport on 1 April 1984. London taxis are licensed by the Assistant Commissioner of the Metropolitan Police via the Public Carriage office, and their fares are controlled by the Secretary of State for Transport. In the rest of England and Wales, the decision whether to have a system of licensing taxis is up to the distinct council, although a taxi may not legally ply for hire in the streets without a licence. 85 per cent of district councils do in fact licence vehicles over all or part of their area; of these over 95 per cent also control fares.
4. It is true that the current level of fares for London taxis was set in relation to an oil price 12% higher than now obtains, and that this will have been to the taxi operators' advantage. But fuel accounts

for a comparatively small proportion (10%) of taxi operating costs.
The resulting cost advantage is therefore of the order of only 1%.

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I do not think we can go beyond a lorry-neutral switch - it will have a long-term effect on the balance of payments. (I take it this will mean an increase in the price of a gallon of oil - the price of a gallon of oil is £1.10 at present.)

FROM: K M ROMANSKI
DATE: 12 December 1986

- 1. MISS SINCLAIR (Discussed in draft)
- 2. CHANCELLOR OF THE EXCHEQUER

- cc Chief Secretary
- Financial Secretary
- Minister of State
- Economic Secretary
- Sir P Middleton
- Mr Scholar
- Mr Cropper
- Mr McGuigan C&E
- Mr Wilmott C&E
- PS/C&E

Do you want officials to draft a letter for you to send to John Moore?

cc 12/12

TAXATION OF LORRIES: SHIFT IN BALANCE OF TAXATION FROM VEHICLE EXCISE DUTY TO DERV DUTY

Mrs Ryding's minute of 10 November asked for further elaboration of the arguments on whether a shift in taxation from VED to derv duty should be PSBR-neutral or lorry-neutral.

ROMANSKI
TO
CH/EX
12/12

The options

2. We have examined this in the context of a switch, ie a reduction of lorry VED, of £100 million. A PSBR-neutral switch implies an increase in derv duty of £110 million as £10 million of the increase would be offset by increased bus fuel grants. Lorries would bear £80 million of the derv duty increase, and so would be £20 million better off overall. The lorry-neutral switch would require an overall increase in derv duty of £140 million, which would be offset by an increase of £15 million in bus fuel grant, so that the net gain to the Exchequer would be £25 million.

Gainers and Losers

3. The pattern of gainers and losers will be the same whether the switch is PSBR-neutral or lorry-neutral, but obviously the gainers will gain less and the losers more in the latter case, given the larger derv duty increase.

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4. The table below shows the difference between the FSBR-neutral and lorry-neutral position for various types of vehicle. (The figures are not consistent with those in my 5 November minute, because of Department of Transport have revised their track-cost and road-usage figures, but that does not affect the conclusions in that minute):

Vehicle	£ per year		
	Present tax position	FSBR-neutral switch	Lorry-neutral switch
<u>Lorries</u>			
2 + 3 axle, 30 tonnes	10302	9528	9687
3 + 2 axle, 38 tonnes	10076	9255	9417
3 + 3 axle, 38 tonnes	8586	8085	8247
4 axle rigid, 31 tonnes	6461	6812	6901
<u>Other vehicles</u>			
Diesel cars	524	557	565
Taxis	1048	1132	1157

The lorries shown are the largest gainers and losers. The difference would be smaller for other categories of lorry. Stage carriage buses would be unaffected by the choice of switch, since their derv duty is repaid through the bus fuel grant. Coaches would be affected, in a similar manner to taxis, but the precise effect cannot be quantified because Department of Transport do not have separate figures for coaches' mileages and mpgs.

5. In no case is the difference between the two options large - £160 for the largest articulated lorry. The choice between the two would be mainly presentational, were not for the first-year effects of a switch which Department of Transport have now identified.

Transitional effects

6. A switch which is neutral (however defined) in the long term, would result in a revenue shortfall in the year the change is made.

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This arises from the refunds which have to be paid on licences whose VED rates are reduced. Under the existing refund scheme where existing licences have to be cashed in and new ones purchased, Department of Transport advise that the loss could be as much as £150 million. Department of Transport are working on an alternative option which would involve making rebates to licence holders of the difference between the old and new rates for the unexpired portions of their licences. Existing licences would not have to be surrendered, so that the dates on which licences were renewed would not be affected. This would reduce the first-year revenue loss to £50 million. Such a rebate scheme would need legislative provision in the Finance Bill, and Department of Transport are looking at the administrative and legal aspects further, although their present view is that such a scheme would not require any additional casual staff to implement (as opposed to the refund scheme, which DVLC now think would require up to 100 casuals).

7. If a satisfactory rebate scheme can be worked^{out}, the £50 million shortfall would have to be recouped by a derv duty increase which was £25 million greater than that implied by the lorry-neutral switch. In effect, it would be necessary to get away from the concept of long-term neutrality in next year's Budget, in order to recoup the first year revenue loss from the first switch. Given the effect of bus fuel grants, the total increase in derv duty required would be £165 million.

8. In the context of next year's Budget we assume that you will also wish to raise additional revenue from this area equivalent to revalorisation of both derv duty and lorry VED. Last year you raised that amount all from derv duty, and it would be consistent with the aims of the shift in taxation to do so again. That implies a further £55 million on derv duty. The total increase in derv duty, compared to an indexed base, would be £180 million. The duty increase would be 13.2p, compared with 2.4p for revalorisation alone, both figures excluding VAT. Of that 13.2p, 6.6p would be attributed to the shift in the balance of taxation, and a further 3.3p to the need to recoup the first-year revenue shortfall.

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9. We have considered alternatives to recouping the first-year shortfall, apart from increasing the derv duty, but they do not look attractive. Refusing to give any VED refunds at all would be arbitrary in its effect, since it would penalise those who had just taken out licences at the old rates, whereas those whose licences happened to about to expire would get the benefit of the reduced VED immediately. Delaying the VED reductions would lead to considerably increased enforcement problems, as people will be reluctant to take out licences at a high rate of duty, when they know that a lower rate will shortly become available. And the contrast between the immediate derv duty increase and delayed VED reduction is presentationally unattractive.

RPI effects

10. You also asked about the RPI effects. Hitherto neither diesel fuel nor lorry VED figures in the RPI, so that the switch would have had no RPI impact effect. We now understand that Department of Employment are proposing to include diesel fuel in the RPI from next year. We do not yet know what the weighting will be. But as only the use of diesel fuel in private cars should be reflected in the RPI the weighting should be very small, so that the effect should be insignificant, even if the derv duty is increased as suggested in paragraph 7 above.

Conclusion

11. We have only recently been made aware of the first-year revenue loss from VED refunds. This strengthens the argument for making the change in a way which produces offsetting additional revenue in year one. It will mean a rather higher increase in derv duty than we had originally envisaged, about 13p per gallon. But at today's prices, this would still leave the pump price of derv below its pre-Budget 1986 level.

12. We recommend that the derv duty be increased by £165 million to offset the reduction of lorry VED by £100 million, and the first

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(apart from any consideration of revaluation of the duties)

year loss from refunds. This depends on Department of Transport being able to devise and introduce a system of rebates which will keep the first year loss down to £50 million.

13. If you agree with this and the conclusions of my minute of 5 November 1986, as to the option to be pursued, we will prepare a draft letter for you to send to Mr Moore to let him know of your thinking.



K M ROMANSKI



FROM: CATHY RYDING

DATE: 10 November 1986

MR ROMANSKI

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Mr Monger
Mr Scholar
Miss Sinclair
Mr Cropper
Mr McGuigan - C&E
Mr Wilmott - C&E
PS/C&E

**TAXATION OF LORRIES: SHIFT IN BALANCE OF TAXATION FROM VEHICLE
EXCISE DUTY TO DERV DUTY**

The Chancellor was grateful for your minute of 5 November.

2. The Chancellor has commented that your conclusions may well be right, but he would like further elaboration of 9(b), showing the various options, with winners and losers identified and also RPI effects.

C.R.

CATHY RYDING

CR
TO
ROMANSKI

10/11

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Mr. Scholar.

S. P. Middleton Agreed Em

I recommend that the Chancellor write as suggested: this issue is not, in my view, material in relation to the BA privatisation, and we need to make progress before Feb 6.

FROM: K M ROMANSKI
DATE: 18 December 1986

1. MISS SINCLAIR
2. CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Mr Scholar
Mr Cropper
Mr Wilmott (C&E)
Mr McGuigan (C&E)
PS/C&E

MS 18/12

C/OK for letter to issue? Officials had letter typed in final form for you to sign if content,


CR 18/12

ROMANSKI
TO
CH/EX
18/12

TAXATION OF LORRIES: SHIFT IN BALANCE OF TAXATION FROM VEHICLE EXCISE DUTY TO DERV DUTY

As requested in Mrs Ryding's minute of 15 December, I attach a draft reply to Mr Moore's letter of 8 September. We have drafted on the basis that a lorry-neutral switch involving a £100 million reduction in VED is your view at this stage, rather than a definite decision, particularly as Department of Transport have not yet finalised their consideration of the legal and administrative implications of the rebate scheme which would be needed to keep the first year revenue loss down to £25 million.

2. A lorry-neutral switch would, of itself, require a 8.2p increase in the duty on derv, which would imply a 9.4p increase in the pump price of derv. Revalorisation of the derv duty from the 1986 Budget level would add a further 2.4p on the duty, to make the duty increase 10.6p; a further increase on derv to compensate for non-revalorisation of lorry VED from current levels would add a further 0.9p, making the total increase in derv duty 11.5p, which would imply a 13.2p increase in the pump price. But so far as the draft letter is concerned, we consider that you need say no more that, quite apart from the switch, you will wish to consider the question of the appropriate levels of the duties. On past form, Mr Moore is likely to write to you about this in January anyway.



K M ROMANSKI

CONFIDENTIAL



cc
put
 CST
 FST
 MST
 EST
 Sir P Middleton
 Mr Scholar
 Miss Sinclair
 Mr Romanski
 Mr Cropper
 Mr McGuigan
 Mr Wilmott -
 PS/C&E

CH/EX
 TO
 SS/DTP
 19/12

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

The Rt Hon John Moore MP
 Secretary of State for Transport
 Department of Transport
 2 Marsham Street
 LONDON
 SW1P 3EB

19 December 1986

A handwritten signature in cursive script, appearing to read 'John Moore'.

Thank you for your letter of 8 September about vehicle taxation. I have delayed replying until I had seen the outcome of the work done by our officials on switching the balance of lorry taxation from VED to derv.

In the light of their work, I would be prepared to accept that we should be looking for a switch from VED to derv duty of £100 million, and that the switch should be neutral for lorries as a whole. The increased taxation on diesel driven cars and light vans and buses, coaches and taxis would help to offset the first-year cost of carrying out the switch. But a final decision will depend on your Department being able to devise and operate a system for dealing with the problem of refunds in such a way that the first-year cost of the switch is minimised, as well as any developments in the price of derv between now and the Budget. In addition, I shall wish to consider the appropriate level of these duties as part of my Budget judgement.

A handwritten signature in cursive script, appearing to read 'Nigel Lawson'.

NIGEL LAWSON

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH



From the Minister

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The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1P 3AG

EXCHEQU	
31 DEC 1986 3/12	
ACTION	P Walters
COPIES TO	CST, FST, EST, MST, Sir P Middleton 30 Sir G Lither, Sir T Burns, Mr Lawelle, Mr Morick, Mr Edwards, Mr Bugner, Mr Crabbe, Mr Mortimer, Mr Bonney.

December 1986

WAL

Dear Chancellor,

Very shortly I shall be writing to you giving my views on the tax law changes that I hope you will introduce in your Budget Speech. I shall be referring to the very serious situation now being faced by many farmers and to the importance this year of finding ways, through your tax proposals, of holding out a lifeline for the farming industry as farmers struggle to cope and to adjust to the cutbacks in production and to their funding problems.

My purpose in writing this letter is to give advance warning of one particular area where a modest measure could do much to demonstrate the Government's recognition of the difficulties now confronting our farmers. Far from easing, the pressures will surely increase as the reforms secured in Brussels work through. I refer to first year allowances in respect of capital expenditure on plant and machinery.

? You will recall that one of the reasons you gave when you announced the phasing out of first year allowances was that they had been used for tax avoidance purposes. My experience, however, is that few farm businesses and certainly the smaller family businesses, have ever been guilty of the purchasing of unnecessary machinery. Indeed, because of the great technical improvements made by agriculture over the years, the ability to purchase suitable machinery has become an essential component in the productivity achievements of the industry. And I should add that the bulk of farm businesses, being unincorporated, gained nothing from the reduction in the rate of Corporation Tax. In the circumstances, I would urge you to give special consideration to the introduction of a new 100% first year allowance on say the first £30,000 of expenditure on plant and machinery. Such an arrangement would particularly assist the smaller family farm. It is a concession I would envisage applying generally to provide further encouragement to the growth of all small businesses.

Yours sincerely,

Elizabeth Tomis

for MICHAEL JOPLING
(approved by the Minister and
signed in his absence)



FROM: A W KUCZYS
DATE: 5 January 1987

es

MR WALTERS

cc PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
PS/Minister of State
Sir P Middleton
Mr Monck
Mr Cassell
Mr Scholar
Miss Sinclair
PS/IR

CAPITAL ALLOWANCES: SMALL FARMS

You have the action copy of Mr Jopling's letter of 30 December to the Chancellor. The Chancellor's comment is "not on".

AWK

A W KUCZYS

SECRET

B/F 26/1

ROMANSKI
TO
CH/EX
5/1

COPY NO 1 OF 26

FROM: K M ROMANSKI

DATE: 15 January 1987

1. MR SCHOLAR
2. CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Sir Peter Middleton
Sir Geoffrey Littler
Sir Terence Burns
Mr F E R Butler
Mr Cassell
Mr Monck
Mr Sedgwick
Mr Odling-Smee
Miss Sinclair
Miss Evans
Mr Cropper
Mr Ross Goobey
Mr Tyrie
Sir Angus Fraser (C&E)
Mr B Knox (C&E)
PS/C&E
Mr Battishill (IR)
Mr Isaac (IR)
PS/IR

*cd Smithy review
Same as petrol - 5.3p -
have 700 some suggest
advised was when
short price, however
* pres. approx 7/12 on*

BALANCE OF VEHICLE TAXATION: VED AND FUEL DUTY

You asked at Chevening for a paper setting out the arguments for and against a switch in the balance of vehicle taxation from VED to fuel duty, and the effects of such a switch.

Lorry taxation

2. The present proposal for lorry taxation is that there should be a reduction of £100 million in lorry VED which would be lorry-neutral. Because of the transitional cost implied in giving rebates of VED where duty rates are reduced, there would be a net £25 million revenue loss in the first year, but the shift would produce a £25 million revenue gain in subsequent years. The effect of a £100 million lorry-neutral shift on derv prices, together with the effects of revalorisation (using the 3.7 per cent inflation factor from the December RPI) would be as follows:

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	Duty	p per gallon VAT	Price
1. Effect of shift.	8.2	1.2	9.4
2. Revalorisation of derv	2.8	0.4	3.2
3. Compensation for non-revalorisation of VED (except cars)	1.1	0.2	1.4
TOTAL	12.1	1.9	14.0

(Figures may not add due to rounding.)

This equates to a 16.3 per cent increase in derv duty.

3. The main arguments in favour of a shift in lorry taxation are:

(a) it would link total taxation more closely to mileage travelled;

(b) it would encourage more efficient use of fuel;

(c) it would help the international competitiveness of UK hauliers - UK lorry VED is the highest in the EC;

(d) it is sometimes argued that it would enable more revenue to be raised from foreign hauliers operating to the UK - but in practice we allow all fuel in the standard tanks of lorries entering the UK to be admitted duty- and VAT-free, and standard tanks generally contain sufficient fuel for foreign lorries to do virtually all their UK mileage without refuelling in the UK; and

(e) the significance of VED evasion - currently about £20 million for lorries, or about one fifth of total VED evasion - would be reduced, but there is unlikely to be any great effect on the rate of evasion.

4. The main arguments against a large shift in taxation are:

(a) the increase in the price of derv which would result - 14.0p, including the effect of revalorisation and compensation for non-revalorisation of lorry VED - is a large figure. It would affect all derv-users not just lorries. But on current prices it would still leave the pump price of derv about 10p below the pre-1986 Budget price of derv (though oil companies have indicated pending increases of about 6p per gallon). It is worth noting that the UK pump price of derv is already the highest within the EC, except for the Republic of Ireland and Denmark, and in the bulk market, responsible for 80 per cent of UK derv sales, the increase could raise UK effective prices, now mid-way between those of Germany and France, to 5 per cent above those of France and make them the second highest in the EC after the Republic of Ireland;

(b) as derv is to be included in the RPI whereas lorry VED is not, the shift will have some RPI impact. A decision on the weighting within the RPI has not yet been taken (it should be within a couple of weeks) but any conceivable increase in derv duty is most likely to have a negligible effect, ie less than 0.005 per cent;

(c) there is a first year revenue loss of £25 million compared to revalorisation which would have to be made good elsewhere if you wish to have an excise duty package which produces the equivalent of revalorisation overall (recouping it from petrol duty would add a further 0.5p to the petrol price);

(d) the package of lorry VED rates proposed by Department of Transport to reflect road track costs would produce some very large reductions in duty on the heaviest articulated vehicles - the duty on a six-axled 38 tonne vehicle would be reduced to £100, the same as the rate for cars. This might be controversial and could draw attention to the extent to which car VED exceeds car road track costs;

(e) the contrast with the proposed treatment of cars (see below) may be seized upon by those who favour abolition of car VED; and

(f) there could be industrial implications for UK vehicle manufacturers of diesel-driven vehicles whose total tax burden is increased by the shift, both absolutely and relative to competing petrol-driven vehicles eg cars, vans and taxis.

Car taxation

5. If you decided not to revalorise car VED but to recoup the revenue foregone from petrol duty, the effect on petrol prices would be as follows:

	Duty	p per gallon VAT	Price
1. Revalorisation of petrol duty	3.3	0.5	3.7
2. Compensation for non-revalorisation of VED	1.3	0.2	1.5
TOTAL	4.6	0.7	5.3

(Figures may not add due to rounding.)

This equates to a 5.2 per cent increase in petrol duty.

The position in the petrol market is at present unsettled, with different companies announcing different increases from different dates, but the present round of increases is likely to raise the average pump price of petrol from around 168p per gallon to its ^{now} pre-1986 Budget price of 174p, or perhaps a little more, with a second round of increases threatened in due course.

6. The arguments for and against a shift are not all the same for cars as for lorries. So far as the arguments for are concerned, encouragement of a more efficient use of fuel applies equally, and reducing the significance of VED evasion is perhaps more important given the greater revenue at stake. For cars, however, linking total taxation more closely to mileage travelled is something of a two-edged sword. Although it could be defended as more equitable, it will hurt essential car users, such as business users and some rural dwellers. The international arguments do not apply to a switch in car taxation.

7. Of the arguments against, apart from the effect on essential users, the effect on price has to be considered - the petrol price is now significantly higher than that of derv, whereas before the 1986 Budget they were broadly the same. Although the AA are now arguing that any increase in motoring taxes should be on petrol duty, not VED, VED has generally been perceived as a less unpopular tax than petrol duty. To raise equivalent revenue from petrol duty

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is very slightly less RPI efficient than from VED - recouping a standstill on car VED from petrol duty would increase the RPI by 0.01 per cent more than revalorisation of both duties.

Conclusions

8. On lorries the main argument for reconsidering the £100 million switch is the 14.0p increase it implies in the price of derv. One possibility would be to go for a smaller switch - say £50 million, which for a lorry-neutral increase would limit the derv increase to 9.2p. Or the shift could be limited, as last year, to leaving lorry VED rates unchanged and recouping the loss from derv duty. This would result in a 4.5p increase in derv duty and would also save 8 pages of Finance Bill space (in the Schedules).

9. On cars there seems to be no reason for any shift larger than that implied by a VED standstill. That implies a 5.3p increase in petrol taxation, compared to 3.7p for revalorisation. But even if the petrol price does increase as forecast, petrol could still bear such a tax increase.

10. You wrote to John Moore on 19 December to say that you were prepared to consider a £100 million shift in the balance of lorry taxation. I understand that he will be writing to you shortly about that and with his proposals for car VED. If you decide that you do not wish to pursue the switch, we could provide you with a draft letter to send to him, or you could await his letter to you.



K M ROMANSKI



DEPARTMENT OF HEALTH AND SOCIAL SECURITY
 Alexander Fleming House, Elephant & Castle, London SE1 6BY
 Telephone 01-407 5522

From the Secretary of State for Social Services

The Rt Hon Nigel Lawson MP
 Chancellor of the Exchequer
 HM Treasury
 Parliament Street
 LONDON
 SW1P 3AG

19 11 87
 MR WALTER 1911
 CST, FST, EST, MST
 SIR P. MADDLETON
 MR SCHOLAR
 MISS SINCLAIR
 MR ROMANSKI
 MR CROPPER

66 January 1987
 MR ROSS-GOOD
 MR TYRRE
 PS/CBE
 MR KNOX

Nigel

EXCISE DUTY ON ALCOHOL

I am writing to you to urge you to take the public health aspects of alcohol prices into account when you are considering excise duty levels for 1987 Budget.

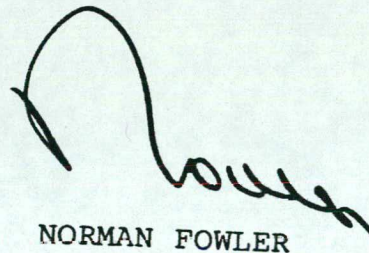
Consumption of alcohol has resumed its upward trend and indicators of alcohol-related harm continue to rise. I am disturbed that the main indicators of harm - deaths from chronic liver disease and cirrhosis, admissions to NHS psychiatric hospitals and discharges from non-psychiatric hospitals on account of alcohol-related illness - have risen to record levels: clearly alcohol misuse is placing an added burden on the health service. Research commissioned by my Department suggested that the cost of alcohol-related harm to the health service was at least £100 million a year at 1983 prices and the cost to industry over £600 million a year for sickness absence alone. These are factors we cannot afford to ignore. I know that colleagues at the Home Office are concerned about levels of alcohol-related violence and under-age drinking and that Peter Bottomley has already written to Peter Brooke urging increases in excise duty as a preventive measure in his campaign against drink driving. I myself am increasingly worried about violent attacks on health service and social security staff at least some of which appear to be alcohol related.

Since the last Budget, there has been an increasing wave of criticism of the Government for its failure to take alcohol-related problems seriously. Recently, the Royal College of Psychiatrists and General Practitioners and the British Psychological Society have all published reports which recommend that more should be done to curb alcohol abuse. The Royal College of Physicians will also

produce a report in February which we believe will take a similar line. I am holding a conference on the prevention of alcohol misuse in February which is intended to demonstrate our commitment to the sensible use of alcohol. This will focus upon ways in which we might encourage sensible drinking habits. However, failure to raise excise duties for a second year running would be seen as a clear indication that the Government did not intend to take this problem seriously.

I am aware that the increase in alcohol consumption since last year has taken place despite a rise in alcohol prices. My officials have examined this carefully and we believe that consumption levels are more closely related to levels of personal disposable income than to price per se. Disposable income has risen more rapidly than inflation. I appreciate that increases which matched those in disposable income would be very substantial and that other factors have to be taken into account. However, on health grounds, I must ask that increases in excise duty be pitched at levels which raise prices by rather more than the Retail Price Index. Our greatest concern is with beer consumption, which still accounts for the majority of alcohol drunk in this country and for the major part of alcohol-related harm.

On a final point, I understand that your officials have been examining proposals to reduce levels of taxation on some low alcohol beer and wine. This has been presented in some circles as a useful health promotion measure. However, the issues involved are very complex and depend a great deal upon the way in which a low alcohol product is marketed. I hope that if such proposals are to be seriously considered, there will be an opportunity for further discussion of the health implications.



NORMAN FOWLER



CH/EXCHEQUER	
REC.	19 JAN 1987
	MR WALTER ^{all}
	EST, FST, EST, MST
	SIR P. MIDDLETON
	MR SCHOLAR
	MISS SINCLAIR
	MR ROMANSKI
	MR CROPPER
	MR ROSS-COOBEN
	MR TYRIE
	PS/C&E, MR KNOX C&E
	January 1987

DEPARTMENT OF HEALTH & SOCIAL SECURITY
 Alexander Fleming House, Elephant & Castle, London SE1 6BY

Telephone 01-407 5522

From the Secretary of State for Social Services

The Rt Hon Nigel Lawson MP
 Chancellor of the Exchequer
 Treasury Chambers
 Great George Street
 LONDON SW1

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 16/11

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Nigel

TAXATION OF TOBACCO PRODUCTS

Cigarette smoking remains the single most important cause of preventable disease and death in this country. Smoking-related illnesses account for some 15 per cent-20 per cent of all deaths in the UK. Although cigarette consumption continues to decrease and encouraging progress has been made over the past years in persuading people to give up smoking - only about one-third of the adult population now smoke - the overall figures mask the rising problem of smoking among young people. If significant progress is to be made in reducing the unacceptably high level of smoking-related deaths and disease, and the associated drain on national resources, this flow of new recruits to the smoking habit must be stemmed.

Recent evidence has suggested no improvement in the numbers of young people starting to smoke, the age at which they start, the numbers of cigarettes they smoke, or the numbers giving up. The 1984 survey of smoking among secondary schoolchildren by OPCS, for example, suggested a disturbing increase in smoking among 11-15 year olds. Forty-one per cent of 5th year school-children were reported as smokers.

A more recent survey is on a smaller sample size, and although the results are not statistically significant they show young smokers as having increased their daily consumption of cigarettes by three per cent over the past year as compared to a five per cent reduction for the overall smoking population. The situation is particularly

E.R.

worrying where young women are concerned. Historically, smoking by women was at its peak during the 1950s and 1960s. There has been a slow decline of smoking among women in general since then, but the latest survey actually shows an increase amongst young women (aged 16 - 24) from 28 per cent in 1985 to 32 per cent in 1986. If this were reflected nationally it would mean that 160,000 more young women are now smokers. Furthermore, the number of cigarettes per day smoked by women in this age group is reported as having increased by 4 per cent over the same period.

The legacy of the increase in smoking amongst women in the 1950s and 1960s has been a 20 per cent increase in lung cancer in women since 1979. Lung cancer now looks set to overtake breast cancer as the leading cause of death from cancer among women; we are expecting over 10,000 deaths from lung cancer among women this year. If more young women are not dissuaded from starting smoking, or persuaded to give up, it seems certain that we shall be faced with further increases in the smoking-related ailments among women of which lung cancer and coronary heart disease (also on the increase) are the biggest killers.

A substantial increase in the price of cigarettes would help reduce smoking among all age groups. Its greatest effects may well be amongst the lower end of the 16 - 24 year bracket, that is teenagers with their relatively limited financial resources. It might be thought that following recent rises in duty the public appetite for further tax increases would have diminished. In fact, the opposite is true. In the NOP survey carried out in 1985, 43 per cent said they would approve of the Government increasing the tax on cigarettes and 33 per cent said they would disapprove. In the 1986 survey the level of approval has increased to 48 per cent while the level of disapproval has decreased to 30 per cent. This trend is even stronger amongst smokers.

Because of the strong health arguments, and since there is good evidence to suggest that such a measure would be widely supported by the public, I hope you will find it possible to make a substantial increase in duty on cigarettes in the forthcoming Budget. Last year you referred in your Budget speech to the health reasons underlying the increase in duty on cigarettes. A reaffirmation this year would be very welcome.

A copy of this letter goes to Malcolm Rifkind, Nicholas Edwards and Tom King.

John *exo* *Norman Fowler*

NORMAN FOWLER



DEPARTMENT OF HEALTH AND SOCIAL SECURITY
 Alexander Fleming House, Elephant & Castle, London SE1 6BY
 Telephone 01-407 5522

From the Secretary of State for Social Services

The Rt Hon Nigel Lawson MP
 Chancellor of the Exchequer
 HM Treasury
 Parliament Street
 LONDON
 SW1P 3AG

CH/EXCHEQR	
DATE	19 JAN 1987
TO	MR WALTER ¹⁹¹¹
COPIES TO	CST, FST, EST, MST SIR P. MADDLETON MR SCHOLAR MISS SINCLAIR MR ROMANSKI MR CROPPER
January 1987 MR ROSS-GOODEY MR TYRRE PS/C&E MR KNOXCE	

16/1
 6

Nigel Lawson

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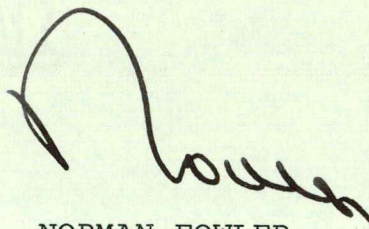
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A handwritten signature in dark ink, appearing to be the name "John". The signature is stylized, with a large loop at the bottom and a small flourish at the top.A handwritten signature in dark ink, appearing to be the name "Norman Fowler". The signature is written in a cursive style with a large, sweeping initial "N".

NORMAN FOWLER



CH/EXCISE
19 JAN 1987

DEPARTMENT OF HEALTH & SOCIAL SECURITY MR WALTER
Alexander Fleming House, Elephant & Castle, London SE1 6BY
Telephone 01-407 5522
From the Secretary of State for Social Services

EST, FST, EST, MST
SIR P. MIDDLETON
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MISS SINCLAIR
MR ROMANSKI
MR CROPPER
MR ROSS-COOBEN
MR TYRIE
PS/CBE, MR KNOX CBE
16 January 1987

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
Treasury Chambers
Great George Street
LONDON SW1

Nigel

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John *exo* *Norman Fowler*

NORMAN FOWLER

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

BR



From the Minister

CONFIDENTIAL

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1P 3AG

CH/EXCHEQUE	
REC.	19 JAN 1987
COPIES TO	

RECEIVED	19 JAN 1987
ACTION	Mr Walker PP
	cc APS/CHX.
SIGNATURE	CHX
REF No.	10786/87
19 January 1987	

At this time of year it is usual for my officials to submit to your officials in the Inland Revenue a Memorandum outlining our views on possible changes to the taxation system. This year, in view of the changes now facing agriculture, I feel I must draw directly to your attention the contents of the Memorandum itself.

It is now abundantly clear to all of us that the farming industry is in the midst of a period of fundamental adjustment. The package of measures I secured in Brussels in December will inevitably mean more changes for our farmers, particularly those in the dairy and beef sectors, which tend to be concentrated in the north and west. Diversification of farm businesses will be the answer for many of them and a way of assisting this process would be through the tax system. Therefore I have set out in the attached note a number of suggestions which I ask you to consider.

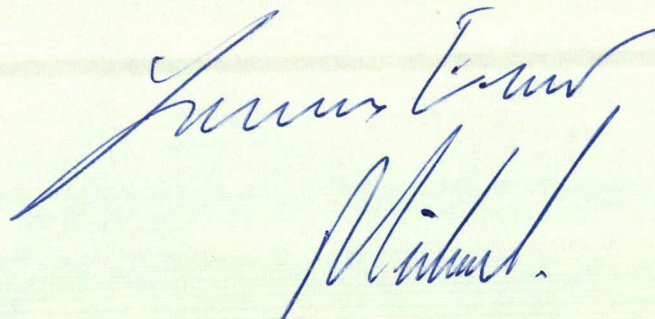
If implemented, the proposals I have outlined would give a signal to farmers, landowners and to the rural community as a whole that the Government is indeed willing to assist the adaptive process now under way. Some of my suggestions are designed specifically to encourage farmers and private agricultural landlords, to take a full part in sustaining the rural economy. There is little doubt that the success of our rural strategy will have to depend heavily on their enterprise.

Of the points detailed in the memorandum the major items are clearly capital allowances for plant and machinery on which I have already

/written you,

written you, the removal of the inflationary penalty from Capital Gains Tax and the recognition of private agricultural landlords as businessmen and of their important contribution to the rural economy.

On the excise duty front I understand that as in past years my officials will be meeting officials from Customs and Excise. I shall write to you further on that subject in the light of this meeting.

A handwritten signature in blue ink, appearing to read "James Evans" on the top line and "Michael" on the bottom line. The signature is fluid and cursive.

MICHAEL JOPLING

CONFIDENTIAL

TAX LAW CHANGES : MEMORANDUM BY THE MINISTRY OF AGRICULTURE,
FISHERIES AND FOOD

INTRODUCTION

1. This Memorandum sets out the changes in tax law affecting agriculture and horticulture which the Ministry would wish to see in the 1987 Finance Bill.
2. Agriculture now faces a period of considerable change. It is now clear that milk production will be further reduced over the next 2 years, the support arrangements for beef are to be weakened, whilst for cereals, steps to curb the escalation of stocks will be inevitable over the next year or so. The industry faces this future at a time when its income is depressed and its balance sheet is weakening. In 1985 aggregate farming income fell to the lowest level in real terms for many decades and 1986 will see only a modest recovery. Borrowing continues to rise - much of it for working capital - but servicing this debt from squeezed income is becoming a serious problem for many farmers, particularly those on smaller family farms. Investment has fallen and more and more farmers are looking for opportunities to generate cash flow from non-farming activities. Further labour shedding, with its impact on the rural infrastructure, is anticipated.
3. Faced with this situation, and the need to provide farmers with every reasonable opportunity to enable them to cope with the adjustments, the following proposed tax changes concentrate on measures that would:-
 - (1) assist the smaller family farm by the introduction of a limited first year capital allowance, designed to help the development of small businesses generally;
 - (2) remove anomalies from Capital Gains Tax which are bearing particularly heavily on farmers;

- (3) encourage private agricultural landlords to let farms, thus assisting the introduction of new blood to the industry;
- (4) do away with a measure which penalises farmers, but no-one else, relating to the treatment of trading income;
- (5) encourage the sale of parcels of poorer land to conservation bodies.
- (6) allow the concession on holiday letting to apply more fairly to the remoter areas.

CAPITAL ALLOWANCES

4. There is little doubt that the withdrawal of first year capital allowances, when the agricultural industry faced the most difficult economic situation for many years, hindered the industry's adaptation and diversification. When the withdrawal of the allowances were announced in 1984 it was explained that this should be seen as a quid pro quo for reform of company taxation. It was explained that the allowances reflected outdated economic priorities or circumstances and served to distance a firm's investment decisions from tax planning strategies. But it should be noted that the small to medium size farm business seldom possesses the spare resources to allow it to invest in unwanted farm machinery for tax planning purposes so that purchasing decisions are invariably taken on the basis of need. Moreover, as only 5% of farming businesses are incorporated, some 95% gained nothing from the reductions in the rate of Corporation Tax.

5. In the view of the Department the present economic priorities and circumstances call for help to be given to small to medium size farm businesses to help them invest in essential plant and machinery necessary for the adjustments they will need to make. For example one medium size tractor might cost some £20,000 and a medium sized combine harvester more than double that sum, and therefore we recommend that, say, £30,000 would be a realistic level at which to set a new 100% first year allowance. Such an allowance would be aimed at all small businesses whether in farming or not. Agreement to such a proposal would provide a very real boost to the development of new small businesses which form an essential plank of the Government's economic and employment policies.

6. The introduction of optional balancing charges or allowances in respect of expenditure on agricultural buildings has been welcomed by the agricultural industry although few are likely to benefit. A particular difficulty faced by agriculturalists and horticulturalists is that once buildings have been erected there is little incentive to demolish them and return the land to a green field site even though the original and often specialised, purpose of the buildings has long since disappeared. For example, many who constructed new dairy parlours three or four years ago might now find them redundant because of milk quotas. As quotas are further reduced more farmers will find, under the present tax regime, they will have to wait for almost 25 years before benefiting from the full capital allowances even though the building will have no dairying function. We suggest that consideration be given to ways of overcoming such a disadvantage where it can clearly be shown that the building can no longer be used for its intended purpose and is of limited value to the farm business.

CAPITAL GAINS TAX

7. Between the introduction of Capital Gains Tax in 1965 and the provision for indexation in the 1982 Budget, the Retail Price Index rose by 548%. Over the same period agricultural land prices increase by 750%. Unlike many other business resources, agricultural land is usually retained for very long periods. It therefore follows that farmers and private agricultural landlords have been badly affected by the continuing retention of such a substantial inflationary element in CGT. As a result, CGT has acted as a disincentive to the taking of sound business decisions, particularly necessary at the present time when the industry is adjusting to financial pressures. The Department considers that steps should be taken this year to relieve the agricultural industry of some of the inflationary content of CGT.

8. It is therefore suggested as our first preference that the base date from which increases in value are calculated should be brought forward progressively from 1965 towards the 1982 indexation date. As an alternative, an automatic cut-off could be introduced so that CGT would not apply when an asset had been held for, say, 10 years.

9. Our second preference relates to the present provision under which small, part disposals of agricultural land, escape CGT up to a monetary limit of £20,000. This brings very limited benefit to agriculture. In current circumstances, a farmer of long standing, faced with bank servicing charges which he is unable to meet, may well wish to sell off a portion of his agricultural land. But the £20,000 limit would rarely apply and so the farmer would be faced with a CGT bill to add to his financial pressures. This is a further example of the way the tax system acts as a disincentive to agricultural restructuring. We therefore urge that the monetary limit be raised to at least £50,000.

10. Our third point concerns the annual CGT exemption of £6,300. Owners of land are generally unable to take advantage of this annual exemption. The reason is that it is not feasible for them to dispose of farm land in small annual parcels. They are therefore disadvantaged compared with those owning readily realisable assets such as stock exchange securities. It is therefore suggested that landowners should be able to carry forward unused annual allowances for a number of years.

11. A further example in which CGT acts against what can be sound business decisions is where a farmer who is an owner-occupier decides to retire from farming but wishes to continue living in the farm house and to retain the ownership of his land. In such circumstances he may well wish to let the land, perhaps to a new entrant to farming. However, he is discouraged from so doing as this would immediately mean loss of his business status; he would be deemed to have become a landlord and therefore ineligible for retirement relief. Such fiscal measures can therefore work against present Government policies of encouraging the letting of land and the introduction of new blood into the industry. We suggest that retirement relief be allowed in such circumstances.

AGRICULTURAL LANDLORDS

12. Despite changes introduced by the Chancellor in recent years, the tax system continues to interfere with the process whereby private agricultural landlords let land to tenants, such letting being essential if the agricultural industry is to be broadly based. Indeed, the letting of agricultural land to tenants provides one of

the few ways in which able, young people can start out on their own. However, since 1961 the proportion of farms in Great Britain, wholly or mainly tenanted, has fallen from 46% to 29% of the total. The trend continues and in our view needs to be halted.

13. The role of the private agricultural landlord is usually quite different from that of his urban counterpart. He is often intimately involved with his tenants in planning the farming programme, in funding farm improvements, in planting woodlands as well as funding essential maintenance work. The private agricultural landlord is therefore closely engaged in running a business, as are his tenants. Indeed, in the economic climate now facing the industry the role of the landlord has become even more crucial, as tenants look for ways to diversify their businesses and look to the landlord for assistance. The Department therefore urges that private agricultural landlords be treated for tax purposes for what they are, normal businessmen. This would involve allowing such landlords to claim those reliefs available to owner-occupiers and tenant farmers, in particular retirement and roll-over reliefs against CGT and the ability to recover VAT on repairs and maintenance to tenanted buildings. Such a step would be an important factor in easing the industry's adaptive process.

INCOME TAX

14. Agriculture remains the only industry sector where restrictions are imposed which prevent farmers and growers from setting their farm business losses against other trading income when farm losses occurred for more than five consecutive years. While it is recognised that the original intention was to guard against abuses of the tax system by so-called hobby farmers, in present circumstances farmers are being prevented by it from acting like any other businessmen in supporting one form of trade by their involvement in another. This anomaly can deter farmers from diversifying their farm businesses into non-agricultural enterprises. Moreover, faced by heavy servicing costs for their farm businesses and the current pressures on farming profitability, it is now much more likely that a significant number of farms will be facing trading losses for a number of consecutive years. We therefore recommend that section 180 of the Income and Corporation Taxes Act 1970 be repealed.

CONSERVATION

15. At a time when the Government is anxious to assist rural conservation, it would clearly be appropriate to extend to additional bodies the extra statutory concession which allows land of outstanding national interest to be sold at a special price to bodies such as the Nature Conservancy Council. The list of bodies that currently benefit from this provision are found in paragraph 12 of Schedule 6 to the Finance Act 1975. When it was drawn up conservation had a much lower priority than it has today. In view of the considerable public interest in the conservation of the countryside, we suggest that important organisations such as the Royal Society for the Protection of Birds and the Royal Society for Nature Conservation among others be allowed to take advantage of this "douceur" system. We therefore recommend that consideration be given to the identification of suitable bodies to be added to the Schedule.

HOLIDAY LETTING

16. Farm tourism can make an essential contribution to the profitability of the farm, particularly in remote areas. However, despite the concession on holiday letting contained in the Finance Act 1984, in such areas it can be virtually impossible for holiday lettings to be secured for the necessary minimum qualifying period of 70 days. The Department considers that a much more realistic minimum period would be 50 days. In addition to the qualifying period the tax provision requires that the property shall be available for commercial letting for 140 days. A period of 100 days would be more realistic for the remoter areas.

16 JANUARY 1987



From the Minister

CONFIDENTIAL

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1P 3AG

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

tab RJS BR

19 JAN 1987

DATE	19 JAN 1987
ACTION	Mr Walker's
	CC APS/CHX
SIGNATURE	CHX
REF No.	10786/87
19 January 1987	

Nigel Lawson

At this time of year it is usual for my officials to submit to your officials in the Inland Revenue a Memorandum outlining our views on possible changes to the taxation system. This year, in view of the changes now facing agriculture, I feel I must draw directly to your attention the contents of the Memorandum itself.

It is now abundantly clear to all of us that the farming industry is in the midst of a period of fundamental adjustment. The package of measures I secured in Brussels in December will inevitably mean more changes for our farmers, particularly those in the dairy and beef sectors, which tend to be concentrated in the north and west. Diversification of farm businesses will be the answer for many of them and a way of assisting this process would be through the tax system. Therefore I have set out in the attached note a number of suggestions which I ask you to consider.

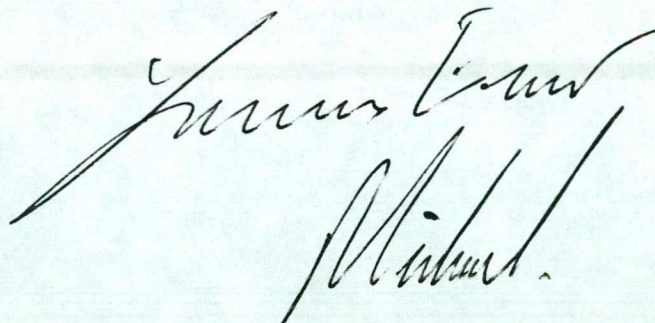
If implemented, the proposals I have outlined would give a signal to farmers, landowners and to the rural community as a whole that the Government is indeed willing to assist the adaptive process now under way. Some of my suggestions are designed specifically to encourage farmers and private agricultural landlords, to take a full part in sustaining the rural economy. There is little doubt that the success of our rural strategy will have to depend heavily on their enterprise.

Of the points detailed in the memorandum the major items are clearly capital allowances for plant and machinery on which I have already

/written you,

written you, the removal of the inflationary penalty from Capital Gains Tax and the recognition of private agricultural landlords as businessmen and of their important contribution to the rural economy.

On the excise duty front I understand that as in past years my officials will be meeting officials from Customs and Excise. I shall write to you further on that subject in the light of this meeting.

A handwritten signature in cursive script, appearing to read "James Evans" on the top line and "Michael" on the bottom line. The signature is written in dark ink on a light-colored background.

MICHAEL JOPLING

CONFIDENTIAL

TAX LAW CHANGES : MEMORANDUM BY THE MINISTRY OF AGRICULTURE,
FISHERIES AND FOOD

INTRODUCTION

1. This Memorandum sets out the changes in tax law affecting agriculture and horticulture which the Ministry would wish to see in the 1987 Finance Bill.
2. Agriculture now faces a period of considerable change. It is now clear that milk production will be further reduced over the next 2 years, the support arrangements for beef are to be weakened, whilst for cereals, steps to curb the escalation of stocks will be inevitable over the next year or so. The industry faces this future at a time when its income is depressed and its balance sheet is weakening. In 1985 aggregate farming income fell to the lowest level in real terms for many decades and 1986 will see only a modest recovery. Borrowing continues to rise - much of it for working capital - but servicing this debt from squeezed income is becoming a serious problem for many farmers, particularly those on smaller family farms. Investment has fallen and more and more farmers are looking for opportunities to generate cash flow from non-farming activities. Further labour shedding, with its impact on the rural infrastructure, is anticipated.
3. Faced with this situation, and the need to provide farmers with every reasonable opportunity to enable them to cope with the adjustments, the following proposed tax changes concentrate on measures that would:-
 - (1) assist the smaller family farm by the introduction of a limited first year capital allowance, designed to help the development of small businesses generally;
 - (2) remove anomalies from Capital Gains Tax which are bearing particularly heavily on farmers;

- (3) encourage private agricultural landlords to let farms, thus assisting the introduction of new blood to the industry;
- (4) do away with a measure which penalises farmers, but no-one else, relating to the treatment of trading income;
- (5) encourage the sale of parcels of poorer land to conservation bodies.
- (6) allow the concession on holiday letting to apply more fairly to the remoter areas.

CAPITAL ALLOWANCES

4. There is little doubt that the withdrawal of first year capital allowances, when the agricultural industry faced the most difficult economic situation for many years, hindered the industry's adaptation and diversification. When the withdrawal of the allowances were announced in 1984 it was explained that this should be seen as a quid pro quo for reform of company taxation. It was explained that the allowances reflected outdated economic priorities or circumstances and served to distance a firm's investment decisions from tax planning strategies. But it should be noted that the small to medium size farm business seldom possesses the spare resources to allow it to invest in unwanted farm machinery for tax planning purposes so that purchasing decisions are invariably taken on the basis of need. Moreover, as only 5% of farming businesses are incorporated, some 95% gained nothing from the reductions in the rate of Corporation Tax.

5. In the view of the Department the present economic priorities and circumstances call for help to be given to small to medium size farm businesses to help them invest in essential plant and machinery necessary for the adjustments they will need to make. For example one medium size tractor might cost some £20,000 and a medium sized combine harvester more than double that sum, and therefore we recommend that, say, £30,000 would be a realistic level at which to set a new 100% first year allowance. Such an allowance would be aimed at all small businesses whether in farming or not. Agreement to such a proposal would provide a very real boost to the development of new small businesses which form an essential plank of the Government's economic and employment policies.

6. The introduction of optional balancing charges or allowances in respect of expenditure on agricultural buildings has been welcomed by the agricultural industry although few are likely to benefit. A particular difficulty faced by agriculturalists and horticulturalists is that once buildings have been erected there is little incentive to demolish them and return the land to a green field site even though the original and often specialised, purpose of the buildings has long since disappeared. For example, many who constructed new dairy parlours three or four years ago might now find them redundant because of milk quotas. As quotas are further reduced more farmers will find, under the present tax regime, they will have to wait for almost 25 years before benefiting from the full capital allowances even though the building will have no dairying function. We suggest that consideration be given to ways of overcoming such a disadvantage where it can clearly be shown that the building can no longer be used for its intended purpose and is of limited value to the farm business.

CAPITAL GAINS TAX

7. Between the introduction of Capital Gains Tax in 1965 and the provision for indexation in the 1982 Budget, the Retail Price Index rose by 548%. Over the same period agricultural land prices increase by 750%. Unlike many other business resources, agricultural land is usually retained for very long periods. It therefore follows that farmers and private agricultural landlords have been badly affected by the continuing retention of such a substantial inflationary element in CGT. As a result, CGT has acted as a disincentive to the taking of sound business decisions, particularly necessary at the present time when the industry is adjusting to financial pressures. The Department considers that steps should be taken this year to relieve the agricultural industry of some of the inflationary content of CGT.

8. It is therefore suggested as our first preference that the base date from which increases in value are calculated should be brought forward progressively from 1965 towards the 1982 indexation date. As an alternative, an automatic cut-off could be introduced so that CGT would not apply when an asset had been held for, say, 10 years.

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16 JANUARY 1987



Minister of State for the Environment,
Countryside and Planning

Department of the Environment
2 Marsham Street London SW1P 3EB
Telephone 01-212 3434

70

HM TREASURY - MCU	
RECD.	27 JAN 1987
ACTION	✓/K Dallas P.P.
	cc APS/CHX
	CE.
SIGNATURE	CHX
REF No.	11228/87

25 January 1987

Dr Nigel,

Your announcement in the last budget that you proposed a duty differential to off-set the higher production cost of unleaded petrol was a most welcome development in our policy for introducing unleaded petrol. My officials have kept in close touch with yours and I am pleased to hear that discussions have gone well. You will now be taking your final decision on the size of the differential required.

The UK has already achieved a modest network of unleaded petrol stations for the use of overseas tourists without regulatory intervention, but it is clear that there will be little penetration of the home market until the price of unleaded petrol becomes attractive to UK motorists. This is well recognised by the oil industry. They would not, I am sure, wish to see the unleaded petrol market over-stimulated to the point of encouraging the fuel's use by those whose cars cannot safely run on it. However, if the differential in duty were to prove insufficient to cover the extra costs of its production and distribution, they have made it clear that we could not expect to see any immediate increase in demand or further investment in supply. Our whole non-regulatory approach would thus be in jeopardy.

I recognise that the necessary tax differential cannot be precisely determined, but I hope that you feel able in exercising your judgement to give a clear price signal to suppliers and consumers alike. The volume of unleaded petrol consumed will still be small this year; the change to unleaded fuel can only be gradual. The total revenue yield from leaded plus unleaded petrol must be capable of being estimated for the forthcoming year very nearly as exactly as in the past. The revenue at risk in the year from an adequate differential introduced now must be small indeed; and rates of duty can be re-set to secure the desired revenue in future years.

RESTRICTED

A good start for unleaded petrol would gain credit for our policy,
and avoid unjust accusations of continued stagnation in this
market.

W. Waldegrave

WILLIAM WALDEGRAVE

The Rt Hon Nigel Lawson MP

PWP



C/

John Moore's office phoned.

He cannot find any particularly attractive option for the £15m.

He is content for you to decide on the proposals for Farmers' hgv rates and Trade Licences.

Officials are meeting today to sort out the problems on the figures and I will let you know the outcome. Mr Romanski will be sending a minute over next day or so on all of this

CR 29/1

[Handwritten signature]
[Handwritten signature]

DOE
Waldegrave

Confidential

DEPARTMENT OF THE ENVIRONMENT: MR WALDEGRAVE - 25 JANUARY

Mr Waldegrave welcomes the proposed introduction, in the 1987 Budget, of a duty differential in favour of unleaded petrol, and hopes that it will prove sufficient to cover the extra costs of production and distribution.

Comment

Based on the information regarding higher production costs provided to us by the oil industry, the duty differential provided for by starter 5 will indeed be sufficient to cover those costs.

CONFIDENTIAL



FROM: CATHY RYDING

DATE: 28 January 1987

MR ROMANSKI

cc PS/MST
Mr Scholar
Miss Sinclair
Miss Evans
PS/C&E**CHANCELLOR'S MEETING WITH SECRETARY OF STATE FOR TRANSPORT**

The Chancellor met the Secretary of State for Transport yesterday evening at 5.30 pm to discuss options for the 1987 Budget.

2. The Chancellor and Secretary of State agreed that there were a number of problems with the option that had been explored in correspondence last year. The Chancellor outlined two options which he now saw as possibilities:-

- (i) A VED standstill with the lost revenue recouped from derv (an increase of 4.5p) and petrol (5.3p);
- (ii) As above but an increase in derv duty of the same size as petrol (ie 5.3p). This would yield around £15 million extra revenue compared to option (i) which could be used if there were any particularly attractive options available.

The Secretary of State said that his Department had made a number of proposals for minor VED rates - and attached to this minute are details which the Secretary of State handed to the Chancellor at the meeting. However, these were not without problems, and he would think again whether there was any particularly attractive option for which the £15 million could be used.

3. There was some confusion at the meeting as to the increase in petrol and derv prices implied by option (i). The figures you provided for the Chancellor implied increases of 4.5p for derv and 5.3p for petrol. As you will see from the attached notes,

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Department of Transport officials estimate figures of 4.0p and 4.5p. Also, the Secretary of State had been given a figure of £320 million for the revenue cost of option (i) whereas your figure, I think, was £325 million. I should be grateful if you could investigate the reason for this discrepancy.

CR

CATHY RYDING

EXTRACT FROM
OVERVIEW MTG 19/1

BUDGET - SECRET - EXTRACT FROM
BLO DOCUMENT J87/2

EXTRACT FROM FIRST BUDGET OVERVIEW MEETING 19.1.86

3. On fuel duties and VED, it was agreed that VED on cars should remain at £100, with the lost revenue being recouped by an over-indexation of petrol duty. It was agreed that there was a strong case for making a switch from lorry VED to derv gradually, so as to prepare the ground and to signal to derv users which way the trend was going. The two most promising options seemed to be either a VED standstill with the lost revenue recouped from derv (ie. an increase of 4.5 per cent) or an increase in derv duty of the same size as petrol (ie. 5.3 per cent) with some reduction in lorry VED. The Chancellor would have an early and informal discussion with the Secretary of State for Transport.

BUDGET - SECRET

BUDGET SECRET

FROM: K M ROMANSKI

DATE: 26 January 1987

- B 271,
1. MISS SINCLAIR
 2. CHANCELLOR OF THE EXCHEQUER

cc PS/Minister of State
Mr Scholar
Miss Evans
PS/Customs

MEETING WITH MR JOHN MOORE: BALANCE OF VEHICLE TAXATION

You are meeting Mr Moore on 27 January to discuss the balance on vehicle taxation between VED and fuel duty. The arguments for and against a shift in the balance, on both lorries and cars are set out in my minute of 15 January. This minute summaries the effect of the various options.

Lorries

2. There are 4 possible packages:

	derv price increase (p per gallon)	lorry & other VED revenue change (£m)	total net revenue change, compared to revalorisation
a. £100m lorry- neutral switch	14.0	- 100	- 20
b. derv duty increase equal to petrol duty increase	5.3	- 15	0
c. derv duty increase to compensate for non-revalorisation of VED	4.5	0	0
d. revalorisation of both derv duty and VED	3.2	+ 20	0

(a) is the option in your letter of 19 December to Mr Moore (copy attached). The overall revenue loss has been reduced

BUDGET SECRET

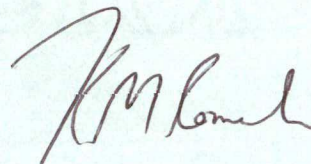
to £20 million as a result of revised Department of Transport figures on the cost of rebates. (b) is the front runner which you are to put to Mr Moore, with (c) as fallback. (d) is included for comparison.

3. The latest information on the price of derv is that it is now generally about 159.6p per gallon - 15.4p below the pre-Budget 1986 price.

Cars

4. The favoured option is a 5.3p per gallon increase in petrol^{taxation}, which would yield £75 million over revalorisation, in order to compensate for non-revalorisation of car VED. Revalorisation of both duties would add 3.7p to a gallon of petrol, and £3.70 to car VED.

5. The latest information on the price of petrol is that it is now generally about 175.5p per gallon - 1.5p above the pre-Budget 1986 price.



K M ROMANSKI

CONFIDENTIAL



cc CST
 FST
 MST
 EST
 Sir P Middleton
 Mr Scholar
 Miss Sinclair
 Mr Romanski
 Mr Cropper
 Mr McGuigan - C
 Mr Wilmott - C &
 PS/C&E

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

The Rt Hon John Moore MP
 Secretary of State for Transport
 Department of Transport
 2 Marsham Street
 LONDON
 SW1P 3EB

19 December 1986

A handwritten signature in cursive script, appearing to read 'John Moore'.

Thank you for your letter of 8 September about vehicle taxation. I have delayed replying until I had seen the outcome of the work done by our officials on switching the balance of lorry taxation from VED to derv.

In the light of their work, I would be prepared to accept that we should be looking for a switch from VED to derv duty of £100 million, and that the switch should be neutral for lorries as a whole. The increased taxation on diesel driven cars and light vans and buses, coaches and taxis would help to offset the first-year cost of carrying out the switch. But a final decision will depend on your Department being able to devise and operate a system for dealing with the problem of refunds in such a way that the first-year cost of the switch is minimised, as well as any developments in the price of derv between now and the Budget. In addition, I shall wish to consider the appropriate level of these duties as part of my Budget judgement.

A handwritten signature in cursive script, appearing to read 'Nigel Lawson'.

NIGEL LAWSON

Information:

~~BUDGET - CONFIDENTIAL~~

AIDE MEMOIRE ON SECRETARY OF STATE'S THREE MAIN OPTIONS

NB. Figures have been rounded and should be regarded as giving broad orders of magnitude

"ORIGINAL PROPOSAL ON BOTH": Substantial duty switch for petrol and diesel vehicles

Switch £100m for diesel vehicles, plus sufficient on petrol vehicles to maintain present duty differential of 14p per gallon; then revalorise total VED+fuel yield and seek that additional revenue from fuel duties only

<u>increase in</u> <u>derv duty</u>	<u>change to</u> <u>lorry/bus VED</u>	<u>increase in</u> <u>petrol duty</u>	<u>change to</u> <u>car/1.van VED</u>
12p (£190m)	£100m less	13p yielding £710m (15p at pump incl. VAT)	450m less (£20 off car VED)

*Reform needs
improvement
year.*

Effect for

lorries: overall £45m up (ie revalorisation @ 3.7%). Fuel duty up £145m (16.2%). VED rates down by average 22%, but selectively. Details in Table B.

buses: overall £25m up (16%), all from fuel duty, of which £15m rebated for local services, so net revenue £10m. No change in VED.

cars: overall £260m up. (3.7%). Fuel duty £710m up (15%). VED £450m down. £20 (20%) decrease in VED rate. 0.5m diesel cars and light vans suffer £30m (16% or £60 pa) increase in fuel duty.

"GENERAL ON BOTH": Freeze VED rates for both petrol and diesel vehicles, and recover equivalent amount by more than revalorising both fuel duties

<u>increase in</u> <u>derv duty</u>	<u>change to</u> <u>lorry etc VED</u>	<u>increase in</u> <u>petrol duty</u>	<u>change to</u> <u>car etc VED</u>
4p (£60m)	-	4.5p yielding £260m (5p at pump)	-

Effect for

lorries: overall £45m up (3.7%), all from fuel duty (up 5.3%). No change in VED. Details in Table C.

buses: overall £10m up, all from fuel duty, of which £7m rebated for local services. So net revenue £3m. No change in VED.

cars: overall £260m up (3.7%), all from fuel duty (up 5.2%). No change in VED. 0.5m diesel cars and light vans suffer £10m (5% or £20 pa) increase in fuel duty.

"GENERAL ON DIESEL ONLY": Freeze VED rates for diesel vehicles and recoup from more than revalorisation of derv duty. Revalorise VED* and petrol duty

<u>increase in</u> <u>derv duty</u>	<u>change to</u> <u>lorry etc VED</u>	<u>increase in</u> <u>petrol duty</u>	<u>change to</u> <u>car etc VED</u>
4:5p P (£60m)	-	3p yielding £185m (4p at pump)	£100m more. Rate up to £105

104.

Effect for

lorries: overall £45m up (3.7%), all from fuel duty (up 5.3%). No change to VED. Details in Table C.

buses: overall £10m up, all from fuel duty, of which £7m rebated for local services. So net revenue £3m. No change in VED.

cars: overall £285m up (4%). Fuel duty £185m up (3.7%). VED £100m up. £5 increase in VED rate. 0.5m diesel cars and light vans suffer £10m (5% or £20 pa) increase in fuel duty, as well as VED increase.

*In fact, slightly more than revalorisation due to rounding to £5.

MOTORCYCLES NOTE

Motor cycle VED rates are normally linked to car rates. £100 rate implies m/c rates of £40, £20 and £10. £105 would imply £42, £21, and £10.50.

DLVTI

26 January 1987

PROPOSALS FOR MINOR VED RATES

Farm tractors and haulage vehicles

Freeze at present level, pending results of a survey under way to improve our track cost information. Revenue effect will be negligible.

Vehicle numbers and rates

389,000 vehicles
£8m p.a. at
current rates.
Revalorisation
would produce
£0.3m. ✓

Farmers' hgv rates

Implement third and last phase of increasing these concessionary rates to bring them into line with the vehicles' use of the roads.

28,000 vehicles
£7m p.a. at
current rates.
Increase produces
£2m (29%).

Trade licences

Increase to £100 as second step due towards bringing them into line with the PLG rate, whether or not PLG rate is frozen. The car trade licence currently stands at £70, having been increased from £46 last year. The trade motorcycle rate should be £20 (up from £14).

Car trade licence

90,000 licences
£6m in full year
at current rate
£9m in full year
of new rate. 43%
increase.

Motorcycle trade licences:

included above

- very few.
Revenue
negligible
Increase 43%

Recovery vehicles

Part of the modernisation of the trade scheme involves the creation of a new tax class for recovery vehicles, which, unlike vehicles properly covered by trade plates, are very much the property and equipment of the motor trade itself. The new class is to be introduced from 1 Jan 1988. Once again the PLG rate is ultimately envisaged, but we want to offer a concessionary rate at the outset to induce motor traders to re-register their vehicles in the correct class. I propose an initial £50.

Perhaps 20,000
vehicles. Full
year revenue loss
of £0.5m - £1m. ✓

Drawbar trailers

Freeze. Provided lorry rates are subjected to selective increases, or frozen, drawbar combinations will cover their costs without the need for increases in the VED trailer supplement.

4000 vehicles.
£1m revenue in
current year.
Revalorisation
would have pro-
duced £0.03m. ✓

Private
and
Light
Goods

R E S T R I C T E D



DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Cathy Ryding
Private Secretary to
The Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
LONDON SW1P 3AG


CH/EXCHEQUER	
REC.	28 JAN 1987
ACTION	MR ROMANSKI
COPIES TO	PS/MST MR SCHOLAR MISS SINCLAIR MISS EVANS RS/C+E

28 January 1987

Dear Cathy

We spoke following the discussion between my Secretary of State and the Chancellor yesterday afternoon. I promised to let you have a note of our deadlines for decisions. I enclose a note prepared by officials here setting these out which I hope you will find helpful.

yours sincerely


SARAH STRAIGHT
Private Secretary

R E S T R I C T E D

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VED: DEADLINE FOR BUDGET DECISIONS

1. As a target, 16 Feb for a final decision would cover most contingencies.
2. If Chancellor requires more time for a final decision, we could cope with the practicalities, within limits set out below, while running some risk through reducing checking etc.
3. Overtime working might then be needed if unforeseen anomalies or equipment failure occurred.
4. Deadlines would be:
 - a. Final decision by Chancellor among three permutations: we need to know 3 runners by 17 Feb
final decision by 3 Mar
 - b. Final decision between two permutations: 2 runners by 23 Feb
final decision by 3 Mar
 - c. Decision without prior identification of runners: final decision by 25 Feb

Time: 11.00 hrs in each case.

DLVTI

27 January 1987

RESTRICTED



DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

Our Ref : JM/PSO/1628/87

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
LONDON SW1P 3AG



17 February 1987

Dear Nigel.

Thank you for your letter of 11 February about VED. I have asked my officials to proceed in accordance with it.

CH/EXCHEQUER	
REC.	19 FEB 1987
ACTION	CST FST EST MST SIR P MIDDLETON
COPIES TO	MR CASSELL
	MR SCHOLAR
	MISS SINCLAIR
	MISS EVANS
	MR CRAPPER
	MR TYLKE
	MR ROSS GIBBERT PS/C+E

19/2

JOHN MOORE

*Pse type***DRAFT LETTER TO:**

The Rt Hon John Moore MP
Secretary of State for Transport
Department of Transport
2 Marsham Street
LONDON
SW1P 3EB

February 1987

Following our meeting on 27 January, I am writing to let you know my decisions on vehicle excise duty rates.

I understand, that following our discussion, you are not looking for any reduction in lorry VED rates. On that basis, I propose to leave main lorry VED rates and the rate for cars and light vans unchanged. I am content for your officials to stop work on the rebate scheme which would have been necessary in the event of duty reductions.

I have also considered the proposals for minor VED rates in the note you handed me at our meeting. I am content with your proposals to leave unchanged the rates for buses, coaches and taxis, motor cycles, pre-1987 cars, agricultural tractors and haulage vehicles and drawbar trailers. I am also content with your proposal that we should implement the final stage of increasing the concessionary rates for farmers' hgvs, and that the new rate for recovery vehicles should be set at £50. But on trade licences, I would prefer a longer staging process, and would propose to set the rates at £85 for cars and £17 for motor cycles.

NIGEL LAWSON

SECRET

FROM: K M ROMANSKI

DATE: 2 February 1987

- RC 2/2*
1. MISS SINCLAIR
 2. CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
 Financial Secretary
 Minister of State
 Economic Secretary
 Sir P Middleton
 Mr Cassell
 Mr Scholar
 Miss Evans
 Mr Cropper
 Mr Tyrie
 Mr Ross Goobey
 Mr Knox (C&E)
 PS/C&E

*c/ Para 12 lists points
 for decisions.*

*Answers in margin.
 CR 2/2.*

VEHICLE EXCISE DUTY

This minute seeks decisions on vehicle excise duty following your meeting with Mr John Moore on 27 January and his subsequent reactions.

Lorries

2. Mrs Ryding's minute of 28 January records that you discussed two options with Mr Moore :

(i) VED standstill with lost revenue recouped from derv (4.5p increase); and

(ii) £15 million reduction in lorry VED rates, recouped by increasing derv by as much as petrol (5.3p).

As requested in Mrs Ryding's minute, I confirm that these figures are correct for price increases, including VAT - Department of Transport officials agree. The figures of 4p and 4.5p which they supplied to Mr Moore were for the duty increases alone, rounded to the nearest ½p. The difference of £5 million in the total

SECRET

revenue gain from revalorisation arose because our figure included the minor oil duties, whereas Department of Transport's did not. The elements are agreed to be

	£m
Petrol	185
Derv	40
Minor oils	5
Car VED	75
Lorry and other VED	20
	<hr/>
	325

3. We now understand from his Private Office that Mr Moore does not want any reduction in lorry VED rates. In the light of that, there seems to be no reason for you to insist on a reduction. This raises the following questions:

a. Do you want Department of Transport to work on any package involving increased lorry VED rates (with prepared options, the deadline for decisions is 3 March; the deadline for producing a new option is 27 February);

b. Can Department of Transport stop work on the VED rebate scheme which would have been needed to limit revenue loss if there had been any reductions in VED rates.

4. So far as derv duty is concerned, we understand that Mr Moore has it in mind that, although he does not want any reduction in lorry VED, you might still wish to increase derv duty by the same amount in pence as petrol. Although this would produce a £15 million revenue gain with negligible RPI impact, and the current price of derv is about 15p below the pre-Budget 1986 price, there seems no reason to impose a real increase in taxation in this area, with its consequent impact on business costs. But Department of Transport do not, of course, need to have any indication of the derv duty increase at present. (They need to know much nearer Budget Day, so they can calculate the new road track cost and tax allocations).

Cars

5. Mr Moore is content with the proposal that car VED should be unchanged, and the revenue recouped from over-indexation of petrol duty. The question again arises whether you wish Department of Transport to prepare an option for any change in car VED.

Minor VED rates

6. Mr Moore gave you a note with his proposals for minor VED rates (copy attached). In most cases this is to leave the rates unchanged. This would apply to the following categories of vehicles:

- buses, coaches and taxis;
- motor cycles;
- pre-1947 cars (not mentioned in the note, but we understand from Department of Transport officials that no change is proposed);
- agricultural tractors and haulage vehicles; and
- drawbar trailers (supplementary duty rates for vehicles towing trailers).

So long as the main VED rates are unchanged, to leave the rates unchanged for these vehicles seems reasonable. Non-revalorisation of these VED rates has been allowed for in the scorecard figures - the total cost is only some £2 million. But if the main VED rates are changed, it would be appropriate to change at least some of the minor VED rates, as they are linked to the main rates.

7. There are, however, two areas where Department of Transport are proposing increases in duty rates, farmers HGVs and trade

SECRET

licences. There is also a need to settle on a duty rate for a new taxation class, recovery vehicles, which it has been agreed in principle should be legislated for the Finance Bill.

Farmers' lorries

8. The proposed increase in VED for farmers' HGVs would be the third and final step in a three-stage increase in the duty rates for these vehicles to bring them up to 60 per cent of the main lorry rates, because farmers' lorries on average do 60 per cent of an ordinary lorry's mileage on the public roads. The intention to make this increase in three annual stages has been announced, so the increases this year are expected. There has been little criticism or controversy caused by these increases - for instance, the NFU Budget representation does not mention them. Ordinary hauliers have been critical of the farmers' concessionary rates, arguing that they create unfair competition, and so not to raise farmers' VED rates could lead to criticism from them. If farmers HGV rates were not to be increased, it would be necessary to announce whether the increase was merely being deferred, or whether the 60 per cent target was being abandoned. I therefore recommend that you agree to increase farmers' lorry VED rates as previously announced. This will yield £2 million in 1987-88 and in a full year.

Trade licences

9. The proposed increase in trade licence rates also forms part of a pre-announced plan, in this case to raise the rate of duty for trade licences to the full car or motor cycle rate of duty. Trade licences enable motor dealers to use new vehicles on the road without licensing them separately. Last year, the conditions for using these licences were eased, following a consultation exercise. The question of raising the duty rates was covered in the same exercise, and traders generally accepted it, because they recognised the advantages which they gained from these licences. In last year's Budget the rates were increased from

SECRET

£46 to £70 (£9 to £14 for motor cycles), with effect from 1 January 1987 (annual licences run for the calendar year) with hardly any controversy. To increase the rates now £100 and £20, respectively, from 1 January 1988 would raise £2 million in 1987-88 and £3 million in a full year. But although the intention to increase the rates to those amounts has been announced, the number of stages has not. So, there would be no reason not to make the increase in two further stages, which would imply duty rates of £85 and £17. This would yield £1 million in 1987-88 and £1½ million in 1988-89. This would reduce still further the risk of criticism, and so I recommend accordingly.

Recovery vehicles

10. A Budget starter has been agreed in principle to create a new licence class for recovery vehicles. At present, some of these vehicles are licensed as light vans (at £100) or lorries (mainly at £130 or £290). But most use trade licences. Although these are currently £70, the owner would not need a licence for each vehicle, only for as many as were on the road at any one time - a trader who dealt in new cars as well as owning recovery vehicles might not need any additional licences for his recovery vehicles. Although Mr Moore's long term aim is to set the rate for these vehicles at the car rate, he is asking for a low rate of duty at first to encourage those traders who currently use trade plates to register their recovery vehicles correctly in the new class. He has suggested a rate of £50, and this seems reasonable, so I recommend you agree. The new rate would take effect from 1 January 1988. The revenue effect would be a gain of about £0.5 million in 1987-88 (from the additional licences taken out by those currently using trade licences) but a loss of about £0.5 million 1988-89, as those currently using dealer licences switch to the cheaper recovery vehicle rates.

11. The net effect of these changes (with either size of increase for trade licences) would be to reduce the scorecard loss in both

SECRET

1987-88 and 1988-89 for lorry and other VED from £20 million to £15 million. There would be no RPI effect. This would balance out the £5 million foregone from not revalorising the minor oil duties.

Summary

12. This minute asks for the following decisions

NO a. Do you want Department of Transport to work on any lorry VED changes (paragraph 3);

YES b. Can they stop work on the rebate scheme needed if lorry VED rates were to be reduced (paragraph 3);

NO c. Do you want Department of Transport to prepare an option for any change in car VED (paragraph 5);

YES d. Are you content that most minor VED rates should remain unchanged (paragraph 6);

YES e. Do you agree the farmers' HGV rates should be increased to 60 per cent of the main lorry rates (paragraph 8);

YES f. Do you agree that the trade licence rate should be increased to £85 for cars and £17 for motor cycles (paragraph 9);

YES g. Do you agree that the rate for recover vehicles should be set at £50 (paragraph 10).

13. When I have your views, I will prepare a draft letter for you to send to Mr Moore.



K M ROMANSKI



FROM: CATHY RYDING

DATE: 28 January 1987

MR ROMANSKI

cc PS/MST
Mr Scholar
Miss Sinclair
Miss Evans
PS/C&E

CHANCELLOR'S MEETING WITH SECRETARY OF STATE FOR TRANSPORT

The Chancellor met the Secretary of State for Transport yesterday evening at 5.30 pm to discuss options for the 1987 Budget.

2. The Chancellor and Secretary of State agreed that there were a number of problems with the option that had been explored in correspondence last year. The Chancellor outlined two options which he now saw as possibilities:-

- (i) A VED standstill with the lost revenue recouped from derv (an increase of 4.5p) and petrol (5.3p);
- (ii) As above but an increase in derv duty of the same size as petrol (ie 5.3p). This would yield around £15 million extra revenue compared to option (i) which could be used if there were any particularly attractive options available.

The Secretary of State said that his Department had made a number of proposals for minor VED rates - and attached to this minute are details which the Secretary of State handed to the Chancellor at the meeting. However, these were not without problems, and he would think again whether there was any particularly attractive option for which the £15 million could be used.

3. There was some confusion at the meeting as to the increase in petrol and derv prices implied by option (i). The figures you provided for the Chancellor implied increases of 4.5p for derv and 5.3p for petrol. As you will see from the attached notes,

CONFIDENTIAL



Department of Transport officials estimate figures of 4.0p and 4.5p. Also, the Secretary of State had been given a figure of £320 million for the revenue cost of option (i) whereas your figure, I think, was £325 million. I should be grateful if you could investigate the reason for this discrepancy.

CR

CATHY RYDING

Information:

BUDGET - CONFIDENTIAL

AIDE MEMOIRE ON SECRETARY OF STATE'S THREE MAIN OPTIONS

NB. Figures have been rounded and should be regarded as giving broad orders of magnitude

"ORIGINAL PROPOSAL ON BOTH": Substantial duty switch for petrol and diesel vehicles

Switch £100m for diesel vehicles, plus sufficient on petrol vehicles to maintain present duty differential of 14p per gallon; then revalorise total VED+fuel yield and seek that additional revenue from fuel duties only

<u>increase in derv duty</u>	<u>change to lorry/bus VED</u>	<u>increase in petrol duty</u>	<u>change to car/l.van VED</u>
12p (£190m)	£100m less	13p yielding £710m (15p at pump incl. VAT)	450m less (£20 off car VED)

Reform makes impossible this year.

Effect for

lorries: overall £45m up (ie revalorisation @ 3.7%). Fuel duty up £145m (16.2%). VED rates down by average 22%, but selectively. Details in Table B.

buses: overall £25m up (16%), all from fuel duty, of which £15m rebated for local services, so net revenue £10m. No change in VED.

cars: overall £260m up. (3.7%). Fuel duty £710m up (15%). VED £450m down. £20 (20%) decrease in VED rate. 0.5m diesel cars and light vans suffer £30m (16% or £60 pa) increase in fuel duty.

"GENERAL ON BOTH": Freeze VED rates for both petrol and diesel vehicles, and recover equivalent amount by more than revalorising both fuel duties

<u>increase in derv duty</u>	<u>change to lorry etc VED</u>	<u>increase in petrol duty</u>	<u>change to car etc VED</u>
4p (£60m)	-	4.5p yielding £260m (5p at pump)	-

Effect for

lorries: overall £45m up (3.7%), all from fuel duty (up 5.3%). No change in VED. Details in Table C.

buses: overall £10m up, all from fuel duty, of which £7m rebated for local services. So net revenue £3m. No change in VED.

cars: overall £260m up (3.7%), all from fuel duty (up 5.2%). No change in VED. 0.5m diesel cars and light vans suffer £10m (5% or £20 pa) increase in fuel duty.

"GENERAL ON DIESEL ONLY": Freeze VED rates for diesel vehicles and recoup from more than revalorisation of derv duty. Revalorise VED* and petrol duty

<u>increase in derv duty</u>	<u>change to lorry etc VED</u>	<u>increase in petrol duty</u>	<u>change to car etc VED</u>
4: 4 p (£60m)	-	3p yielding £185m (4p at pump)	£100m more. Rate up to £105

104.

Effect for

lorries: overall £45m up (3.7%), all from fuel duty (up 5.3%). No change to VED. Details in Table C.

buses: overall £10m up, all from fuel duty, of which £7m rebated for local services. So net revenue £3m. No change in VED.

cars: overall £285m up (4%). Fuel duty £185m up (3.7%). VED £100m up. £5 increase in VED rate. 0.5m diesel cars and light vans suffer £10m (5% or £20 pa) increase in fuel duty, as well as VED increase.

*In fact, slightly more than revalorisation due to rounding to £5.

MOTORCYCLES NOTE

Motor cycle VED rates are normally linked to car rates. £100 rate implies m/c rates of £40, £20 and £10. £105 would imply £42, £21, and £10.50.

DLVTI

26 January 1987

PROPOSALS FOR MINOR VED RATES

Farm tractors and haulage vehicles

Freeze at present level, pending results of a survey under way to improve our track cost information. Revenue effect will be negligible.

Vehicle numbers and rates

389,000 vehicles
£8m p.a. at
current rates.
Revalorisation
would produce
£0.3m. ✓

Farmers' hgv rates

Implement third and last phase of increasing these concessionary rates to bring them into line with the vehicles' use of the roads.

28,000 vehicles
£7m p.a. at
current rates.
Increase produces
£2m (29%).

Trade licences

Increase to £100 as second step due towards bringing them into line with the PLG rate, whether or not PLG rate is frozen. The car trade licence currently stands at £70, having been increased from £46 last year. The trade motorcycle rate should be £20 (up from £14).

Car trade licence

90,000 licences
£6m in full year
at current rate
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of new rate. 43%
increase.

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included above

- very few.
Revenue
negligible
Increase 43%

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Part of the modernisation of the trade scheme involves the creation of a new tax class for recovery vehicles, which, unlike vehicles properly covered by trade plates, are very much the property and equipment of the motor trade itself. The new class is to be introduced from 1 Jan 1988. Once again the PLG rate is ultimately envisaged, but we want to offer a concessionary rate at the outset to induce motor traders to re-register their vehicles in the correct class. I propose an initial £50.

Perhaps 20,000
vehicles. Full
year revenue loss
of £0.5m - £1m. ✓

Drawbar trailers

Freeze. Provided lorry rates are subjected to selective increases, or frozen, drawbar combinations will cover their costs without the need for increases in the VED trailer supplement.

4000 vehicles.
£1m revenue in
current year.
Revalorisation
would have pro-
duced £0.03m. ✓

RESTRICTED



QUEEN ANNE'S GATE LONDON SW1H 9AT

BR

HM TREASURY - MCU	
REC'D.	- 3 FEB 1987
3 ACTION	R Walker FP.
	February 1987
	CC 1985/CMT, CS
SIGNATURE	CMT.
REF. No.	11725/87

Dear Nigel:

TAXATION OF ALCOHOL

I think a number of us are becoming increasingly concerned about the consequences of heavy alcohol consumption. Norman Fowler is coming under increasing pressure, not least from the medical profession; John Moore and I have a shared interest in reducing drunken driving; and I am keenly and increasingly concerned about the links between alcohol and crime, including public disorder. There is no doubt that heavy drinking results in additional strains on the police, the courts and the prisons, and I am sure Norman Fowler would say the same about the health and social services. At some point we may need to look at these issues collectively, especially if we propose to revise the licensing laws.

I am writing to you now because of the Budget timetable and because I am convinced that taxation can play a part in influencing drinking habits.

Last year, the Home Office Research and Planning Unit prepared a comprehensive paper on alcohol and crime. This was discussed at meetings of the Ministerial Group on Crime Prevention (MGCP) at which the Treasury is represented.

One of the most difficult problems is how to discourage binge beer-drinking by young men, which as the Research and Planning Unit paper shows, is associated with a good deal of public disorder crime near licensed premises. A Working Group of the Standing Conference on Crime Prevention had already looked at the prevention of violence near licensed premises; and demonstration projects are being set up to follow up the Working Group's report. We hope that these will provide some answers to controlling this problem. But the Ministerial Group on Crime Prevention also concluded that the taxation system for beer could provide an important means of influencing drinking habits. This conclusion has been given added force by the widely reported disturbances on New Year's Eve, in which heavy drinking played a part.

The Treasury provided a paper for the last meeting of MGCP: while the Group appreciated that beer taxation already discriminates against higher strength beers, the discrimination is very slight. The Group concluded that I should approach you to see what scope there is for changing the tax structure for beer, to try to encourage consumption of lower strength beers.

The Rt Hon Nigel Lawson, M.P.

/over....

RESTRICTED

.... A further paper by the Research and Planning Unit explains the arguments in more detail and I am enclosing a copy. I strongly support the Group's conclusions; and I gather that similar representations have been made to you by DHSS and Department of Transport Ministers on the grounds that such a change in the taxation might have benefits for health and in reducing drunken driving.

I am well aware of the sensitivities of the whole issue: but there is no reason why the change should lead to either a reduction in consumption of beer or a reduction in tax revenue. What we are seeking is a switch in consumption from higher to lower strength beers, i.e. a reduction in the consumption of alcohol rather than of alcoholic drinks. I believe that, rightly presented, a change to a more steeply graded taxation system for alcohol beers would be difficult to oppose: a reduction in alcohol-related health problems, a reduction in drunken driving, and a reduction in alcohol-related crimes, are all aims to which few could object.

More generally, I believe that there is a good case for maintaining, or even increasing, the cost of alcohol in real terms. In preparing your proposals for Budget, I should be very grateful if you could take into account these wider social issues, with their public expenditure implications.

I am copying this letter to Norman Fowler and John Moore, and to those Ministers who attend the Ministerial Group on Crime Prevention.

Conroy,

Douglas.

SELECTIVE TAXATION - A VALUABLE DIMENSION FOR THE PREVENTION OF ALCOHOL MISUSE IN THE UK ?

David Riley and Joy Mott.

Research and Planning Unit,
Home Office, 50 Queen Anne's Gate, London SW1H 9AT.

The medical profession has recently renewed calls to curb alcohol consumption in the United Kingdom in the attempt to reduce the extent of alcohol-related illness, social problems, road accidents and crime. The British Medical Association [1] and the Royal College of Psychiatrists [2] have argued that the evidence linking the level of national per capita consumption to the price of alcohol is overwhelming, and that the Government could act to reduce or stabilize consumption by using the level of excise duty to increase the real cost of alcohol. The BMA supported the view that the prices of alcoholic beverages should increase at least in line with the Retail Price Index.

There is, however, some evidence that across-the-board increases in taxation on alcoholic beverages may not be effective as a means of influencing the consumption patterns for selected groups of the drinking population [3,4]. Recent research in Holland found that changes in self-reported consumption levels by young male drinkers over a 23 year period were not consistent with movements in national per capita consumption [5].

On the other hand, a policy of selective taxation which related the amount of excise duty levied more closely to pure alcohol content within each of the main types of beverage may provide a more efficient fiscal strategy. At present the UK alcohol tax structure has some degree of selectivity in that the proportion of the retail selling price made up by excise duty is broadly consistent with differences in the amounts of pure alcohol in standard measures with spirits attracting the highest levels of duty. But the amount of duty levied is not very closely related to the amount of pure alcohol in standard measures of beverages within each of the main types. The excise duty on a pint of beer containing 4.5% alcohol by volume is just 3p more than for a pint of beer containing 3% alcohol. The excise duty on 70 cl bottles of wine containing 8% alcohol by volume is the same for wine containing 12% alcohol. Thus, the present tax structure provides little or no price disincentive for the consumption of beverages with the highest pure alcohol contents within each type.

The retail price of 10cc of pure alcohol consumed as spirits can actually be lower than the price for the same amount consumed as beer. Table 1 shows the average retail price in December 1986 for 10cc of pure alcohol in five types of beverage using the prices of one supermarket chain's own brands as an example.

Insert Table 1

Attempts at reducing alcohol consumption by increasing the relative price of all alcoholic beverages presumably aim to change the behaviour of the drinking population by reducing the number of drinking occasions or the number or size of drinks consumed during each occasion. More selective taxation as proposed here could reduce alcohol consumption without requiring such changes in drinking behaviour. Using the analogy of reducing road casualties by encouraging the development of safer cars and by road improvements, or of reducing the number of lung-cancer victims by encouraging smokers to switch to low tar cigarettes, alcohol consumption could be reduced by encouraging the drinking of low-alcohol beverages or by lowering the alcohol contents of standard measures of each type of beverage. Thus, alcohol related ills could be tackled by promoting 'sensible' drinking by encouraging people to drink 'safer' beverages with lower pure alcohol contents.

It may be worth noting that the advent of so-called 'light' beers may represent a step in the wrong direction since they are generally lighter in carbohydrates but with relatively higher pure alcohol contents than standard beers.

In Norway and Sweden levels of excise duty on particular types of beverage are deliberately used to try to direct drinkers to those beverages with the lowest pure alcohol contents. Spirits are taxed at a higher level than wines and beers and there is a threefold classification of beer reflecting the alcohol content with the level

of taxation fixed accordingly. In 1980 the tax on 'strong' beer in Sweden was ten times greater than on 'light' beer [4].

Adopting the Norwegian-Swedish model of alcohol taxes in the UK could provide four main benefits:

- a. there would be an immediate impact on the competitiveness of lower-than-average strength drinks which would carry a lower tax burden, heavier drinkers and those with preferences for high alcohol content beverages would be most affected and the effects of the revised tax structure would be automatically targetted on those whose drinking behaviour causes most concern;
- b. adjusting the pure alcohol levels at which different tax bands operated would encourage manufacturers to reduce the alcohol content of their products;
- c. drinkers would have an incentive to buy the less expensive lower-strength beverages because they would either have to spend more money on purchasing a given volume of pure alcohol or consume less if their spending was not to increase;

d. the amount of alcohol consumed in standard measures of particular beverages would be reduced without otherwise changing drinking behaviour.

The available evidence suggests that it is unlikely that drinkers generally would increase the number of drinks consumed to compensate for a lower pure alcohol content in standard measures. Research has shown that the subjectively experienced, rather than the physical, effects of alcohol are to a considerable extent determined by the drinker's expectations and appear only marginally related to the pure alcohol content of a drink [6,7]. Drinkers' loyalties to the beverages produced by particular manufacturers could be maintained if the pure alcohol contents of existing brands were reduced rather than by the introduction of new products.

There is already some evidence from market research [8] that drivers in the UK are willing to drink the low-alcohol beers and lagers that are presently available. It has been suggested that it only needs a major brewer to promote these products more actively for more drinkers to drink them. The BMA [1] noted that such products have gained a massive share of the traditionally large Australian beer-drinking market following vigorous marketing and lower taxation levels, admittedly with increasingly stringent drink-driving laws.

How the amount of revenue collected from excise duty on alcohol under the proposed structure would change would depend upon the pure alcohol levels at which the various tax bands came into operation. If the level of national per capita consumption was reduced as a result then so would the costs of dealing with alcohol-related ills, both in the short- and the long-term.

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- 1 British Medical Association. 1986. Young people and alcohol. London: Chameleon Press.
- 2 Royal College of Psychiatrists. 1986. Alcohol, our favourite drug. London: Tavistock.
- 3 Tuck, M. 1980. Alcoholism and social policy: are we on the right lines? Home Office Research Study No. 65. London: HMSO.
- 4 Davies, P. and Walsh, D. 1983. Alcohol problems and alcohol control in Europe. London: Croom Helm.
- 5 Knibbe, R.A., Drop, M.J., Van Reek, J. and Saenger, G. 1985. The development of alcohol consumption in the Netherlands: 1958-1981. British Journal of Addiction, 80, pp. 411-420.
- 6 Steele, C.M. and Southwick, L. 1985. Alcohol and social behaviour I: the psychology of drunken excess. Journal of Personality and Social Psychology, 48, pp. 18-34.
- 7 Hull, J.G. and Bond, C.F. 1986. Social and behavioural consequences of alcohol consumption and expectancy: a meta-analysis. Psychological Bulletin, 99, pp. 347-360.
- 8 PAS Ltd. 1984. Beer market survey.

TABLE 1

PRICE AND DUTY PER 10CC ABSOLUTE ALCOHOL
(Supermarket own brands, November 1986)

BEVERAGE TYPE	PRICE PER LITRE	PURE ALCOHOL CONTENT	PRICE PER 10CC PURE ALCOHOL	EXCISE DUTY PER 10CC PURE ALCOHOL
Beer	85p	4.0%	21.1p	8.8p
Wine	2.56	11.5%	22.2p	8.3p
Sherry	3.07	14.5%	21.2p	6.6p
Vermouth	3.17	14.7%	21.2p	6.5p
Spirits	8.34	40.0%	20.8p	15.7p



1 Alex
2 Ruf

FROM: CATHY RYDING
DATE: 3 February 1987

MR ROMANSKI

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Sir P Middleton
Mr Cassell
Mr Scholar
Miss Sinclair
Miss Evans
Mr Cropper
Mr Tyrie
Mr Ross Goobey
Mr Knox - C&E
PS/C&E

VEHICLE EXCISE DUTY

The Chancellor was grateful for your minute of 2 February.

2. On your paragraph 12 :-

- (a) the Chancellor does not want Department of Transport to work on any lorry VED changes;
- (b) Department of Transport can stop work on the rebate scheme needed if lorry VED rates were to be reduced;
- (c) the Chancellor does not want Department of Transport to prepare an option for any change in car VED;
- (d) the Chancellor is content that most minor VED rates should remain unchanged;
- (e) the Chancellor agrees that farmers' HGV rates should be increased to 60 per cent of the main lorry rates;
- (f) the Chancellor agrees that the trade licence rate should be increased to £85 for cars and £17 for motor-cycles;
- (g) the Chancellor agrees that the rate for recovery vehicles should be set at £50.

CR

CATHY RYDING

BUDGET CONFIDENTIAL

FROM: K M ROMANSKI

DATE: 10 February 1987

- B 10/2*
1. MISS SINCLAIR
 2. CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
 Financial Secretary
 Economic Secretary
 Minister of State
 Sir P Middleton
 Mr Cassell
 Mr Scholar
 Miss Evans
 Mr Cropper
 Mr Tyrie
 Mr Ross Goobey

C/letter to issue?

OK-

CR 10/2

Mr Knox (C&E)
 PS/C&E

VEHICLE EXCISE DUTY

Mrs Ryding minuted me on 3 February with your reactions to my minute of 2 February about Budget decisions on VED.

2. I attach a draft letter for you to send to Mr Moore reflecting these decisions. It assumes that they can be regarded as firm. The duty standstills are consistent with either option for excise duties as a whole and, because they form part of pre-announced staged increases, the increases for farmers' hgvs and trade licences could also be consistent with either option.



K M ROMANSKI

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH



From the Minister

CONFIDENTIAL

Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1P 3AG

CH/EXCHEQUER	
REC.	11 FEB 1987
ACTION	
COPIES TO	
	11 February 1987

495 br

HM TREASURY - MCU	
REC'D.	13 FEB 1987
ACTION	FP
	person: 10786/87
	cc APS/CHX
SIGNATURE	CHX
REF No.	12253/87

EXCISE DUTIES ON ALCOHOLIC DRINKS

When I wrote to you on 19 January about other taxation issues, I promised to let you have my views on excise duties following the planned inter-departmental discussions at official level. These have now been held.

Our alcoholic drinks industry provides employment for about 75,000 people and contributes about 0.6 per cent to GDP. The industry is important in terms of its contribution to government funding - some £6.3 billion in excise duties and VAT in 1985. Employment in the industry has, however been falling and is now 27 per cent below what it was in 1980, with the fall in the distilling sector being particularly acute.

The fortunes of the different sectors within the industry have varied over recent years. Beer production and consumption has been falling (with some levelling off in 1986), while wine imports and consumption have shown significant growth. Spirits production has still not fully recovered from the major difficulties in the period between 1979 and 1983 when it fell by 45 per cent. Cider production and consumption which has shown rapid growth in the late 1970s is still stagnating.

Your decision last year to freeze duty levels was widely welcomed by the whole industry. Naturally, they hope for similarly favourable treatment this year. I certainly take the view that it would be damaging if duties were to be increased in real terms. As the analysis above suggests, the sector most able to bear an increase would be wines; but I recognise that the European Court ruling prevents you from increasing duties on wines by relatively more than those on beer. Profitability in the brewing sector has been improving in the last few years and, despite the standstill on excise duties, brewers felt able to increase their prices in 1986. If, therefore, you are

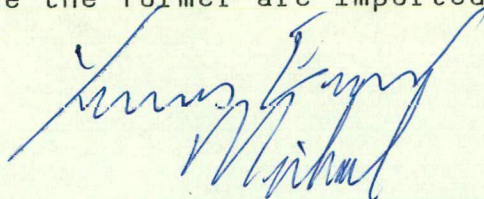
/ disposed to some ...

disposed to some increase in the duty on wines, I could not really argue that this should not be matched on beer, although I would hope that this would no more than match inflation since the last budget.

The position of cider is much more difficult. On the one hand, per degree of alcohol it is subject to a substantially lower rate of tax than beer. But the big increase in duty applied at the 1984 budget was followed by a prolonged period of stagnation in production and consumption from which the industry is only now showing signs of emerging. Nonetheless, if there is to be a modest increase in the duty on beer I think it should probably be matched on cider in money terms or at least to a level which would avoid any increase in the differentials between the duties applied to these drinks per degree of alcohol.

This leaves spirits, which are, of course, still taxed much more heavily than any of the other alcoholic drinks having regard to alcohol content. There is a strong case for reducing this differential as, indeed, you have been doing in all recent budgets. The Scotch Whisky industry continues to face difficulties of falling market shares both at home and overseas. Profitability in the industry is still very shaky and, as you know, the industry has suffered particularly from the abolition of stock relief. I would, therefore, urge you to treat this sector more favourably.

I know that this year's decisions in the alcoholic drinks sector are complicated by the need which you have identified to restructure the duty categories, principally to deal with the complaint of Spanish Sherry importers while protecting the interests of the British Wine and Sherry producers. The proposals which our officials have discussed for a new duty band for 13-15 per cent fortified wines and a reduction in the duties applied to the 15-18% band (which would benefit Spanish Sherry) are, I agree, the least objectionable course open to you; I would hope, however, that the rates for 13-15 per cent fortified wines are kept as close as possible to the light wine rates, and that the reduction in the 15-18 per cent band is not so great as to radically alter the current effective duty differential between British sherry and Spanish sherry. I would also hope that if you follow this solution you will do all you can to avoid widening the differential in duty rates per degree of alcohol between fortified wines and spirits since, generally speaking, while the former are imported, the latter are major UK products.



MICHAEL JOPLING

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH



From the Minister

CONFIDENTIAL

Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1P 3AG

CH/5	11 FEB 1987
RC	
10	

11 February 1987

1495 bf

HM TREASURY - MCU	
RECU	13 FEB 1987
ACTION	FP
	specimen: 10786/87
	CAPS/CHX
SIGNATURE	CHX
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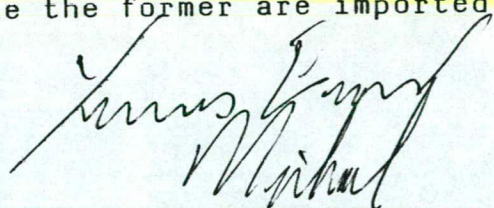
/ disposed to some ...

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MICHAEL JOPLING



plup

Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

11 February 1987

The Rt Hon John Moore MP
Secretary of State for Transport
Department of Transport
2 Marsham Street
LONDON
SW1P 3EB

A large, stylized handwritten signature in black ink, appearing to read 'John Moore'.

Following our meeting on 27 January, I am writing to let you know my decisions on vehicle excise duty rates.

I understand, that following our discussion, you are not looking for any reduction in lorry VED rates. On that basis, I propose to leave main lorry VED rates and the rate for cars and light vans unchanged. I am content for your officials to stop work on the rebate scheme which would have been necessary in the event of duty reductions.

I have also considered the proposals for minor VED rates in the note you handed me at our meeting. I am content with your proposals to leave unchanged the rates for buses, coaches and taxis, motor cycles, pre-1987 cars, agricultural tractors and haulage vehicles and drawbar trailers. I am also content with your proposal that we should implement the final stage of increasing the concessionary rates for farmers' hgv's, and that the new rate for recovery vehicles should be set at £50. But on trade licences, I would prefer a longer staging process, and would propose to set the rates at £85 for cars and £17 for motor cycles.

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Sir P Middleton
Mr Cassell
Mr Scholar
Miss Sinclair
Miss Evans
Mr Cropper
Mr Tyrie
Mr Ross Goobey

Mr Knox (C&E)
PS/C&E

A large, stylized handwritten signature in black ink, appearing to read 'Nigel Lawson'.

NIGEL LAWSON

DOE
Ridley

~~CONFIDENTIAL~~



2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:
Your ref:

The Rt Hon Nigel Lawson MP
HM Treasury
Parliament Street
LONDON
SW1

20 FEB 1987

MR D. DENTON-IR
CST FST EST MST
SIR P MIDDLETON
MR CASSELL
MR SCHOLAR
MR GILMORE
MISS SINCLAIR
MR WIRE
MR WALTERS
MR CROPPER
PSIR
PS/CTE

20 February 1987

Dear Chancellor

I have seen a copy of Richard Luce's letter to you of 8 January about possible tax concessions in the arts and heritage field in the next Budget.

As you know I am always cautious in suggesting further tax concessions for owners of heritage property, considering that they have benefitted like the rest of us from general reductions in taxation as well as from some specific concessions like zero-rate VAT on alterations to listed buildings. However I do think that Richard's particular point about the treatment of interest charges in relation to items accepted in lieu of tax is worthy of support. Representations on this issue have been made to me too and I agree with the convention that we could gain credit from the heritage lobby for what would be a relatively minor concession.

I am not so sure about the suggested review procedure, which looks rather cumbersome to me. I would prefer to see the waiver being initially for a tighter period of, say, nine months, with any extension to be agreed upon by Ministers closely monitoring the case. While I accept that some cases can take longer to process I regard nine months as being an adequate time for the majority to be completed. Perhaps officials should discuss the detail if the principle, to which I hope you will give serious consideration, is agreed.

I am copying this letter to Richard Luce.

Yours sincerely

Isobel A. Ogilvie (Private Secretary)

NICHOLAS RIDLEY

(Approved by the Secretary of State in draft and signed in his absence.)

DRAFT LETTER FROM THE CHANCELLOR OF THE EXCHEQUER

To: Rt Hon Michael Jopling MP
Ministry of Agriculture, Fisheries & Food
Whitehall Place
LONDON SW1A 2HH

ok

Thank you for your letters of 30 December, 19 January and 11 February giving me your detailed suggestions for tax measures in the Budget.

You will not expect me to respond point by point but I do find it extremely valuable to have the comments and suggestions of my colleagues at an early stage.

[NL]

DRAFT

**MINISTRY OF AGRICULTURE: MR JOPLING - 30 DECEMBER, 19 JANUARY AND
11 FEBRUARY**

30 DECEMBER

One representation on capital allowances calling for introduction of a new 100 per cent first year allowance on first £30,000 of expenditure on plant and machinery.

Rates of capital allowances are of general application. The incentive element in the capital allowance system was phased out as an integral part of 1984 reforms designed to produce more neutral system of business taxation. First year allowances for machinery and plant ceased to be generally available on and after 1 April 1986. Relief is now given at rates more closely linked to economic depreciation.

To reintroduce a discriminatory system of allowances would run counter to business tax reform strategy. The Chancellor has already commented "not on" (Mr Kuczys' minute of 5 January). - attached

19 JANUARY

A number of direct tax representations

(A) **CAPITAL ALLOWANCES**

His first point repeats the representations in his letter of 30 December. He now makes one further point on this subject:

MEASURE TO OVERCOME DISINCENTIVE TO DEMOLITION OF REDUNDANT FARM BUILDINGS

Expenditure on the construction of agricultural or forestry buildings or works incurred before 1 April 1986 but after 11 April 1978 qualified for a 20% initial allowance and annual writing down allowances of 10%. Such assets will be fully written down for tax purposes after 8 years.

For expenditure incurred on or after 1 April 1986 the rate of annual writing down allowance is normally 4% and there is no initial allowance. Where an asset, subject to the new rate of allowance, is destroyed, demolished or sold, a system of balancing adjustments operates, at the option of taxpayers; this enables allowances given to be brought into line with depreciation actually experienced.

The new system thus already provides an incentive to the demolition of redundant farm buildings since this will be an event likely to trigger a balancing allowance.

A system of balancing adjustments would not be compatible with the former system of allowances and would in any event be of no incentive value in the case of buildings or works more than 8 years old. Incentives to demolition, where needed, would be better dealt with by way of grant than via the tax system.

(B) CAPITAL GAINS TAX

MOVE BASE DATE FORWARD PROGRESSIVELY FROM 1965 TO 1982 FOR EXEMPT GAINS ON ASSETS HELD FOR MORE THAN 10 YEARS

The object is to provide full or substantial relief for the accrued inflation content of pre-1982 capital gains (although the alternative proposal would go much wider). Such relief was ruled out on grounds of cost at the time of the 1984 Review. Either suggestion would also exempt real gains as well and this could have capricious effects; in particular, landowners would benefit to a far greater extent than those who had invested in equities. Moreover, cut-off schemes tend to be complex (problems with losses and share pools) and would cause market distortions.

INCREASE MONETARY LIMIT FOR SMALL PART DISPOSALS RELIEF

Ministers have considered and rejected this proposal.

ALLOW LANDOWNERS TO CARRY FORWARD ANNUAL EXEMPTION

The annual exemption, which is extremely generous compared with the main income tax allowances, was introduced in order to keep thousands of small cases out of the system altogether. A carry

forward (which in practice would be difficult to restrict to landowners alone) would remove the administrative benefits of the exemption and impose a more onerous compliance burden on taxpayers to report all small gains and losses to establish unused amounts.

ALLOW CGT RETIREMENT RELIEF TO FARMERS WHO RETIRE FROM FARMING AND THEN LET FARMLAND

Capital gains tax retirement relief is broadly designed to give a measure of relief to businessmen aged 60 or over, who have been obliged to reinvest money in their business at the expense of adequate pension arrangements and who fund their retirement out of the proceeds of the disposal of their businesses. The relief is available providing the disposal takes place within 12 months of retirement or longer in certain circumstances. The relief is not however available on the disposal of investments of any kind, including land which is let. To extend the relief in the circumstances outlined would effectively be to give relief on investment assets and would undermine the principle of the relief itself and set a very costly precedent. Again it is not clear that agricultural landlords are in a special position when compared with other individuals who may wish to let business premises after retirement.

(C) AGRICULTURAL LANDLORDS

ALLOW CGT RETIREMENT AND ROLLOVER RELIEFS TO PRIVATE AGRICULTURAL LANDLORDS

These reliefs are only available, broadly, to persons carrying on a trade, profession or vocation: and not to those who let land even if that land is used for business purposes. It is not clear that agricultural landlords are in so special a position compared with other commercial landlords. The justification for the proposal is the need to revitalise the tenant farm sector, but it is unclear how much effect the extension of these reliefs would have. Many large landowners are exempt bodies such as charities and pension funds. Moreover, much of the benefit of any change would accrue to existing landlords. It is likely that the provisions of the Agricultural Holdings Act will be of greater significance, and the benefits of the tax relief disproportionate to the difficulties arising from breaching the principle that the CGT reliefs are not available for let assets. To extend the retirement relief to lettings would in effect be to give relief on investment assets, which would undermine the principle of the relief itself and set a very costly precedent

(D) INCOME TAX

REPEAL SECTION 180 OF THE INCOME AND CORPORATION TAXES ACT 1970

Section 180 ICTA 1970 restricts sideways relief against other income for farming losses where losses have been made in each of the previous five years. However, there is a let-out for genuinely long-term farming operations. Also, Section 180 does not prevent farmers from obtaining relief in other ways eg losses can still be carried forward against future farming profits.

Contrary to what MAFF's representation suggests, Section 180 does not impose a very much stricter regime on farmers than applies to other traders. Under Section 170 ICTA 1970 other traders can lose sideways relief for their losses if there is evidence that they are

not operating on a commercial basis. When set against this, the objective test provided by Section 180 does not seem ungenerous. We are not aware of farmers (as opposed to hobby farmers) having any general problems with this provision.

Confidential: The possibility of tightening the rules for hobby farming losses was recently considered as part of a strategy for removing tax shelters. Ministers decided that action on this subject should not be pursued.

(E) CONSERVATION

BENEFIT OF DOUCEUR ARRANGEMENTS TO BE EXTENDED TO RSPB AND OTHERS

Land of heritage quality can be sold to specified national bodies with the benefit of tax exemption under the "douceur arrangements" (whereby the value of the tax exemption is shared between the vendor and the purchaser). Mr Jopling recommends that voluntary conservation bodies, such as the Royal Society for the Protection of Birds and the Royal Society for Nature Conservation, should be added to the list of specified national bodies, which is now in Schedule 3 of the Inheritance Tax Act 1984.

This point has been considered by the Government on a number of occasions in recent years. The conclusion has been that in order to protect the heritage the special purchase advantages conferred by inclusion in Schedule 3 ought not to be made too widely available. It should be limited to bodies which are largely dependent on Vote or local authority finance and to the few, nationally pre-eminent organisations already nominated which can be relied upon not to abuse the terms of Schedule 3 by on-selling property acquired with the benefit of tax exemption. If the qualifying conditions were relaxed, it would be difficult to re-draw the boundaries satisfactorily - for example, to make distinctions between a number of privately run charities and other organisations that are also likely to press for inclusion in the list

The Financial Secretary is currently considering the point. Inland Revenue recommend no change (Mr Denton's note of 11 February).

(F) HOLIDAY LETTINGS

REDUCE QUALIFYING CONDITIONS LAID DOWN IN SECTION 50 OF THE FINANCE ACT 1984

The shorter holiday season in the more remote parts of the country was fully taken into account in framing the qualifying conditions which must be satisfied if proprietors of furnished holiday lettings are to claim the tax reliefs associated with treatment as a trade for tax purposes. The original proposal, which was drawn up after consultation with the tourism industry, was that accommodation should be available for letting for 180 days a year and actually let for 90 days. However, to meet this problem, these were subsequently relaxed during the passage of the 1984 Finance Bill to 140 and 70 days respectively.

The qualifying conditions are intended to target the relief on genuine holiday letting businesses and there is a danger that any further relaxation in the rules would enable second home owners to benefit from the legislation. Most genuine letting businesses

should be able to satisfy both the 140-day and 70-day requirements and, indeed, there must be some doubt about the viability of those that can not. We have seen no evidence to suggest that these conditions are causing significant problems.

11 FEBRUARY

Mr Jopling's third letter is in respect of excise duties on alcoholic drinks.

He is against any large increase in drinks duties. He hopes for no more than revalorisation on beer and wine, less than revalorisation on spirits and an increase on cider either to match that on beer in money terms or at least to a level which would avoid any increase in the duty differential (per degree of alcohol) between beer and cider.

Comment

Final decisions on main excise duties not yet taken.

Mr Jopling^g also hopes that in restructuring the wine duty:

- (a) The rates for 13-15 per cent fortified wines are kept as close as possible to light wine rates
- (b) The reduction in 15-18 per cent band not so great as to radically alter current effective duty differential between British sherry and Spanish sherry.
- (c) The duty differential (per degree of alcohol) between fortified wines and spirits is not increased.

Comment

- (a) The proposed increase does not keep the rates close.
- (b) Proposed reduction of one-third minimum necessary to show good faith in answering the Spanish sherry shippers' complaint.
- (c) Final decisions on rates not yet taken.



cc Chief Secretary
 Financial Secretary
 Economic Secretary
 Minister of State
 Sir P Middleton
 Mr Scholar
 Miss Sinclair
 Mr Walters
 Mr Romanski
 Mr Cropper
 Mr Tyrie
 Mr Ross Goobey
 PS/C&E
 Mr Knox - C&E

Treasury Chambers, Parliament Street, SW1P 3AG
 01-270 3000

3 March 1987

The Rt Hon Norman Fowler MP
 Secretary of State for Social Services
 Department of Health and Social Security
 Alexander Fleming House
 LONDON
 SE1

1. Copy
2 pup

Norman

Thank you for your two letters of 16 January giving me your detailed suggestions for taxation of alcohol and tobacco.

You will not expect me to respond point by point but I do find it extremely valuable to have the comments and suggestions of my colleagues at an early stage. On the point you make about low alcohol beers and wines, you will have seen my letter of 3 March to Douglas Hurd.

A copy of this letter goes, as yours, to Malcolm Rifkind, Nicholas Edwards and Tom King.

Yours ever
Nigel Lawson

NIGEL LAWSON

MR FOWLER

DRAFT LETTER FROM THE CHANCELLOR OF THE EXCHEQUER

To: Rt Hon Norman Fowler MP
 Department of Health and Social ^{Security} ~~Services~~
 Alexander Fleming House
 LONDON
 SE1

OK ✓

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taxation of alcohol & tobacco

You will not expect me to respond point by point but I do find it extremely valuable to have the comments and suggestions of my colleagues at an early stage. On the point you make about ^{low} alcohol ~~related violence~~, you will have seen my letter of [] to Douglas Hurd. ^{beers & wine} A copy of this letter goes, as yours, to Malcolm Rifkind, Nicholas Edwards and Tom King.

[NL]

DRAFT

DHSS

DEPARTMENT OF HEALTH AND SOCIAL SECURITY: MR FOWLER - 25 JANUARY
2 (letters)

Mr Fowler's first letter concerns alcohol duties. He argues for over-revalorisation of alcoholic drinks on health grounds. He also expresses desire to be involved in any further discussion on reduced taxation of low alcohol beer and wine.

Comment

Final decisions on main excise duties have yet to be taken.

On the question of further discussion on low alcohol beer and wine, Customs' submission on Mr Hurd's representation (Mr Jefferson Smith of 12 February - copy attached for ease of reference) includes a proposal to set up an inter-departmental working group on this subject.

Mr Fowler's second letter concerns tobacco. He argues for a substantial increase in taxation again on health grounds.

Comment

Final decisions not yet made on excise duties.



RS

Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

3 March 1987

Rt Hon Michael Jopling MP
Minister of Agriculture, Fisheries and Food
Whitehall Place
LONDON
SW1A 2HH

Stan Michael

Thank you for your letters of 30 December, 19 January and 11 February, giving me your detailed suggestions for tax measures in the Budget.

You will not expect me to respond point by point but I do find it extremely valuable to have the comments and suggestions of my colleagues at an early stage.

Nigel Lawson

NIGEL LAWSON

cc Chief Secretary
Financial Secretary
Economic Secretary
Sir P Middleton
Mr Cassell
Mr Scholar
Mr Gilmore
Miss Sinclair
Mr Burr
Mr Walters
Mr Cropper



120

Treasury Chambers, Parliament Street, SW1P 3AC
01-270 3000

PS/IR
Mr D Denton - IR
PS/C&E

3 March 1987

The Rt Hon Nicholas Ridley
Secretary of State for the Environment
Marsham Street
LONDON
SW1

Nigel Lawson

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You will not expect me to respond point by point but I do find it extremely valuable to have the comments and suggestions of my colleagues at an early stage.

I am copying this letter, as yours, to Richard Luce.

Nigel Lawson

NIGEL LAWSON

DRAFT LETTER FROM THE CHANCELLOR OF THE EXCHEQUER

To: Rt Hon Nicholas Ridley
Secretary of State for the Environment
Marsham Street
LONDON SW1

NL

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[NL]

DRAFT



12

Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

3 March 1987

The Hon William Waldegrave
Minister for the Environment
Marsham Street
LONDON
SW1

Wm Waldegrave

Thank you for your letter of 25 January giving me your detailed suggestions for tax measures in the Budget.

You will not expect me to respond point by point but I do find it extremely valuable to have the comments and suggestions of my colleagues at an early stage.

Nigel Lawson

NIGEL LAWSON

DRAFT LETTER FROM THE CHANCELLOR OF THE EXCHEQUER

To: The Hon William Waldegrave
Minister for the Environment
Marsham Street
LONDON SW1

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You will not expect me to respond point by point but I do find it extremely valuable to have the comments and suggestions of my colleagues at an early stage.

[NL]

DRAFT

British Shipping Review 1987



Invest or Vanish

The question that has to be asked in 1987 is whether the political will exists to ensure that there is a British merchant fleet of sufficient size to meet the nation's needs in the next decade and beyond. The UK owned and registered fleet declined dramatically in 1986. At the 31st December, 1985, there were 627 ships (of over 500 gross registered tons) totalling 15.9 million deadweight tons which by the end of November 1986 had declined to 523 ships of 10 million deadweight tons. (Some 75 of these ships totalling around 3 million deadweight tons are registered in the Isle of Man.) In addition, around 160 ships of about 7.0 million deadweight tons controlled by UK companies are registered abroad. Figure A shows how the fleet has declined over the last 10 years.

This fleet is bound to decrease further if present circumstances continue to prevail. There is no apparent slackening of the pace at which existing ships are being sold or transferred to more hospitable registries. Orders for new tonnage have virtually dried up, having declined from 363,000 deadweight tons in 1983 to 5,000 deadweight tons in the first nine months of 1986.

GCBS has warned the Government for some years that the UK owned and registered merchant fleet was facing unprecedented difficulties but even within the industry this rate of decrease was not expected. In 1985, the GCBS forecast that by 1990 there would be between 400 and 500 ships of 7 – 10 million deadweight tons and 300 – 400 ships of 5 – 7 million deadweight tons by 1995. Even the lower of these estimates now looks wildly optimistic. Unless present trends can be reversed, we can see no reason why the mainland UK fleet should exceed 100 ships by 1995.

It takes a long time to build up a sizeable merchant fleet and even longer to train the seafarers who will man it. Action is needed now to reverse the decline. Fortunately there is still time to act — the world fleet that will be trading in the year 2000 for the most part has yet to be built.

Why has the British fleet declined?

In part because it cannot be insulated from world conditions. The tanker slump

Figure A.

UK Owned Trading Fleet Over 500 grt

	31.12.75		31.12.82		30.11.86	
	mn. dwt	No.	mn. dwt	No.	mn. dwt	No.
UK owned and registered	50.0	1614	24.8	868	10.1	523*
UK owned, registered in British Territories overseas (partially estimated)	N/A	—	1.2	50	4.1	75
UK owned, foreign registered (partially estimated)	N/A	—	2.8	105	2.5	90
TOTAL	50.0	1614	28.8	1023	16.7	688
UK fleet as percentage of world fleet	8.9%		4.2%		2.9%	

* Includes some 75 vessels of 3.0 million deadweight tons registered in Isle of Man and Channel Islands.

N/A Not available, but known to be small.

that began in the early 1970s and still continues is well documented as is its spill-over into all other sectors of the industry, to a large extent because otherwise redundant shipyards around the world have been enabled by government subsidies to sell ships at well below cost. Britain has always been strong in the liner trades so the impact of containerisation — which replaced 7 ships by 1 — necessarily appeared severe, even whilst the productivity of the fleet increased dramatically. Furthermore, the operations of shipowners based in low cost countries in the Far East and the Soviet bloc has grown significantly over the last 10 years. Ship operators from high cost countries have to reduce their costs or sell their ships.

The British registry is far from alone in suffering significant reductions. For example, the Norwegian flag fleet has declined since 1975 from 45 to just over 11 million deadweight tons and the West German fleet from 13 to 6 million deadweight tons. In addition, both these countries, like Britain, also operate substantial tonnage under foreign flags — in their case about 40 per cent in terms of ships and 45 per cent in terms of tonnage. And British companies may well have judged markets better and sold

loss-making ships earlier than some of their competitors; the casualty list among British companies has been very small. This commercial reaction was right. Loss-making activities have to go. But the need for sea transport goes on, and if British operators are to maintain a substantial presence in world maritime affairs, they cannot be left devoid of assistance at the level accorded to their principal competitors.

In 1987 the free market in shipping no longer exists. It is true that cargo reservation, although far too extensive for comfort, is not as widespread a threat as is sometimes alleged. But on the supply side, governments the world over, from our EEC colleagues to the developing world, from the USA to the Soviet bloc, from Japan to Brazil to Korea, all give very substantial fiscal aid to their shipowners, either direct or through their shipyards.

Britain also gives some aid through the tax reliefs available to all industries. But not nearly as much as many of our competitors or as much to industries in the UK that are located in development areas. The most important aid that was available to British shipping was withdrawn in 1984 just at the time that the need for help was increasing.



P & OCL's LIVERPOOL BAY in Hong Kong harbour.

Shipowners' costs where there is scope for variation between countries, fall into two main areas — capital costs and labour costs.

Labour costs can be tackled by shipowners (though governments can be helpful or hinder as is explained in the next section). It is to reduce these costs that many ships are flagged out — not to evade safety standards or taxation.

The other major cost is the cost of finance. Before 1984 British shipowners enjoyed a favourable fiscal regime that allowed them to write off quickly the cost of a ship against their taxable profits. This was broadly comparable in effect to the wide range of aids and subsidies available to our competitors. It was also highly successful. In the 10 years from 1975 to 1984, whilst the fleet was declining by 30 million deadweight tons, 12 million deadweight tons of new ships were bought.

This regime was removed by the 1984 Finance Act as part of a general reform of corporate taxation and the impact on investment in the industry was devastating. Ships on order for UK registry plummeted from 363,000 deadweight tons in 1983 to only 5,000 deadweight tons in the first nine months of 1986. Unless action is taken there is unlikely to be significant investment in ships of any flag by the British shipping industry.

GCBS has suggested to the Government a number of measures that would help relieve our capital costs. They are:

- (a) a 50 per cent ship allowance for investment in new or secondhand ships. This would go far to restore the pre-1984 position. It is an essential step if the larger, high cost units of the fleet are ever to be replaced;
- (b) roll-over relief for balancing charges. The tax allowances on the sale value of a written down ship now have to be repaid to the Inland Revenue. GCBS would like to see these retained in the industry, *provided* they were reinvested in a new ship within a relatively short period. This would be in line with the practice of many of our competitors as well as the existing rules for Capital Gains Tax and would be of significant encouragement to reinvestment in shipping;
- (c) some modifications to the rules of the Business Expansion Scheme to enable it to be more widely used by shipowners. For example, the rule that half the voyages of a ship must include a visit to a British port is a major impediment to worldwide — or even Europe-wide — trading. Given suitable changes the BES has

considerable potential to assist owners expand the UK fleet by purchasing good second-hand ships — and thereby not adding to the ship surplus.

None of the GCBS proposals involve cost unless the ventures concerned are successful. Then they merely defer tax, and unlike a subsidy are not a permanent drain on the Treasury. They reflect the assistance given elsewhere in the economy by way of Regional Development Grants or through the BES scheme.

Why should the Government act? Not because shipping companies or their shareholders want to depend on government help, but because the country needs a shipping industry. The defence needs are obvious and well known; not only in direct support of the armed forces but also to ensure civilian supplies in an emergency — an issue which is beginning to concern NATO. The need is not only for ships but for men. The balance of payments benefits have always been large and become more significant as the North Sea bonanza

glitters a little less brightly. At present they are shrinking and the nation's sea transport account shows a billion pound deficit. As a trading nation Britain surely cannot depend exclusively on others for shipping services. And employment, not only at sea and in shipping company offices but also in the ancillary industries, must be important.

The decision is the Government's — and ultimately the country's. A major national asset is wasting away. But it need not.

The first British ship to be fitted with advanced auxilliary sail power, pictured in the Solent.



Which Flag, and Why?

Flagging-out on the scale experienced during 1986 is unprecedented in the history of the British shipping industry. But it is nothing other than a strategy for survival which has nothing whatever to do with avoidance or evasion of maintenance or safety requirements. Whatever the flag, the ship is as good as its owners, managers and seafarers make it, and the cost reductions which enable a UK company to keep its ships rather than have to sell them and charter in other peoples do not entail any compromise on standards. Neither has it anything to do with tax evasion. British shipping companies are liable to tax wherever their ships are registered and a safe ship is a commercial necessity. All ships are supervised by the European port state inspection system. What flagging-out does represent is a strategy to bring crew costs closer to those of our major competitors. And British shipowners are not alone in this endeavour. The greater part of the US fleet has long been flagged-out as have large parts of the fleets controlled by Japanese, Greek and, increasingly, German and Norwegian shipowners, to name only a few developed countries whose owners have had to take this step.

It is, of course, nothing new that a part of the British fleet has to be manned by foreign seafarers if it is to be competitive. Since the days of the Honourable East India Company seafarers from the Indian sub-continent have been employed on British ships. As late as the end of 1976, 20,000 such seafarers, together with others from Hong Kong, Singapore, West Africa and elsewhere, were employed on over 550 British ships — more than one-third of the then fleet — at locally agreed rates of pay.

With the increasing surplus of UK ratings, there has been growing resistance from the NUS to the employment of low cost non-domiciled seafarers on UK registered ships. As a result the option of employing foreign seafarers on new UK registered ships has by now effectively vanished. In most cases the only alternative to disposing of a marginally economic ship now is to flag it out.



Not all such ships employ foreign crews. Most retain British officers, at least in the senior ranks. In a number of cases the shipowners have been able to conclude special agreements with the British seafarers' unions permitting the continued employment of their members. For example, an approach that has been adopted by some companies flagging-out is the negotiation of a gross wage with lower fringe benefits from which the seafarer can make his own arrangements for medical insurance and pension contributions and which can legitimately qualify for 100% tax relief. The significance of the potential saving may be assessed by the fact that, for the average officer or rating serving on a UK ship, the difference between what his employer pays out and what he actually receives lies in the region of 40% to 45% in the area of direct wage costs alone.

A major potential saving under some of these agreements arises from reductions of leave from the high levels negotiated by many companies in the 1970s, when there was a shortage of qualified officers in particular, to levels more in line with the international norm. Of course the

higher the leave entitlements of individuals the more relief-crew members have to be employed to cover their absences. GCBS is discussing possible improvements in this area with the officers union NUMAST.

In order to make flagging-out less necessary, GCBS has asked the Government to introduce a special tax regime for seafarers. Until 1984 most seafarers benefitted from the tax concession available to all UK residents who worked away from the UK for 30 days or more. Shipowners believe that an easing of the rules here would enable better agreements to be negotiated for vessels remaining on the UK mainland register.

We acknowledge the importance of the Secretary of State for Transport's recent announcement that the Government was prepared in principle to assist with training and repatriation costs. This is very welcome but its impact will not be known until the details have been worked out. It is most unlikely that these measures themselves will be sufficient to counter the commercial attraction of flagging-out.

EC: A Policy for Shipping

A major policy development of the year was the adoption in December by the EC's Council of Transport Ministers of the first stage of a Community Shipping Policy. This followed doggedly persistent activity by both the Dutch and the UK Governments (which held the Presidency of the Community during the first and second halves of the year respectively). Community governments were clearly influenced by the likely introduction of the majority voting procedure in shipping (as opposed to the present requirement for unanimity) from January.

The policy package was warmly welcomed both by GCBS and by CAACE, the EC shipowners' organisation.

It comprises four new regulations. Two deal with external shipping policy and will give positive support to Community shipping companies when faced with hostile legislation and the unfair practices of other maritime nations. The first

provides a programme of co-ordinated action to counteract protectionist activity by other countries, designed to safeguard free access for EC ships to cargoes in ocean trades. It provides for a procedure of diplomatic representations to offending countries and, where those fail, specific counter-measures aimed at correcting the harm to EC operators caused by such practices. The second regulation provides protection for EC liner shipping companies from unfair pricing practices or "dumping" in shipping by state owned or supported companies which damage the Community shipping industry. It is analogous to the anti-dumping Regulations that have protected Community manufacturing industries for many years. Both of these regulations come into force from July 1987.

The other two regulations are more introspective. The third applies the Community's Competition Rules to shipping, acknowledging the social value of liner conferences by creating a formal group exemption for conference agreements, subject to a number of qualifications. The regulation meets a

long-standing obligation on governments under the Treaty of Rome. However, a number of important issues are still being studied, including the treatment of liner consortia.

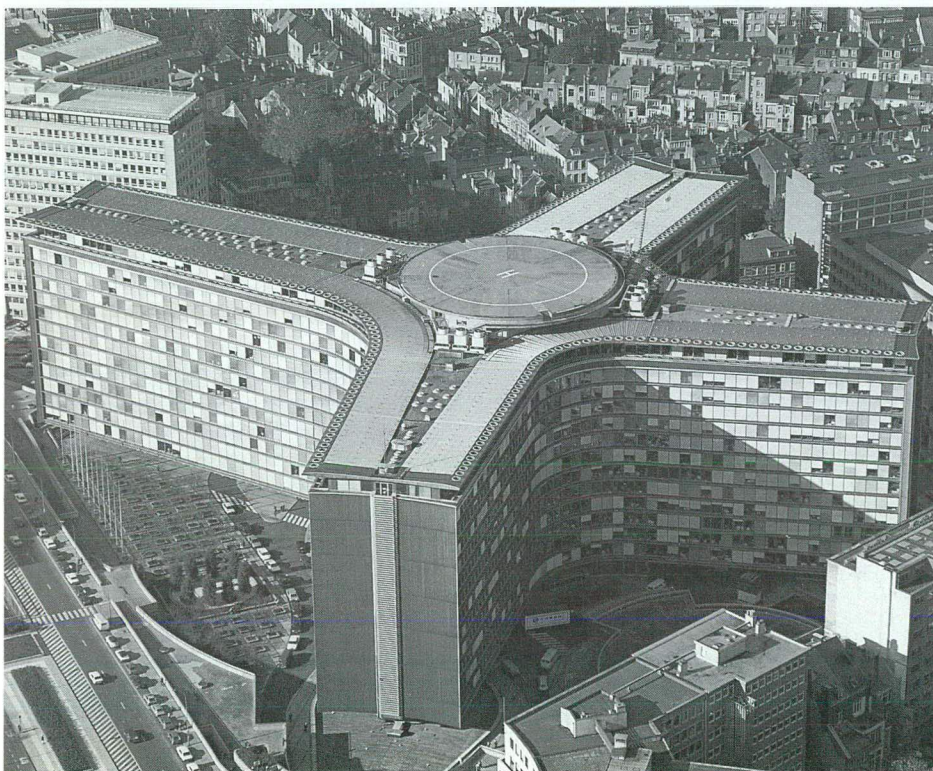
The fourth regulation, also dealing with internal Community shipping relations, was the most contentious. It applies the fundamental Community principle of freedom to provide services to the maritime transport sector. It lays down a timetable for the removal of cargo reservation measures in individual Member States and also of cargo-sharing arrangements contained in bilateral agreements between Member States and third countries. GCBS has welcomed this regulation, although the length of the timetable for phasing out the restrictions was disappointing.

A serious omission, however, was the failure of governments to come to any agreement to eliminate restrictions in the national coastal trades of individual Member States — i.e. cabotage and restrictions in the offshore sector. This was no surprise, since it was always likely to be the most difficult and sensitive area. However, the injustice remains that the UK coastal trade is open to all-comers, both within and outside the Community, while half of the EC states reserve their cabotage trade to ships flying the national flag. The UK Government has made its position on this issue quite plain to other Member States and has warned that it would take unilateral action if no progress could be achieved in Brussels.

UK owners now look to the Government to fulfil its promise, either by taking a case before the European Court in order to open cabotage trades within the Community, or by compensating UK operators through the closure of the British coast.

Now that governments have acknowledged that the EC has a specific role to play in shipping, GCBS and CAACE are preparing for the second stage of the Common Shipping Policy. The European Commission has promised a second proposal during 1987, dealing in particular with the issues of ship financing, employment, and technical standards. In these and other areas, including scrapping policy, CAACE has called for urgent further EC action to help strengthen the competitive position of Community fleets.

The Berlaymont Centre, Headquarters of the European Commission.



Let There Be Light — If You Pay!

The users of British ports are subjected to a special tax that is not levied in any other North European country except Ireland and Sweden. This is the imposition of light dues, used to fund the provision of lighthouses, navigational marks and buoys and, since January this year, the electronic position-finding device known as the 'Racal-Decca Navigator'. In most European countries these are funded out of general taxation. In the UK they are paid for by commercial ships entering ports in the British Isles. A large containership coming up the Channel pays some £14,000 if it turns left into Southampton, and nothing at all if it turns right into Le Havre, Antwerp, Rotterdam, Hamburg, etc.

This is a powerful disincentive for shipowners to use British ports. A report produced by the Department of Transport statistical service on Liner Shipping and Freight Rates, published in March 1986, acknowledged that light dues were an important factor in putting up the cost of shipping services out of the UK ports and in discouraging competition. GCBS, together with the British Ports Association, the British Shippers' Council, the Freight Transport Association and the Association of British Chambers of Commerce, has suggested that this burden should be borne by Government. Not only have they been turned down but the cost of providing the Racal-Decca Navigator system — a vital navigation aid — now has also been placed on the light dues system.

This would matter less if either shipowners got value for money or light dues were allocated fairly. Neither is the case.

In the first place very few ships operated by GCBS members need the vast number of lights, buoys, fog horns and other navigational marks that have been erected over the centuries. For the most part, they pre-date the invention of radar and of the Racal-Decca Navigator. Within five years cheap, high quality, satellite navigation systems will enable almost any merchant ship to fix its position within 100 metres, day or night, in sunlight or in fog. Of course, some fixed aids are still useful and some vessels need more than others, particularly yachts.

But modern merchant ships need less aids, and many that they do need, in the approaches to ports, are provided by Harbour Authorities and are funded separately.

Secondly, those who most need the lights and other aids pay nothing at all towards their cost. The Government has consistently refused to impose light dues on yachtsmen, although these recreational navigators have only limited equipment at their disposal and need more of the traditional navigational aids. Fishermen and Royal Naval vessels are also currently exempted from making any contribution to costs. In contrast Sweden, the other North European country that recovers the full cost from light dues, charges yachtsmen, fishermen and the Royal Swedish Navy as well as merchant ships.



The Needles lighthouse.

A further expensive anomaly arises from the funding of the navigational aids around the Irish Republic out of the same General Lighthouse Fund that pays for the aids around the UK coast. Despite a recent agreement between the two Governments which increases the Irish contribution to the fund, navigational aids in the Republic are, and will continue to be, substantially subsidised by dues

collected from ships using UK ports. GCBS believes there are no comparable cases — in Europe at least — of navigational aids of one independent state being subsidised by taxes raised in another country.

The cost of providing the lighthouses and other navigational aids in the UK and Ireland is very substantial. The 1987/8 budget for Trinity House, the Northern Lighthouse Board and the Commissioners of Irish Lights is expected to total some £60 million. Yet the number of users — or at least payers — is declining as ship sizes increase and in some cases trade diminishes. A 14 per cent increase in light dues was announced in February, and strongly resisted by shipowners, shippers and port authorities. Unless there is a radical reform, further excessive increases in light dues are inevitable in the future.

GCBS believes that, whoever pays, increases in costs could be mitigated by a thoroughgoing review of the number and type of aids currently provided. There also appears to be scope for more economical administration. The Department of Transport has recently imposed new financial disciplines on the three General Lighthouse Authorities. It has also instigated no fewer than three investigations by consultants into various aspects of their operating and administrative practices.

The fact remains, however, that the three authorities together employ nearly one-and-a-half people for each navigational aid that they provide, whereas the National Swedish Administration of Shipping and Navigation provides nearly four navigational aids for each person employed. Furthermore, the Swedish Administration also fulfils many other safety duties performed in the UK by the Department of Transport, the Hydrographer of the Navy, and the pilotage authorities, as well as operating eight ice-breakers.

Expensive light dues are not just a problem for shipping companies. They are paid for by all of us who eat New Zealand lamb, wear Far Eastern shirts, drive a Japanese car on Middle Eastern petrol or who burn Polish coal. They also affect all who work in exporting industries. In short, almost everyone.

In The Arabian Gulf



For nearly three years the war between Iraq and Iran has affected all shipping entering the Gulf. The origins of the conflict lie in a long-standing argument over control of the Shatt-al-Arab waterway, formed by the confluence of the Tigris and Euphrates, although other considerations have now assumed greater significance. This is Iraq's only access to the sea and is of great strategic importance to them. The border between the two countries lies on this waterway and near its mouth Iran is able to control access to Iraqi ports.

Under pressure from other OPEC states, Iran and Iraq reached an agreement regarding their border in 1975, but this detente only lasted until 1979 when the Shah of Iran was overthrown. The Ayatollah Khomeini had been living

in Baghdad in exile for 15 years until 1978 when the Shah asked the Iraq leadership to expel him. Khomeini went to Paris and from there was able to orchestrate the revolution. His expulsion from Baghdad antagonised the Ayatollah against the Iraqi leader, Saddam Hussein and, following the Islamic revolution in 1979 in Iran, Khomeini called for revolution against the Iraq regime.

Hostilities opened in 1980 with the Iraqi invasion across the Shatt-al-Arab. It took some 2 years for those forces to be dislodged and the hostilities left some 80 ships trapped in ports such as Basra and Korramshahr. These vessels are still there. With Iraq having no access to the sea they have sought since 1983 to deny the use of the Gulf to vessels serving Iranian interests, and to strangle their enemy's vital oil exports.

Around 8 million barrels of oil per day

pass through the Straits of Hormuz. This is some 20 per cent of the total world production and represents the equivalent of five 250,000 ton tankers. Although Britain is not dependent on Arab oil there are significant exports from the UK to the region. An average of five or six UK vessels per week go in and out of the Straits. Several British vessels are permanently based there.

Iraq's targets were initially vessels on passage to or from the Kharg Island oil terminal, and subsequently the Sirri Island oil terminal and, in late 1986, Larak island terminal far to the south. Attacks on vessels at sea have been carried out with Exocet missiles fired from Super Etendard and Mirage 5 aircraft.

Iran has sought ways both to retaliate and counter these Iraqi attacks. In 1984 they adopted a policy of attacking vessels

they suspected were serving Iraqi interests. The first few attacks took place near the Saudi Arabian coast, but after two Iranian aircraft were intercepted and destroyed by the Saudi Arabian airforce they have taken place in less well guarded areas of the Gulf.

In the second half of 1984 and the first half of 1985 Iranian Phantom aircraft conducted many attacks in the Eastern basin of the Gulf. Iran then used helicopters apparently based on oil platforms in the centre of the Gulf. In the last few months they have used their naval forces to attack vessels just outside the territorial waters of the United Arab Emirates.

For the past three years GCBS has recorded the movements of all UK based vessels in the Gulf and is seeking ways to monitor the movements of all British

controlled vessels, regardless of flag. This information is passed to interested Government departments, including the Ministry of Defence.

GCBS has acted as the central link for information with regard to attacks on merchant ships, liaising both with owners and with the Government to ensure that the most useful conclusions are drawn from such information. Advice from the MOD on the weapons being used has been obtained and owners have been advised of measures which may be taken to reduce the chance of attack from either side. The latest series of attacks by the Iranian navy has resulted in a higher profile being taken in the area by the Royal Navy.

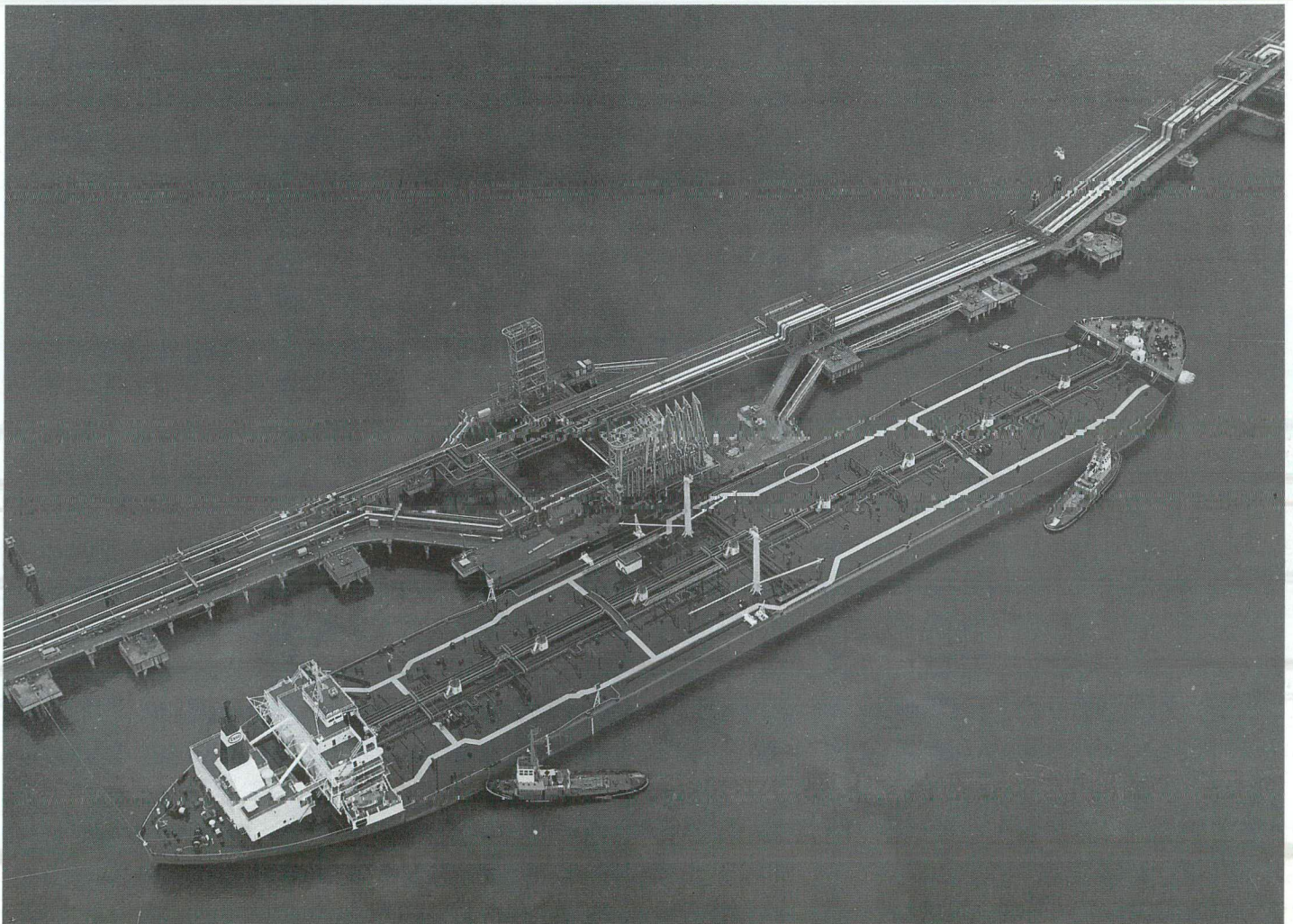
Areas of particular risk have been identified and there have been negotiations with the seafarers' unions to

ensure that their members only enter these areas voluntarily, and receive an agreed bonus.

All this information and advice has been accumulated into a set of Guidance Notes for Owners and Masters which are made available to members. The notes, which are kept under constant review and are now in their tenth edition, have also been made available to the international shipping community.

There appears to be no early end in sight to the war and the shipping industry fears that attacks on shipping will continue. Pressure has been brought to bear on governments nationally and internationally to urge them to show more concern at these flagrant breaches of international law and exert effective pressure on the belligerents.

Berthing at an oil terminal.



Offshore — Off Hire?

Everyone has come to understand that oil prices are a volatile factor in the world economy. A depressed oil price may bring short term benefits at the petrol pump but the wider implications — not least for the United Kingdom — have sunk in. Thus there is little need to emphasise that the offshore world is in crisis. Production has been reduced, exploration and development have been cut back — savagely. This collapse in activity is worldwide. But our priority for concern and a revival of confidence is in our own back yard — our sector of the North Sea and the other waters around the United Kingdom — our Continental Shelf. For ours is by far the most significant sector in the EEC, indeed Europe generally, and is a major sector in the world league.

Warnings about our reserves running

down and revenue from North Sea oil declining have to be put into perspective. They may not last for ever and it may be that today we have to plan in terms of a 40 or 50 year span of availability. But within such a period there is much to benefit the nation and much to sustain several branches of industry. What is more, technological advances and new discoveries will probably extend our “shelf-life” as an oil producer.

For example, within our Continental Shelf area we currently have some 32 offshore oil fields and 16 offshore gas fields in production. 153 major discoveries are as yet undeveloped and therefore available for production — including the largest of all the “Clair Field”. All this is in only a quarter of the British sedimentary basin. There are large areas west of Scotland (the Rockall Trough) which have not yet been touched. They await the 21st century and further advances in technology — which will

surely come. The offshore industry has a future!

So there is ample justification for the nation to stand by the British companies that have done so much to create the services on which this young industry depends and who are now hanging on, desperately hoping to survive — for survival is now the name of the game. For the nation — and that includes the Government — to turn its back on these problems and leave the market place to work things out would be irresponsible. If British offshore fleet operators do not survive the current crisis so as to be able to compete for the opportunities yet to come, we will have cast a vital strategic British service industry to the mercy of foreign operators. Many of these foreign operators will have survived because they were supported by a protected, indeed subsidised, home base.

The fleet which has been developed, indeed to a large extent invented, to serve

A platform supply vessel which supports offshore drilling rigs and production fields.



the UK's offshore industry covers a fascinating array of operations:

- Anchor Handling and Towing
- Platform Supply
- Standby Safety
- Seismic Survey
- Fire Fighting
- Saturation and Air Diving Support
- Mobile Rigs
- Heavy Lift/Construction
- Floating Hotels
- Well Stimulation and Floating Production
- Drilling Ships

There are over 300 of these vessels in the UK fleet today. Some of the operations mentioned above will mystify the reader. The functions of some of the seemingly more obvious will also cause surprise. For example "straightforward" platform supply vessels' transport casings and other hardware, containerised supplies, bulk shipments of water, fuel oil, brine, chemicals, liquid mud (for drilling) and cement.

The British offshore fleet faces a commercial crisis to which there is no commercial solution. The fleet is as competitive as any but our major competitors are better placed to survive.

Cut-backs in scheduled exploration programmes have reduced mobile rig activity by more than 40 per cent. There has been a similar reduction in the number of OSVs in work and the impact on the OSV sector is graphically illustrated in the table below.

Significantly, almost one-third of the vessels working in the UK Sector are on the spot market (i.e. trading more or less on a day-to-day basis) and average vessel utilisation has been around 50 per cent throughout 1986. Effectively therefore

about half the vessels stationed in the UK sector have been without regular employment.

But this situation has been developing while the UK sector remained wide open to foreign operators. Apart from formal protectionism in a number of the EEC and other countries there has been the long-standing unsatisfactory situation regarding the Norwegian Sector where rarely more than one "foreign" vessel is to be found at any one time. It was therefore a combination of these factors which led the Department of Energy's Offshore Supplies Office (OSO) to take steps last year to declare the British OSV Sector an area of "special interest". Following this the OSO have monitored tenders for foreign vessels, particularly Norwegian, for seeking work in the British Sector. This was a welcome demonstration of practical, and pragmatic, support which, but for the subsequent contraction in the UK Sector market, would have been of real benefit to British owners in terms of increased home sector opportunities. As it is, British owners have secured a larger proportion of a diminishing number of employment opportunities. But the pressure needs to be kept up if the full potential benefits of the UK offshore oil business are to be reaped by the nation.

The justification for action in support of the offshore fleet is surely compelling. First it could be, indeed should be, an investment in the future of the merchant shipping industry. OSV owners have built, converted and repaired extensively in British shipyards; seafarers offshore are of the highest quality reflecting the demanding and often dangerous nature of the job. If those capabilities are lost to the offshore sector (as well as to the deep sea trades) they might never be regained. The offshore sector also deserves protection on strategic grounds; the UK's

offshore oil and gas industry could not operate without the marine support provided by the offshore fleet and surely it is preferable that the majority of that vital support capability should be British. Finally there is defence, where the acknowledged shortage of mine counter-measures vessels can no longer be met by the fishing fleet. This could be met largely by OSVs, which would have many other defence roles.

Overseas governments have demonstrated a greater willingness to provide helpful financial packages than does our own. For example moratoria on shipbuilding loans are freely available in other countries yet the British offshore owner who has been such a good customer of British shipyards has to prove that he is on the verge of bankruptcy before he can even be considered for similar help.

Employment in overseas sectors is largely, sometimes exclusively, reserved to home fleets. The American Jones Act is one such example and even recently within the EEC several of our partners have demonstrated their determination to protect their sector while expecting, and enjoying, freedom to enter ours. In Norway also, while their shipowners express their opposition to protectionism in clear terms, national tendencies coupled with oil company attitudes keep the foreigner out of the way. Thus there is justification for the OSO to question Norwegian access to our Sector while theirs remains confined to their own ships.

Reduced activity because of the collapse of the oil price, combined with earlier encouragement to irresponsible levels of shipbuilding abroad have produced a major worldwide surplus of OSV tonnage which must somehow be put right before there can be some balance in employment conditions and a justification for investment in the next generation of OSVs.

Individual British offshore fleet companies have not created the problems and cannot be expected individually to provide the solutions. There is a role for Government to play, there is a price for Government (also) to pay and that is justified by the future which will benefit the nation if the British offshore fleet can survive.

	OSVs (UK and other flags) stationed in North Sea			OSVs (UK and other flags) stationed in UK sector		
	Total	Working	Laid-up	Total	Working	Laid-up
October 1985	302	283 (94%)	19 (6%)	173	167 (97%)	6 (3%)
October 1986	292	191 (65%)	101 (35%)	137	105 (77%)	32 (23%)



SUFFOLK MARINER'S *fire-fighting capabilities.*



OCEAN BENLOYAL which has drilled in the North Sea since the late 1970s.

ACKNOWLEDGEMENTS

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The front cover shows the Shell tanker ENTALINA in Sydney Harbour.

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5th March, 1987

The Rt. Hon. Nigel Lawson, MP.,
Chancellor of the Exchequer,
HM Treasury,
Parliament Street,
London, SW1P 3AG.

Shall I
acknowledge?

** Ask
See X - state in
a case to BOS.
I understand that he has
subjected us to a
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w/ pr. for the
have an issue
situation*

WITH THE COMPLIMENTS
OF THE
PRESIDENT

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913

CONFIDENTIAL



FROM: A W KUCZYS
DATE: 10 March 1987

*6/7 with
response
(or 13/3)
107*

MR REED - Inland Revenue

cc PS/Financial Secretary
Mr Scholar
Miss Sinclair
Mr Milner
PS/IR

SHIPPING: BES

Mr Runciman, the President of the GCBS, has sent the Chancellor a copy of the British Shipping Review 1987. I attach an extract.

2. The Chancellor has noted that the GCBS are still banging on about the BES. He understood that this had been satisfactorily resolved, and that was why there is nothing in the Budget. You told me, however, that the new Statement of Practice was still not ready, although you hoped to put it to the Financial Secretary this week. The Chancellor would be grateful for an urgent situation report.

AWK
A W KUCZYS

Shipowners' costs where there is scope for variation between countries, fall into two main areas — capital costs and labour costs.

Labour costs can be tackled by shipowners (though governments can be helpful or hinder as is explained in the next section). It is to reduce these costs that many ships are flagged out — not to evade safety standards or taxation.

The other major cost is the cost of finance. Before 1984 British shipowners enjoyed a favourable fiscal regime that allowed them to write off quickly the cost of a ship against their taxable profits. This was broadly comparable in effect to the wide range of aids and subsidies available to our competitors. It was also highly successful. In the 10 years from 1975 to 1984, whilst the fleet was declining by 30 million deadweight tons, 12 million deadweight tons of new ships were bought.

This regime was removed by the 1984 Finance Act as part of a general reform of corporate taxation and the impact on investment in the industry was devastating. Ships on order for UK registry plummeted from 363,000 deadweight tons in 1983 to only 5,000 deadweight tons in the first nine months of 1986. Unless action is taken there is unlikely to be significant investment in ships of any flag by the British shipping industry.

GCBS has suggested to the Government a number of measures that would help relieve our capital costs. They are:

(a) a 50 per cent ship allowance for investment in new or secondhand ships. This would go far to restore the pre-1984 position. It is an essential step if the larger, high cost units of the fleet are ever to be replaced;

(b) roll-over relief for balancing charges. The tax allowances on the sale value of a written down ship now have to be repaid to the Inland Revenue. GCBS would like to see these retained in the industry, *provided* they were reinvested in a new ship within a relatively short period. This would be in line with the practice of many of our competitors as well as the existing rules for Capital Gains Tax and would be of significant encouragement to reinvestment in shipping;

(c) some modifications to the rules of the Business Expansion Scheme to enable it to be more widely used by shipowners. For example, the rule that half the voyages of a ship must include a visit to a British port is a major impediment to worldwide — or even Europe-wide — trading. Given suitable changes the BES has

considerable potential to assist owners expand the UK fleet by purchasing good second-hand ships — and thereby not adding to the ship surplus.

None of the GCBS proposals involve cost unless the ventures concerned are successful. Then they merely defer tax, and unlike a subsidy are not a permanent drain on the Treasury. They reflect the assistance given elsewhere in the economy by way of Regional Development Grants or through the BES scheme.

Why should the Government act? Not because shipping companies or their shareholders want to depend on government help, but because the country needs a shipping industry. The defence needs are obvious and well known; not only in direct support of the armed forces but also to ensure civilian supplies in an emergency — an issue which is beginning to concern NATO. The need is not only for ships but for men. The balance of payments benefits have always been large and become more significant as the North Sea bonanza

glitters a little less brightly. At present they are shrinking and the nation's sea transport account shows a billion pound deficit. As a trading nation Britain surely cannot depend exclusively on others for shipping services. And employment, not only at sea and in shipping company offices but also in the ancillary industries, must be important.

The decision is the Government's — and ultimately the country's. A major national asset is wasting away. But it need not.



Tony

Both these two (heritage
and BES) are definitely not
for the speech - C ticked
the ~~refer~~ marginal comments on
the draft, albeit not ~~yesterday~~
these minutes. Will you pursue
them now?

Andrew

AMH

Thanks. Done. Both
are possibles for
FST's wind-up speech
T.

What is FST is copy list of?



DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
LONDON SW1P 3AG

March 11. 87

Dear Nigel.

BUDGET STATEMENT : SHIPPING

I understand that as matters stand you are not planning to announce next week any changes in the fiscal system which will be of specific advantage to the shipping industry. However, Revenue officials have told us that they are working on an improvement in the guidelines setting out the terms on which ship chartering can be regarded as an eligible activity under the Business Expansion Scheme. I am most grateful for this as I believe there is scope for new investment here and the two projects that have already been announced have aroused quite a bit of interest.

It would help to show that the Government is continuing to look for ways of alleviating the industry's problems within our overall fiscal strategy if you could, next Tuesday, either announce the change in the guidelines or at least indicate that an early and separate announcement can be expected.

Surely not in Budget Speech. Save for another day.

JOHN MOORE

CH/EXCHEQUER	
REC.	12 MAR 1987
ACTION	FST
COPIES TO	



Inland Revenue

Policy Division
Somerset House
FROM: J H REED
DATE: 13 MARCH 1987

1. MR MCGIVERN *Approved in draft*
2. FINANCIAL SECRETARY

BES: SHIP CHARTERING

You will recall that we undertook to produce a revised version of the Statement of Practice describing the circumstances in which a trade of ship chartering would be considered to satisfy the normal BES requirement that a trade must be carried on wholly or mainly in the UK. Recently, the Chancellor asked what was happening about this (Mr Kuczys's minute of 10 March). And on 11 March the Secretary of State for Transport wrote to the Chancellor suggesting that the Chancellor should either announce on Tuesday the change in the guidelines or at least indicate that an early and separate announcement can be expected.

2. The delay has largely been caused by work on the Budget and Finance Bill taking priority. And there were some difficulties in producing a satisfactory statement that would give the shippers, and the Department of Transport, what they wanted without creating or exposing weaknesses in either the BES or other areas of tax which draw on similar concepts. But we have now produced a draft for your approval which we think reconciles these needs.

"Wholly or mainly in the UK"

3. It is a statutory BES requirement that a qualifying trade must be carried on "wholly or mainly in the UK". It is not sufficient that the BES company should be resident in the UK

cc PPS
Mr Scholar
Miss Sinclair
Mr Milner
Mr Cropper
Mr Ross Goobey
Mr Tyrie

Mr Painter
Mr McGivern
Mr Cleave
Mr German
Mr Sadler
Mr Reed
Mr Carr
PS/IR

for tax purposes (although this is also a condition) as this could be the case yet virtually the whole of the company's activities could be carried on abroad. As Mr Peter Rees said in 1981 during the Finance Bill debates "The purpose of this relief is primarily and essentially to generate business activity inside the United Kingdom".

Existing Statement

4. The Statement of Practice (copy attached) deals with all trades, but paragraph 5 deals with ship chartering. This says

"In the particular case of ship chartering the qualifying trade would be considered to satisfy the test if all the charters are entered into the United Kingdom and over one half of the time ships spend on charter is on voyages between ports of call at least one of which is in the United Kingdom. If these conditions are not met the test may still be satisfied but this will depend upon all the relevant facts and circumstances."

5. This test was devised in order to permit the expected use of BES (short sea voyages around Northern Europe) while maintaining some UK element. The GCBS acquiesced in this although they would have preferred to let in all ship chartering provided that the ship was UK registered (as it has to be for the BES relief to apply). We explained to them that their version would be inconsistent with the BES legislation and anyway would let in ship chartering with only a very small UK connection.

6. Since the relief for ship chartering was introduced last year there have been, so far as we know, two BES offers for ship chartering companies. One, Edinburgh Tankers, failed to achieve its minimum subscription of £4.5 million but the offer has now been extended to the end of March, and since the offer was underwritten for the minimum subscription it will presumably go ahead. We do not know how the other offer, Bromley Shipping, has fared. We think it unlikely that any

doubts over the application of the "wholly or mainly in the UK" requirement will have had a significant effect on these offers.

7. However, this requirement may well have had an impact on the number and nature of the offers coming forward. The GCBS have told us that several of their members have looked at the possibility of raising BES finance but have decided against. The main reason given for this is that they could not be sure that the company would, over the three year qualifying period, meet the test that the ship should spend at least half its time on charter on voyages with at least one port of call in the UK. The reason for this doubt is that the ship chartering business is in general very responsive to changes in market conditions and ships go where the demand is. So if the company were tied to calling at UK ports it might have to take on less profitable business, or even lay up the ship.

8. You will see that the Statement says that the test may be satisfied even if the particular port of call test is not satisfied "but this will depend upon all the relevant facts and circumstances". However, little interest has been shown in this exception and the main purpose of a revised Statement of Practice would be to explain more fully what facts and circumstances are likely to be relevant.

A revised Statement

9. It is not an easy matter to devise a Statement which will make it clear whether or not a particular trade qualifies. The difficulty is that in deciding whether a trade takes place mainly in the UK there is a wide variety of factors which may be relevant but the weighting to be attached to each will depend upon the particular circumstances. Nevertheless, we have, with the help of our lawyers, devised the following paragraph which we think would be of some help to shippers:

"In the particular case of ship chartering the qualifying trade would be considered to satisfy this test if all the charters are entered into in the United Kingdom and the provision of the crews and the management of the ships while under charter take place mainly in the United Kingdom. If these conditions are not met the test may still be satisfied but this will depend upon all the relevant facts and circumstances."

10. The new feature, in comparison with the existing Statement, is the condition that the provision of the crews and the management of the ships should take place mainly in the UK. From our previous discussions with the GCBS we think they would be content with this - but we shall need to discuss with them the details and the drafting to ensure that there would be no particular difficulties in meeting the proposed condition.

11. The revised Statement should also satisfy the Secretary of State for Transport. In his letter of 22 December to the Chancellor he said

"My suggestion to you is that the Inland Revenue should reconsider their guidelines and adopt as the criterion of activity in the UK not the port calls that the vessel makes but the carrying on of the commercial management. The distinction between this and ship-board functions is already recognised in that part of the Act that deals with qualifying companies."

We do not at present propose going quite as far as this in the revised Statement - we are inclined not to draw a distinction between commercial management and ship-board functions. But we propose to raise this point with the GCBS and DTp.

12. The revised Statement would also ensure that a substantial part of all the company's activities took place in

the UK. This is consistent with the general aim of BES and should not give rise to pressure for concessions for other trades. If there is a risk it is that changing what we say in the Statment about the application of the requirement that a trade be carried out wholly or mainly in the UK, may lead tax planners to think about how this particular rule applies to other trades. For example, take a company (and such companies do exist) which provides all-in package holidays to UK residents at a hotel it rents abroad, and provides UK staff for the hotel. Depending upon the particular facts, it may well be that this would be eligible for BES relief despite the fact that there is relatively little activity in the UK (ie the taking of the bookings and the overall management of the operation).

13. But, as I have said, this is a feature of the existing law. If a company sought our prior approval for such a trade, we think they would find it difficult to argue their case by analogy with that of ship chartering - we would point out the various special features of the latter which make comparisons with land-based trades of little relevance.

14. I should explain why we propose dropping the port of call test. This was meant to provide a simple rule to enable shippers to be sure that they would qualify. Given what has happened since (paragraph 7 above), it clearly has failed in this objective. We therefore think it would be better to drop the port of call test in favour of the proposed test, which sets out more fully how we think the requirement (that the trade be carried on wholly or mainly in the UK) applies to ship chartering. In the unlikely event that an existing share issue has relied upon the port of call test but fails to satisfy the revised Statement we would of course not seek to withdraw BES relief from it on this account, and we would make this clear in the covering press release.

Consultation

15. If you are content, we propose discussing the draft revised Statement with the GCBS and we would give DTp an opportunity to comment. We would report back to you.

Handling

16. It would be impracticable to do all this before the Budget. The Secretary of State for Transport has asked for a Budget day announcement. I understand that the Chancellor does not want to refer to this in his Speech and there does not seem to be much point in mentioning it in a Budget day press release. But you might take the opportunity of saying something in your speech on Wednesday evening. This could be something like

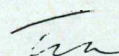
"Last year we extended the BES to ship chartering and there have been encouraging signs of interest in this. However, there are still some doubts about what a ship chartering company has to do to satisfy the BES requirement that its trade must be carried on wholly or mainly in the United Kingdom. We are considering how the existing Statement of Practice can be revised to resolve these doubts and the Inland Revenue are consulting the General Council of British Shipping about this. We hope to reach agreement soon and publish a revised Statement of Practice".

17. However you decide to handle this, you may wish to write on Monday to the Secretary of State letting him know of your intentions. We shall provide a draft letter once you have decided what you want to do.

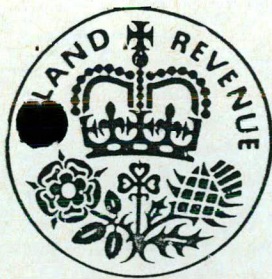
18. We think it would also be prudent to let the GCBS know what is happening so we suggest that we should let them know on Monday or Tuesday.

Conclusion

19. If you are content we shall consult the GCBS and DTp about our draft revised Statement and report back to you. Once you have decided about the handling we shall also provide a letter for you to send on Monday to the Secretary of State for Transport. And we also propose to let the GCBS know what is happening before the Budget or, if you would prefer, on Tuesday afternoon after the Chancellor has sat down.



J H REED



Statement of Practice

SP 7/ 86

Date 12 September 1986

INLAND REVENUE, SOMERSET HOUSE, LONDON

FURTHER COPIES OF THIS STATEMENT MAY BE OBTAINED BY WRITING TO (PLEASE ENCLOSE A STAMPED ADDRESSED ENVELOPE) OR BY CALLING PERSONALLY AT THE PUBLIC ENQUIRY ROOM, WEST WING SOMERSET HOUSE, STRAND, LONDON WC2R 1LB

BUSINESS EXPANSION SCHEME : OVERSEAS ACTIVITIES

1. Under paragraph 5(2) of Schedule 5 to the Finance Act 1983, investors may qualify for income tax relief under the Business Expansion Scheme when they subscribe for new equity capital in an unquoted company which carries on a qualifying trade "wholly or mainly in the United Kingdom".

2. The interpretation of this phrase in any individual case will turn on its precise facts and circumstances. However in general, in looking to see whether this test is satisfied, the totality of the activities of the trade will be taken into account. Regard will be had, for example, to the locations at which the capital assets of the trade are held and where any purchasing, processing, manufacturing and selling is done, and the places at which employees customarily carry out their duties. No one of these factors is in itself likely to be decisive in any particular case. A company may carry on some of these activities outside the United Kingdom and yet satisfy the requirement provided that the major part, that is to say over one-half, of the aggregate of these activities takes place within the country.

3. Accordingly, investment in a company would not be excluded from relief solely because some, or indeed all, of the goods or services it manufactured or processed were exported, or because its raw materials were purchased from abroad. Nor would the warehousing of the raw materials, the storage of products pending sale, or the availability of marketing facilities outside the United Kingdom be sufficient by themselves to deny relief.

/4. In respect

4. In respect of shares issued after 18 March 1986 a company is allowed to have one or more subsidiaries trading wholly or mainly overseas provided that the qualifying trade or trades carried on by the company and its subsidiaries, taken as a whole, are carried out wholly or mainly in the United Kingdom. The principles described in this Statement of Practice will be followed in applying this test.

5. In the particular case of ship chartering the qualifying trade would be considered to satisfy the test if all the charters are entered into in the United Kingdom and over one half of the time ships spend on charter is on voyages between ports of call at least one of which is in the United Kingdom. If these conditions are not met the test may still be satisfied but this will depend upon all the relevant facts and circumstances.



FROM: N WILLIAMS
DATE: 18 March 1987

PPWP
- Press notice already given

MR REED IR

cc Principal Private Secretary
PS/Chief Secretary
Mr Scholar
Miss Sinclair
Mr Milner
Mr Cropper
Mr Ross Goobey
Mr Tyrie
PS/IR

BES: SHIP CHARTERING

1. Following the Financial Secretary's letter of 16 March to the Secretary of State for Transport, Mr Moore wrote on 17 March ... (copy attached) to ask if the Financial Secretary could agree that a press notice could be issued about the reference to the BES guidelines that the Financial Secretary intended to make in his winding-up speech in the Budget Debate this evening.
2. Your advice was that it would be preferable to wait until a final version of the revised Statement of Practice had been agreed with the GCBS and at that stage (probably around the beginning of next month) a Press Release could be issued giving the details of this and also referring in greater detail to the three BES offers for ship chartering companies.
3. I put these points to Mr Moore's office but his view was that he wanted very much to issue a Press Release at this stage with a further one later. Given that this was so, the Financial Secretary was content for a Press Release to be issued by DoT.
- ... 4. I attach a copy of the proposed DoT Press Release which you saw in draft and with which you were content.

NIGEL WILLIAMS
(Assistant Private Secretary)



DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Our Ref : JM/PSO/3135/87

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

17 March 1987

Dear Norman,

Thank you for your letter of 16 March about the change to BES guidelines with regard to ship chartering. This is most helpful, and I am glad you are to mention it in your winding-up speech on Wednesday.

I think that some publicity for this as soon as possible would be well worthwhile. The GCBS themselves will not be slow to criticise us on the question of capital allowances and we should not lose the opportunity to show that we are prepared to meet the industry's points on BES. I should like therefore to issue a press notice about the reference you are to make in your winding-up speech. I do hope you can agree to this. If you can, I suggest that your officials and mine agree on its text straight away.

JOHN MOORE

JOHN MOORE WELCOMES PROPOSED BES GUIDELINES FOR SHIP CHARTERING

John Moore, Secretary of State for Transport, welcomed the Statement today by Norman Lamont, Financial Secretary to the Treasury, announcing a proposed improvement to the Inland Revenue's guidelines on ship chartering under the Business Expansion Scheme (BES).

John Moore said:

"There have recently been three BES shipping schemes and an amendment on these lines should encourage others to come forward."

The change has been proposed following representations from the General Council of British Shipping about the difficulty of complying with part of the current guidelines which require half the voyages of BES-covered ships to start or end in UK ports.

Consultations with the shipping industry have begun on draft new guidelines. These would require all charters to be entered into in the United Kingdom and the provision of crews and the management of the ships, while under charter, to take place mainly in the United Kingdom.

Such an amendment if agreed, would not affect BES relief for a company which had made a share issue on the basis of the existing Statement of Practice.