

PREM 19/2100

CONFIDENTIAL FILING

POLICY ON SMALL FIRMS  
ENTERPRISE PROPOSALS.

ECONOMIC  
POLICY.

PART 1: JUNE 1979

PART 6: MAY 1985

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
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PREM 19/2100





## Published Papers

The following published paper(s) enclosed on this file have been removed and destroyed. Copies may be found elsewhere in The National Archives.

House of Commons Hansard, 21 June 1985, columns 541-608  
"Small Firms"

Signed Wayland Date 3 September 2015

**PREM Records Team**





JA

cc: ①/Emf

10 DOWNING STREET

THE PRIME MINISTER

2 January 1987

Dear Sir

Thank you for your letter of 22 December. I am glad you thought the meeting on 17 December was a useful one, and it was helpful to have your summary of the ground we covered.

Yours  
Royal

John Browne, Esq., M.P.

185



From: JOHN BROWNE, MSc, MBA, MP

C/F ccma  
Lcc/Damp

HOUSE OF COMMONS  
LONDON SW1A 0AA

Rt Hon Margaret Thatcher MP  
10 Downing Street  
London SW1

22nd December 1986

Dear Prime Minister,

R24

Thank you again for giving up your time to see our Smaller Businesses Committee on 17th December. It was very good of you and we all much appreciated it.

May I take this opportunity of re-emphasising some of the main points we were trying to make.

- Business Expansion Scheme

Please may the 'lock in period' be reduced from 5 to 3 years. My own experience of venture capital, particularly in the United States, is that a long 'lock in period' is a great disincentive to investment.

- Capital Gains Tax

We accept the reticence of the Inland Revenue to allow income tax to be deductible for entrepreneurs and their immediate family under the Business Expansion Scheme. However, we feel that such deductability would be fairer and would seem as a real incentive for people to start their own companies if shares in unlisted companies were to exempt from Capital Gains Tax. In order to minimise possible tax avoidance this exemption should only apply to new shares held for at least 3 years.

- Tax Exemption for Retained Earnings

May I remind you that I am a hawk on government spending. However, I do believe that as an added incentive for people to start and invest in newly incorporated businesses, the exemption from corporate tax of the first 15,000 of retained earnings in a 'start up' company should be looked at seriously. It would provide entrepreneurs with incentive to build up equity as opposed to debt in small companies.





- Enterprise Bond

As you know, small companies' profitability and indeed cash flow is often volatile. In years when profits are made the entrepreneur is tempted to invest, often unnecessarily, in assets in order to shield profits from taxation. When profits are low, entrepreneurs resort to bank borrowing which reduces the financial viability of their companies. If companies in profit were allowed to invest in Enterprise Bonds, the government would get an immediate cash inflow of the total amount rather than merely of the tax due. If and when the bonds were redeemed by the company, the government would have had the use of the money in the interim. This would probably improve rather than reduce government cash flow. Small businesses would also be able to use Enterprise Bonds as security for government issued performance guarantees and also for leasing.

- Education

Bill Cash emphasised this point and I would like to second his proposal. I personally feel that education is one of the key elements in the recreation of our enterprise culture. Whilst keyboard skills (or typing) are included in a number of curricula, they are not taken seriously enough in the majority of cases. The keyboard is the link between man and the modern machine. Furthermore, basic accounting knowledge in Britain is lamentably low compared to that of our main competitors. The help that is given to small companies is of limited use when compared to an entrepreneur who has a basic knowledge of accounting and a feel for 'real' as opposed to 'apparent' profits etc. As you quite correctly said, an entrepreneur must know his market, but he must also know the true profitability of his products in that market, (i.e. they may sell, but do they sell at a profit?) This requires a basic knowledge of accountancy. Also, a knowledge of basic accounting means that the accountancy overheads are greatly reduced in a new business.

- Deregulation

We did not have time to deal with this problem. We would like to thank you for what has been done but to urge you strongly to continue this action as we see it as one of the largest problems facing business as a whole in our country.





- Differential Rates of Interest and Taxation etc.

I know we discussed this matter and some of the officers of my committee were in favour. I personally would like to register my strong opposition to two tier interest rates etc. I believe they mitigate against reality and they also create arbitrage, resentment and opportunities for abuse. I personally would strongly oppose two tier interest rates etc.

Finally, may I thank you again for seeing us and for your comments. May I also take this opportunity of wishing you and Denis a very happy Christmas and New Year.

Yours ever

JBm

JOHN BROWNE

ECON 101 - Small Firms. PE 6

SUBJECT  
CC MASTER



10 DOWNING STREET

LONDON SW1A 2AA

18th December, 1986

You might find it helpful if I put down briefly on paper the main points which were raised at yesterday evening's meeting between the Prime Minister and members of the Conservative Parliamentary Smaller Businesses Committee.

JOHN BROWNE raised a number of separate points. First, he pressed for the extension to the general run of small entrepreneurs of the capital and income tax relief available to small businesses under the Business Expansion Scheme. Your own response, and that of the Prime Minister, was that this was a budgetary matter and should be considered in that context; problems of avoidance would be paramount in considering this idea. Secondly, he proposed that there should be £15,000 exemption from Corporation Tax liability where this sum represented retained profits in the early or start-up phase of a small business. You will recall that you suggested this idea was open to abuse since a small businessman could engage in a series of business start-ups, followed by closures, which would permanently exempt him from CT liability. JOHN TOWNEND remarked that a closure would automatically involve a profits distribution.

Finally, John Browne raised the idea of the launching of an Enterprise Bond by means of which small businesses could invest 100% of their profits in a given year in an interest-earning bond, and at that stage avoid any payment of tax on the profit invested. The benefit of this proposal lay in the fact that the businessman concerned would not feel that he needed to invest his profits in unnecessary plant or equipment simply to avoid paying tax on the profits which would otherwise be retained. You will recall that you undertook to discuss this idea with John Browne on some suitable future occasion.

.../...



WILLIAM CASH fixed on the severe problems caused to many small businesses by the high level of interest rates. He proposed that banks should be persuaded to set aside a proportion of their profits, to make a pool from which small businesses could borrow at a rate differential lower than the normal run of customers. He cited a Greek government experiment in this area, which was allegedly useful and effective. In response to this idea, you yourself cited the exploitation danger, that large businesses would set up small subsidiaries specifically to exploit the differential rate. The Prime Minister thought that the lack of competition in the banking world was at the root of the difficulties experienced by small businesses and that the latter was the main problem to be tackled.

HENRY BELLINGHAM majored on the Business Expansion Scheme about which he was enthusiastic. He sought three modifications: first, that the five year "lock-in" rule should be reduced to three years, or tapering provisions introduced to secure the same effect. Secondly, he sought a relaxation of the Scheme's rules, to allow fathers and/or sons to participate contractually in the Scheme where one or the other was developing a small business. Thirdly, he sought a modification to secure that the tax relief available to BES investors should be available from the moment that their money was put into the company, and not (as at present) only when the company started trading.

PETER THURNHAM pressed for the introduction of Preference Shares, as part of the BES eligible capital structure. You will recall that you rebutted this approach on the grounds that BES capital is, by definition, equity risk capital, with the risk offset by the tax relief available.

JOHN TOWNEND thought that the main limitation on small business expansion still remained the bureaucracy and paperwork which cluttered up enterprise. VAT was the worst offender in this area, and he pressed for an increase in the exemption level of €74,000 which currently applies to small businesses. He maintained that this figure was quite inadequate when related to the turnover for businesses which were selling goods rather than services. You will recall that you yourself doubted whether an increase along the lines advocated by John Townend would be admissible under European Community rules.

Page Three

I think that the foregoing is a reasonably comprehensive record of the points raised by members of the Committee, but I am not proposing to copy it to our colleagues, unless you wish me to do so. This record is for your own use, if you wish to follow it up in any way. It will, of course, be kept on file here as well.

*Your ever  
Michael*

MICHAEL ALISON  
Parliamentary Private Secretary

The Rt Hon Lord Young





*plm*

Treasury Chambers, Parliament Street, SW1P 3AG

Stephen Ratcliffe Esq  
Private Secretary to  
The Rt Hon Lord Young of Graffham PC  
Secretary of State  
Department of Employment  
Caxton House  
Tothill Street  
LONDON SW1H 9 NF

23 October 1986

*Dear Stephen,*

**VAT: SMALL BUSINESS REVIEW**

Customs and Excise are tomorrow releasing the VAT consultation document which your Secretary of State and Mr Brooke discussed last week.

I enclose a copy of the final version, together with the statement that my Minister will be making at a press conference tomorrow morning. Mr Brooke will also be interviewed on the Today Programme tomorrow.

*I am copying this, with enclosures, to Mark Addison and Stephen Palmer.*

*Yours ever,  
Mike Norgrove*

M W NORGROVE  
Private Secretary



EMBARGOED: NOT FOR PUBLICATION, BROADCAST OR USE ON CLUB TAPES  
BEFORE 0001 HRS 24 OCTOBER 1986

NO. 1144

24 OCTOBER 1986

#### VAT: SMALL BUSINESS REVIEW

The Minister of State Treasury, the Hon Peter Brooke, MP, today announced the publication by HM Customs and Excise of a consultation paper "VAT: Small Business Review", which contains a package of Value Added Tax proposals designed to help small businesses.

"This consultative document is the first fruit of our review of the VAT system for small businesses. The proposals are intended to reduce the burden of accounting and record-keeping that the VAT system currently imposes on them. The Government is concerned to do all it can to encourage the small business sector," said Mr Brooke.

"In broad terms, the proposals contained in this document would reduce, or simplify, the burden of the VAT system for small businesses. The document contains a number of practical proposals for changes to the system:

- to allow accounting for VAT in cash instead of on invoices;
- to allow annual returns for VAT, rather than the current requirement of quarterly returns;
- changes to registration and deregistration rules;
- improvements to the special, simplified schemes for retailers.

"HM Customs and Excise also propose to employ consultants to advise them to what extent accounting and record-keeping requirements can be eased for small businesses.

"I am convinced that each of these changes would represent a significant simplification of and reduction in the administrative burden on small businesses.

"I am confident the small business community will welcome these moves but I am sure it is sensible to seek their views on the details of the proposed changes before they are implemented.

"I am anxious to press on with these proposals as quickly as possible. Indeed I am aiming to complete the review before the original target of mid-1987. I am, therefore, setting a tight deadline for comments on this consultative document of the end of this year - 31 December - so that decisions can be taken in good time for the 1987 Finance Bill. I hope all small businesses and their representative bodies will let us have their comments as quickly as possible."

#### BACKGROUND NOTE

The review was announced in the HM Customs and Excise management plan at the beginning of this year and publicised in the White Paper "Building Business ... not Barriers", issued last May (Cmnd 9793).

To ensure that small businesses are fully involved in the consultation, HM Customs and Excise will send to 5,000 small traders a simple question and answer form so that responses will be not only from trade and professional bodies but also from traders themselves.

The proposals include a number of possible measures which, it is felt, will benefit the smaller business. These include:-

#### Optional cash accounting

This scheme would allow businesses with an annual turnover below £100,000 to account for VAT on the basis of cash received and paid out. Traders would not have to account for VAT until paid by their customers and would not be able to reclaim VAT until they pay their suppliers.



### Annual VAT returns with regular payments on account

To use this scheme, which is designed to assist small businesses with their VAT payments, traders would be sent an annual assessment of their expected tax liability, for the current year, based on their previous year's VAT payments. This figure would then be divided by ten. Traders would make nine monthly payments by direct debit, starting four months after the beginning of the year, followed by a tenth payment to balance the account accompanied by an annual return. Traders would be allowed two months to prepare the annual return and make this final payment.

### Special schemes for retailers

The workings and scope of the present nine schemes has been reviewed, with the aim of improving and simplifying their operation and making some schemes more widely available.

### VAT registration and deregistration

A number of changes are proposed to ease the rules, in particular so as to allow more time for notifications of liability to register for VAT. In order to release about 250,000 traders from the VAT system and to reduce demands on official resources, the suggestion is also put forward (although no decision has yet been made) that traders whose turnover is below the registration limit should have to deregister.

Additionally, HM Customs and Excise propose to engage the services of an independent consultant to assess and make recommendations about the present record-keeping requirements for VAT and their effect on small businesses.

HM Customs and Excise are now inviting views, representations and general comments on these proposals. To assist this process, a random selection of 5,000 small businesses will be sent a question and answer leaflet which they will be asked to complete and return to Customs.

No final decision on these proposals will be taken until comments have been received and considered. The original intention was for the review of VAT and small businesses to be completed by mid-1987, but the date will be brought forward if possible.



A copy of a consultative document, giving full details of the proposed measures is available on request.

Comments should be sent in writing to the review co-ordinator:

David Brampton  
HM Customs and Excise  
Room 322, Knollys House  
Byward Street  
London EC3R 5AY

to arrive no later than 31 December 1986.

ISSUED BY: THE PRESS AND INFORMATION OFFICE, HM CUSTOMS AND  
EXCISE, KING'S BEAM HOUSE, MARK LANE, LONDON EC3R 7HE  
Telephone 01-382 5468/5469/5470/5471



**Small  
Firms  
Service**

**ANNUAL REPORT 1985-86**



### The Small Firms Service

A service to business provided by the Department of Employment

The men and women who start and run small businesses are, as individuals, utterly different from one another - but they all have two or three things in common.

They're full of drive and ambition. With a shrewd eye for a market opportunity. And they've got the determination to do something about their ideas.

When they succeed, we all of us benefit. Their efforts produce profits within the community and lead to extra employment opportunities for others.

But together with the single-mindedness that can lead to success, there is always the danger that a small business can come up against unexpected problems, especially in its make-or-break early stages.

The modern business world is a complex place. People in small firms have a lot to find out about it - including the fact that things can be done an easy way as well as a hard way. It's also a fact that lack of knowledge can mean opportunities missed as well as problems encountered.

At the Small Firms Service we have access to an enormous pool of information, nearly all of it based on practical experience. And all of this is available at any time to any small firm, just for the asking.

The other main support we can give to a small business is different - and every bit as important - and every bit as important. That is, our counselling service. A firm that uses this can get an opinion on its overall business activities or skilled advice on a specialist area, with every chance that the counsellor will be able to make suggestions that could lead to expansion, or diversification, or some other way to greater efficiency and higher profitability.

This annual report, the first we have published (although the Service has been operating since the early 1970s) sets out the achievements of the Small Firms Service in 1985/8, and illustrates how much assistance is available to the business community... forming yet another link in our national *Action for Jobs* campaign.

# Small Firms Service

## ANNUAL REPORT 1985-86

Introduction by the  
Small Firms Minister,  
David Trippier

There can be no doubt that small firms can make a substantial contribution to our economic well-being and offer both wealth- and job creation potential.

Since 1979 the stock of small businesses has grown substantially and is making an increasing contribution to the economy.

Throughout this time the Small Firms Service has been making its contribution to the success of the sector by providing a professional service which can give practical help, not only to a small business start-up on a sound and informed basis, but increasingly to established businesses ripe for expansion.

This report highlights a number of aspects of the Small Firms Service operations, not least the computerised information base which enables the enquiry staff to deal with a very wide range of enquiries and which can form the 'one stop shop' for the small business that requires information or in-depth advice.

I find it particularly welcome that so many businessmen with such an impressive range of skills and experience are willing as counsellors to make these attributes

available to small businesses. With the development of other support organisations for small businesses I see an increasing role for these skills to be used by established businesses ripe for expansion or moving into new fields such as exporting. It is in such areas that significant wealth- and job-creation lies.

That development of other small business support organisations is good to see. The Small Firms Service has available well over 10 years of experience in assisting small businesses, and I am pleased to see that the Service is making available much of this experience to these new organisations as well as offering practical support such as counselling. I know the Small Firms Service is always ready to help, and I recommend that others working in the small firms scene co-operate with the Service so that the small business has the best possible service.

I commend this report on the work of the Small Firms Service to all those who share my enthusiasm for a thriving small business sector, and I wish the Service continued growth and success in its work.



  
ACTION  
FOR JOBS



The year in perspective

Transfer to Department of Employment

A major event of the year was the transfer in September of the SFS, along with other small firms activities, from the Department of Trade and Industry to the Department of Employment.

The prime aim of the Department is to encourage the development of an enterprise economy. The way to reduce unemployment is through more businesses, more self-employment and greater wealth creation, all leading to more jobs.

The transfer of responsibilities was an integral part of developing the Department's role in this respect. And within that role the Small Firms Service is a practical expression of the support that Government can provide to small businesses and to those considering setting up small businesses.

The primary thrust of the Small Firms Service remains, however, what it has always been - **the encouragement of viable and profitable small businesses;** additional employment will often be a consequence, but for a business to survive and grow it has to be first and foremost profitable.

Meeting the demand

Although 1985-86 was generally a year of consolidation, the Small Firms Service saw a continuing and satisfying increase in the number of enquiries answered and clients counselled.

With this level of activity the Service continues to make a significant contribution to helping new businesses start up and, increasingly, to the development planning for established businesses, some with over 100 employees.

The Small Firms Service aims to provide easy access to its services to all. The Freephone Enterprise Service - costing over £300,000 in 1985/8 - makes initial contact straightforward and cost free to the enquirer.

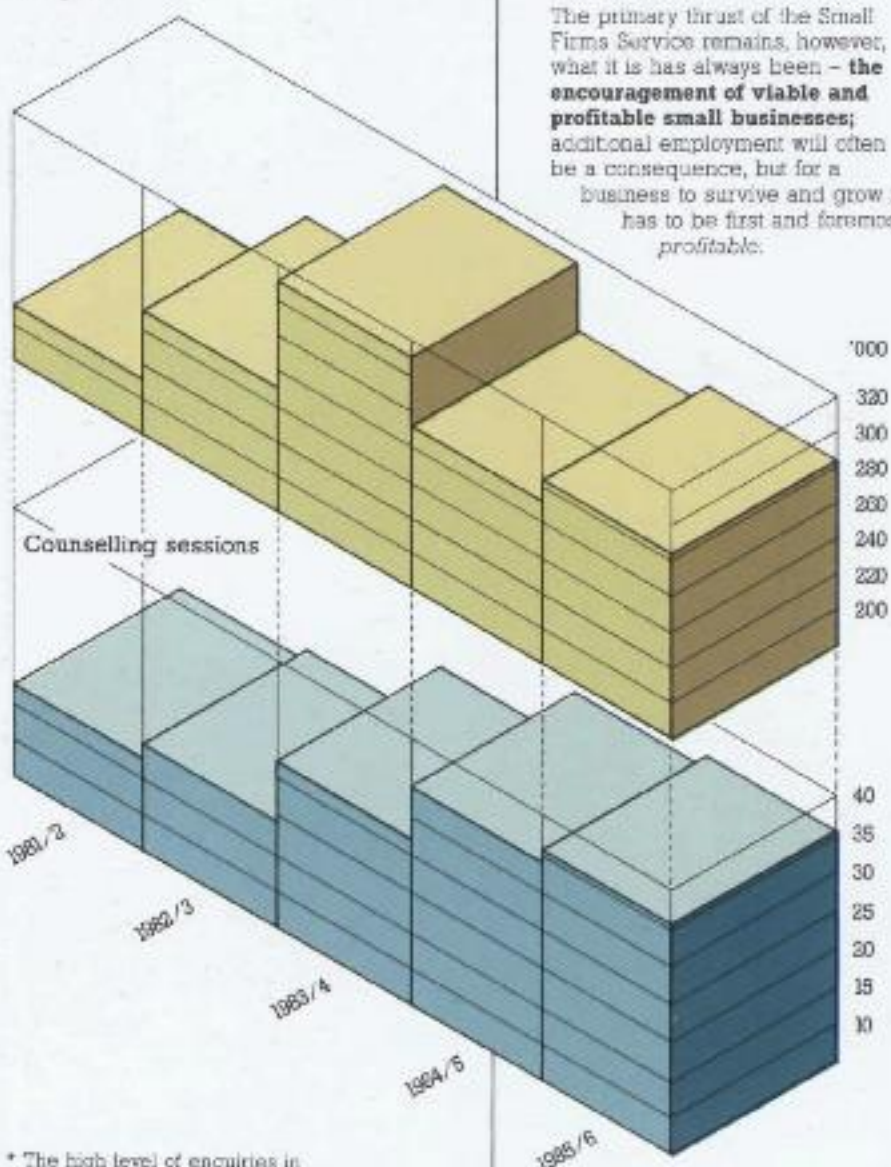
The Counselling Service is available not just at the regional Small Firms Centres, but locally through over 150 area counselling offices. These offices have traditionally included Jobcentres, Chambers of Commerce and local authority premises. A welcome development has been the growth in the number of Local Enterprise Agencies providing counselling accommodation for the SFS. It is hoped that more LEAs will be able to co-operate in this practical way in 1986/7.

Public awareness

The Small Firms Service has received a number of distinguished visitors during the year. The Service was particularly honoured on 11 July 1985 when His Royal Highness the Duke of Edinburgh visited the Manchester



Enquiries



\* The high level of enquiries in 1983/4 can be attributed to a short but intensive publicity campaign.

Small Firms Centre, meeting staff, counsellors and clients.

The SFS has featured in numerous local, regional and national press, TV and radio items. Of particular note was the joint funding with Radio 210 of a programme series for small businesses in which the Reading Small Firms Centre made a major contribution. Advice was also given during the



**We are never far away from your business interests.**

See us on Stand No. Look in at our Stand. Bring your plans and problems and if need be we'll arrange for you to meet a Small Firm helper in confidence - an expert business adviser, ring the bell below.

**Small Firm A big help to a small business. Dial 100. A FREE!**

Whether you're a small business or an owner of a business, the Small Firm Service can help. We can offer you: confidential advice and information. You can see us in person at: **Stand No. 100, A FREE!** at the Small Firms Service Stand at the Business Show, 11th-13th May 1985, 10.00am - 4.00pm. No questions in this category. [www.sfs.gov.uk](http://www.sfs.gov.uk)

**Business development for the smaller firm**

Our Business Development Service exists to help established small businesses. Its counsellors are experienced advisers who will work with you to solve the problems. Their expertise is available - impartially, confidentially and tailored to the needs of the individual firm. The first three counselling sessions are free. To find out more, ring Freephone Enterprise Service.

**Small Firms Service**  
A big help to a small business.  
Dial 100. Ask for FREEPHONE ENTERPRISE SERVICE.

year to a number of radio and TV broadcast producers on small firms matters when preparing programmes on small businesses. And... SFS literature made a fleeting appearance in BBC1's EastEnders!

The Service was pleased to offer free counselling as prizes in worthwhile small business competitions round the country, and to provide experienced counsellors to assist in the assessment and judging of the competitors. On a number of occasions the prizes were presented by Mr Trippier, the Minister for Small Firms.

Personnel

During the year the Small Firms Centre in Liverpool was upgraded from a sub-office of the Manchester Centre to a full regional Centre in its own right to serve the Merseyside Region. It is now better equipped to make a contribution to local economic development in Merseyside.

With over 100 staff and nearly 300 counsellors, there has inevitably been a high turnover of staff and counsellors during the year. This has put a special strain on training, and towards the end of the year reviews began on the training arrangements which should lead to improvements in

1986/7. Talks are taking place with Business in the Community on the potential for co-operation on courses for LEA personnel and SFS counsellors.

The Service learned with deep regret of the death on 25 March of Mr Dennis Parish, the Service's regional manager in the Northern Region based on the Newcastle upon Tyne Small Firms Centre. We join with his colleagues there in expressing our condolences.



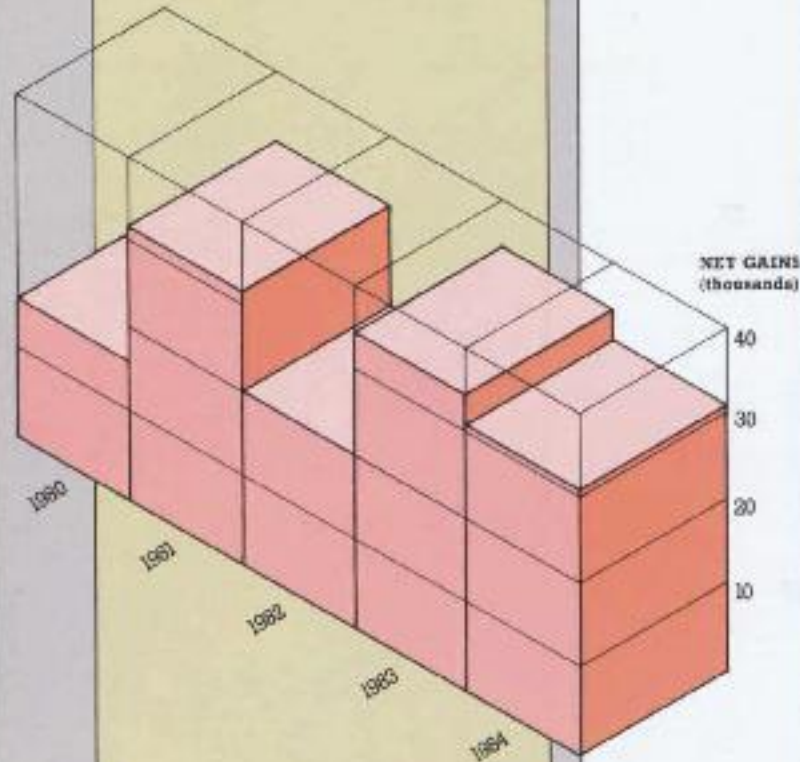
## The Small Firms Sector

### Who the SFS is helping

96% of all firms in the UK are independent and owner-managed. They contribute 20% of the UK's GNP.

Small firms have the potential to offer new employment, and while large firms were shedding jobs small firms were accounting for half of the new private sector employment and now employ 25% of the labour force.

### Small Firms - Starts over Stops

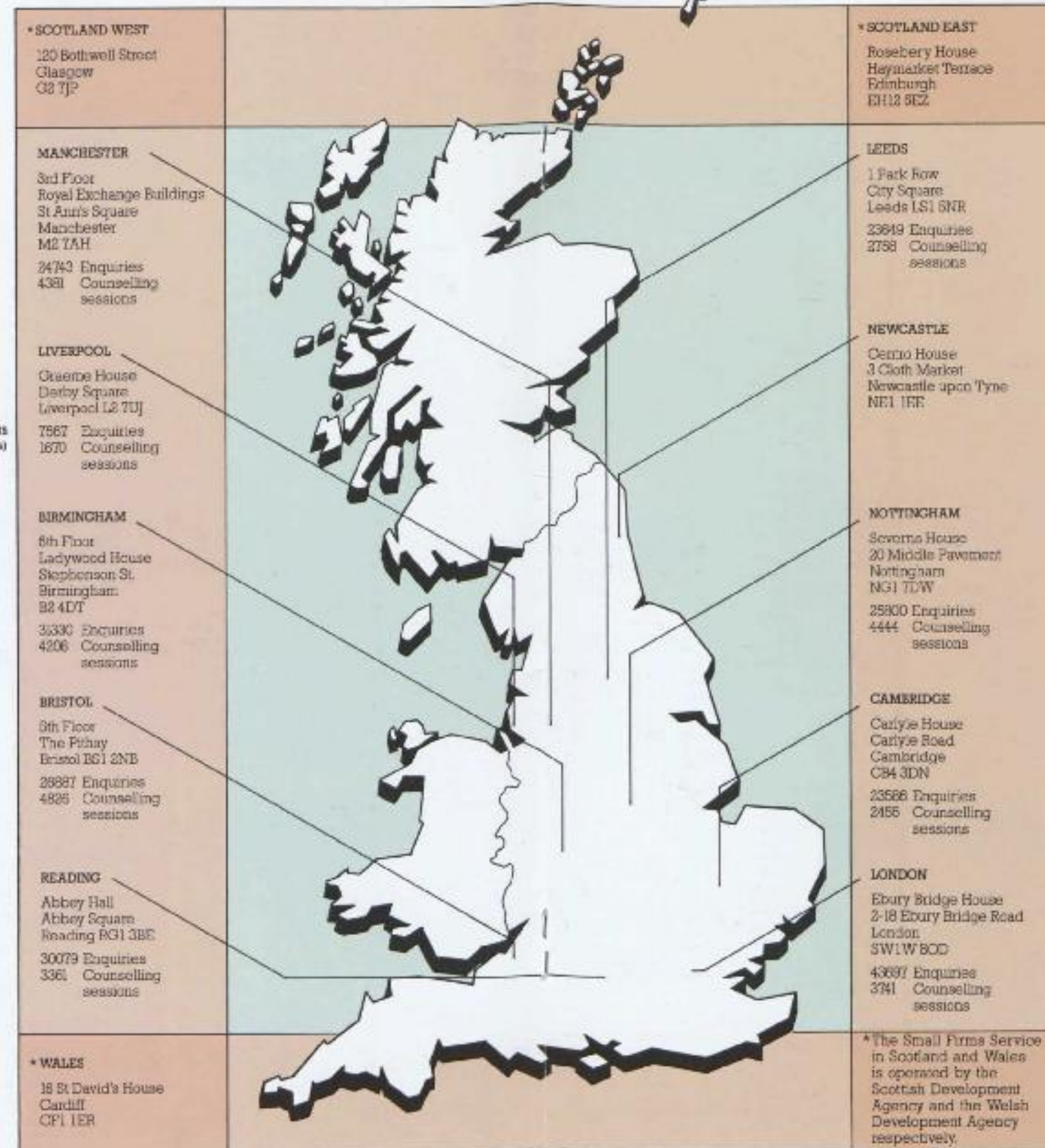


### Small firms offer economic diversity

Small firms are a force for innovation, and lacking the constraints of large organisations can show skill and imagination in developing new ideas which do not appeal to the large firm.

In order to be successful, small firms need to have a good base of business management; the development of vocational training, and the availability of good advice is important to their long-term success. The Small Firms Service plays an important role in ensuring that small businesses have the right kind of professional help to overcome gaps in their management knowledge.

## Small Firms Service organisation



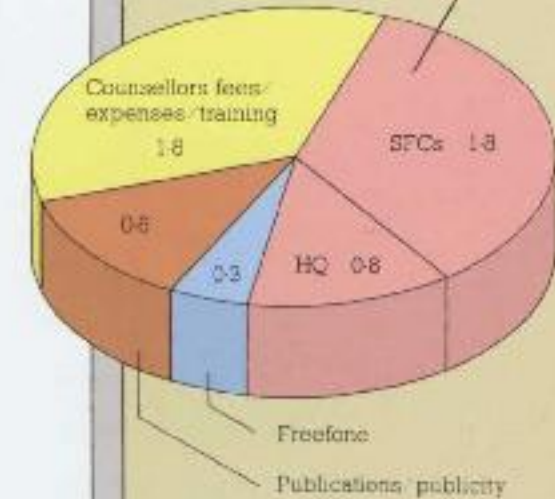
FREEPHONE ENTERPRISE connects you to your nearest centre.

## SFS Statistics

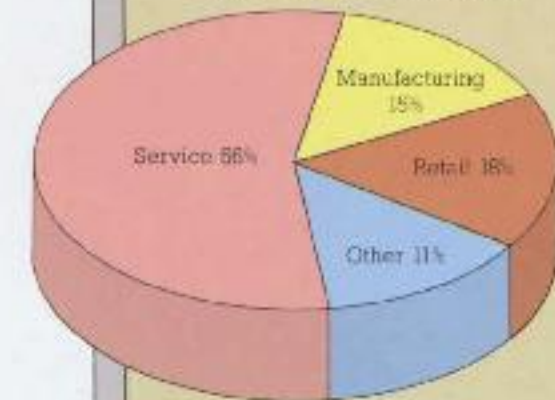
### SFS budget allocation £m

This covers both programme and general administrative expenditure, which fall to different Votes of the Department.

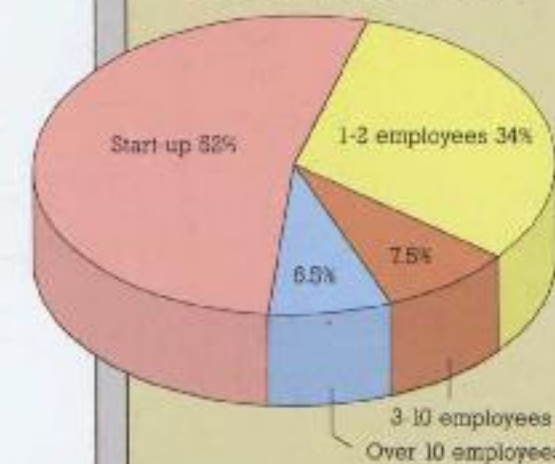
Admin. (inc. computerised enquiry service)



### Types of business counselled



### Size of business counselled





## The practical work of the Small Firms Service

The aims of the Small Firms Service are to provide small businesses, and those considering starting up in business, with:

- a comprehensive enquiry service, and
- practical counselling by experienced businessmen.

### The Enquiry Service

Each Small Firms Centre is staffed by enquiry officers selected for their ability to communicate fluently, particularly over the telephone.

They all undergo specialised training in analytical skills and are given extensive briefing on how business operates and on the jargon involved to help them identify enquirers' needs. This is supplemented by briefing on current issues such as government and local grants, legislation across all government activities, and any other matters that concern small businesses.

They are supported in their daily task by a computerised database of information relevant to small firms.

Apart from answering enquiries directly they are able to do some research to respond to enquirers effectively, and where appropriate refer the enquirer to other specialised sources of information or advice. Where their assessment of the enquiry

justifies it they are able to make bookings for counselling appointments.

The enquiry service is backed up by a range of SFS booklets, other published material useful for small businesses, and by printed information from the computer.

Typical examples of questions asked are:

- I wish to set up as a street trader. Do I require a licence and if so where can I obtain one?
- I wish to purchase a shop and change the use of it. Who should I inform?
- I intend to set up a manufacturing business but require premises. How do I go about it?
- I am looking for a supplier of a specialist piece of machinery. Can you help?
- Could you tell me what EAS is and how do I register for it?
- I want to start my own business. What do I have to do and who do I have to tell?
- The Inland Revenue is going to put me out of business although my order book is full and I can pay them when my present contract is completed. Can you help to save the business?
- I want to raise money to buy a new lorry. Can you help me find it?

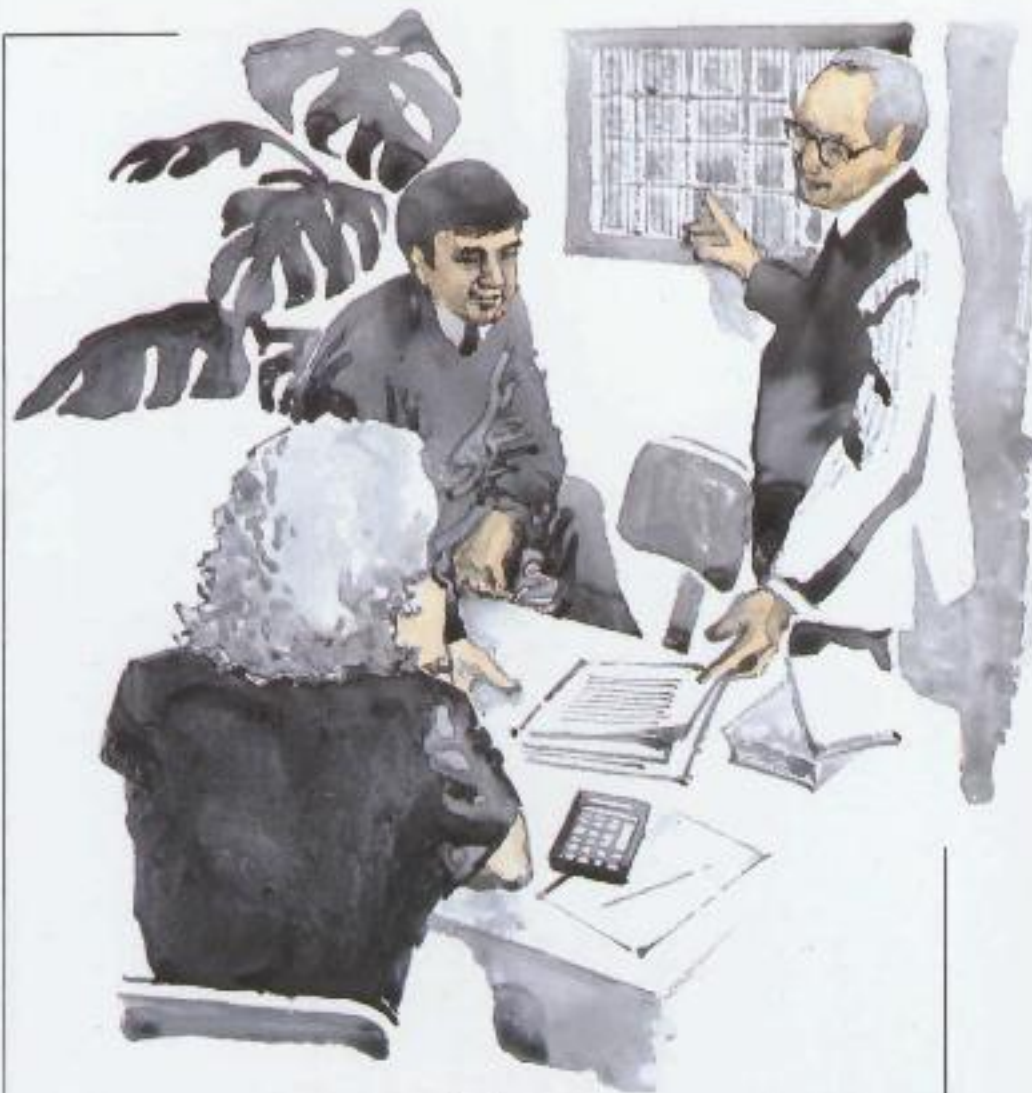
All commercial and financial information divulged during such communications is regarded as totally confidential.

### The Counselling Service

Counselling is provided by experienced business men and women on contract to the Department and selected for their ability to deal with the problems of smaller businesses: the SFS believes it has an unsurpassed access to a national team of business management skills. These skills can cover, for example, raising finance, new market opportunities, modernisation of a production line or stock organisation, and getting into exporting.

Some 80% of counselling effort goes into providing business advisory support to the very successful Enterprise Allowance Scheme run by the MSC. This consists of providing business expertise at information sessions and follow-up counselling to EAS participants who seek further advice.

Traditionally the Service has been seen as largely dealing with start-ups, but although this aspect of SFS work will remain, more publicity is now actively targeted at established businesses to make such firms better aware of the skills and competences that the SFS can offer.



A notable feature in 1985/86 was the shift of clients towards established businesses, those with 3-50 employees, or in some cases more. It is in this area that the Service believes its counselling skills could be used more to help create growth and jobs.

The number of counselling sessions held with small businesses in 1985/86 reached 36,116, a 3% increase on the previous year.

With nearly 300 counsellors, an impressive range of skills and experience is on offer. In addition, all are given refresher training on analytical skills, interpersonal skills, small business finance and the problems of marketing for small businesses.

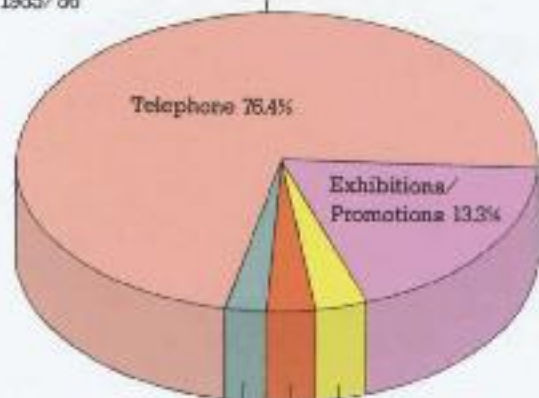
Details of the skills available in the regional counselling teams are available from the Small Firms Centres. The counselling service represents a unique blend of private sector skills, acquired

through senior management in large companies or their subsidiaries or through starting up and running small businesses directly.

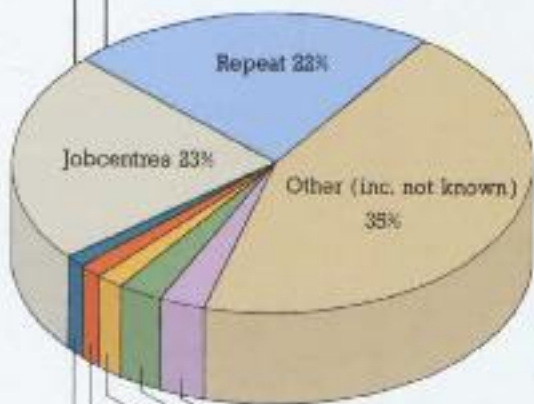
The Government, and many in the small firms sector, are indebted to the contribution made by SFS counsellors in 1985/86.

The following case histories illustrate something of the range of counselling work handled by the Small Firms Service.

How clients approached the SFS in 1985/86



How clients heard of the SFS in 1985/86



### Functional skills/specialisms

Accountancy	R&D	Law	Production
Costs	New product development	Building regulations	General
Audit	Product development	Company	Technical
Book-keeping	Product	Contract	Export
Buying and selling	Process	Employment	Quality control
Financial control	Marketing	Finance	Stock control
Financial statements	General	Insurance	Workshops
Insurance	Advertising	Leasing	Design
Investment	Market	Plant	Planning
Legal	Research	Selling	Administration
Leasing	Customer	UK	Industrial relations
Manufacturing	New product	Exporting	Recruitment
Materials	Launch and evaluation		Public speaking
Merchandising			Computerisation
Personnel			
Production			
Quality control			
Research and development			
Shipping			
Staffing			
Training			
Transport			
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1

### Management buy-out

Pressac Holdings PLC encouraged a management takeover of the W and A Metrology division of one of its subsidiary companies. Wagstaffe and Appleton, W and A Metrology design, manufacture and sell co-ordinate measuring machines.



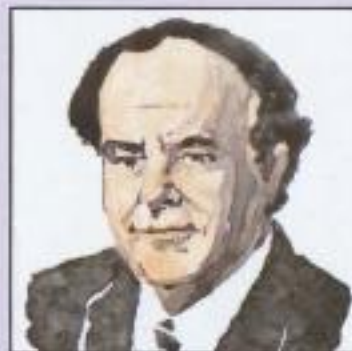
Mr G Carter, a Small Firms Service counsellor, became closely involved in helping establish satisfactory financing for the management buy-out. His past managerial experience in works contracting, surveying and finance, and his self-employed career as a management consultant since the 1970s, gave Mr Carter an excellent basis for counselling. After helping collate a management buy-out package, being involved in the presentation of the case and in negotiations with Pressac, the buy-out was successfully concluded.

One of the current directors involved in the buy-out is acting managing director, Tony Butler, who readily acknowledges the assistance gained from the Small Firms Service. He said 'The strength of the help we obtained was from having a mature businessman as a counsellor, who calmed us down when necessary and talked sense to us as well, helping with all kinds of things, including items such as cash-flow. The help was really tremendous.'

2

### Saved from liquidation

A specialist photographic filter manufacturer, employing 7, was saved from liquidation by advice from Small Firms Service counsellor Jim Warnock.



Mr Warnock was a specialist in several fields including finance, marketing and export, and by consideration of his experienced advice the company restructured its financial base and developed a marketing strategy which led to its survival. Mr Warnock was well qualified for his counselling post, having worked for many years in the chemical and engineering industries, culminating in the post of Managing Director. He now runs his own company specialising in executive search and management consultancy.

3

### Now successful exporter

A designer knitwear company operates from Poulton-le-Fyde, Lancashire, home of the Managing Director, Mr John Roskell. From this base, and with a staff of 300 outworkers, a present turnover of £137,000 is achieved. The products are exclusive, and have been highly successful on the Japanese market where most of the output is sold.

However, the company outlook has not always been so optimistic. In 1982 Mr Roskell, experiencing financial difficulties, approached the Small Firms Service. Regular counselling from Mr F Roby brought the business from a precipice to its current state.



His experience in accounting, co-operative finance, management

structure and control, gained from his career as a Group Financial Controller to a large Merseyside shipping company, assisted in the main areas of counselling, including the introduction of financial management controls, raising capital for overseas expansion (£30,000 arranged through Loan Guarantee Scheme) and aspects of production control, which were necessary for the vital about-turn in the company's history.

4

### Finance for North Sea Oil contract work

A Small Firms Service client employing 180 people accepted a contract for £1.25m for work on two North Sea oil platforms. However, their bank would not increase the finance available to



support the project. The client's accountants contacted the Small Firms Service to enquire if grants were available to support this scheme.

Counsellor Mr M Sherman helped the client organise progress/part payments for materials, and the client was then able to negotiate with the bank, successfully doubling the overdraft facilities available to £106,000 (unsecured). The contract was then completed profitably on time. A further contract on another oil platform has now been obtained, and this work has been financed in the same manner with no difficulty.

Mr Sherman competently advised in this situation, applying experience gained during his extensive career which covered a directorship of a public limited company mechanical engineering, overseas experience as a project engineer, the retail and clothing industry, managerial and financial skills, debt collection, and past experience in the advisory services (Citizens Advice Bureau).

5

### Sportswear Manufacturer

In the spring of 1984 Ryder Sportswear of Orpington, Kent, believed there was an unsatisfied demand for quality protective clothing for sailors and windsurfers - but bankers were unconvinced.

By the end of summer 1984, four Small Firms counselling sessions with counsellor Mr Chris Wilson had helped Ron Cooper, the dynamic young boss of the firm, to learn that good work would earn a good profit. The firm's major problem was finance. With advice on financial control and assistance in preparing cash flow projections, philanthropy towards the firm's debtors was ended.

A business plan was created - and Ryder are presently sailing high. Mr Wilson's specialist knowledge of production, development and licensing, financial control, marketing, management structure and control had paid off. In a small business with few employees the former £5,000 overdraft became a £20,000 (5 year) loan. Yearly expansion has led to a £65,000 turnover, with 8 full time employees and 8 more trainees and part-timers. And the future is looking even better, with double this turnover expected next year.

### Contact with other support agencies

Since its inception, the Small Firms Service has been a prime source of information and advice for small firms on a national basis. Clients would come to it, or the Service could go to the client where this seemed to provide the best solutions.

The Service is now, more noticeably, only one of a number of organisations which aim, like the Service, to support and help small businesses. The development of a working relationship with these other organisations has been a priority task in 1985, and is likely to continue.

The Service welcomes regular exchanges of views and the referral of small business clients between itself and organisations such as CoSIRA, Local Enterprise Agencies, Chambers of Commerce, Local Authorities, etc. It is vitally important for the small business clients that they are referred to the organisation which can best meet their needs

regardless of which is approached first.

Contact with the Local Enterprise Agency Movement in particular has expanded during the year. The resources of the Small Firms Service - notably the extensive computer database of information and the wide range of skills and expertise of the counselling service - can complement well the intimate local knowledge of the Local Enterprise Agencies.

The SFS now holds regular counselling services in 26 Local Enterprise Agency premises. A growing number of Local Enterprise Agencies are now recognising and using the counselling resources of the SFS as support for their own counselling activities.

Joint events take place with many of the organisations within the small firms field. This demonstration of partnership is regarded by the Small Firms Service as important in creating the awareness among small businesses of the opportunities, advice and support available.



The Small Firms Service supports its advisory service with a series of publications covering a wide range of business topics.





**Freefone  
Enterprise**





## Consultation document

### INTRODUCTION

#### General

1. The task of collecting the VAT revenue inevitably requires a clear framework of rules, both to ensure proper payment of the tax due and to give fairness of treatment as between taxpayers. The Government, however, seeks to minimise burdens on business, by improving these procedures, as an important aspect of their aim to encourage enterprise.

Customs and Excise recognise that, despite recent improvements in the VAT system, the rules on accounting for and payment of VAT can still cause problems, especially for small businesses. As was announced in the White Paper "Building Businesses ... Not Barriers" (Cmd. 9793, May 1986), we have been reviewing the VAT policy towards small businesses to see if special arrangements can be provided for them. The first stage of this review has now been completed and this paper sets out a number of proposals and possibilities for change in areas of importance to small businesses.

#### European Community considerations

2. Any proposal to change the rules governing VAT must be in accordance with European Community law. This is contained in the Sixth Council Directive on VAT and, except where otherwise indicated, the possibilities discussed in this paper are consistent with that Directive. In formulating our detailed suggestions, account has also been taken of the proposals recently submitted by the European Commission in a draft 22nd Directive, which would provide a special scheme for small and medium-sized businesses. If implemented, without amendment, the proposed 22nd Directive would provide that:

- Member States must offer a tax exemption scheme (registration threshold) for traders whose turnover does not exceed 10,000 European Currency Units (ECU) - currently equivalent to about £6,900;
- An option for Member States to have a higher registration threshold of 35,000 ECU - about £24,100;
- Member States must offer a simplified "accounting" scheme for charging and collecting tax for businesses with a turnover of less than 150,000 ECU - about £100,000. This scheme would



consist of two elements:

- cash accounting for both outputs and inputs;
- annual returns and monthly or quarterly payments;
- The option for Member States to introduce a flat rate percentage for calculating deductible input tax.

Paragraph 3 below explains how these proposals might apply in the United Kingdom. However we do not suggest the introduction of flat rate schemes because these are more suited to multi-rate systems of VAT and their computation would be likely to prove more burdensome both for individual taxpayers and to ourselves.

### The suggestions for change

3. In setting out the possibilities for change we have been concerned that, within the framework of European Community law, they should offer a substantial simplification and a reduction of burdens for the small business. We have therefore made suggestions in the following areas:

- "Cash Accounting", where VAT would be claimed and paid on a cash basis rather than on the basis of invoices.
- an annual return for VAT with regular payments on account.

Both the possible schemes for cash accounting and annual returns have regard to the draft 22nd Directive and its upper limit of about £100,000. At this level some 660,000 businesses, about 44% of all registered businesses, would have the option, but no obligation, to use these schemes.

- requirements for record-keeping and accounts.

The records a business maintains and preserves for VAT purposes are designed to be primarily for agreement between individual traders and their local VAT office. We propose, however, to employ an outside consultant to look at the impact of our practice on small businesses. He will examine how the concern to minimise burdens on business in the area of record-keeping can be reconciled with our revenue control requirements.

- the VAT registration and deregistration rules.

Our registration threshold is already the maximum permitted under existing European Law (Article 24 of the Sixth VAT Directive). However, the changes we are proposing on registration and deregistration requirements offer an easement of the present legal provisions.

When considering any changes we have to be concerned not only with the burdens which our requirements place on businesses but also with their impact on the proper protection of the revenue and the use of our resources. Without any decisions having been taken at this stage we have to consider whether businesses with turnovers below the registration threshold should be permitted to register, or remain registered, for VAT. At present some



250,000 businesses come within the scope of the tax solely because they choose to do so. These businesses have to be controlled, using valuable resources which we could use more effectively elsewhere, while collectively they produce no revenue. It is not clear whether any proposal to refuse registration to businesses below the obligatory registration threshold would be compatible with European Law. In considering such proposals we would need to discuss the position with our European partners.

- the special schemes for retailers.

Our suggestions here concern only those businesses which are using retail schemes. The changes we propose to the various retail schemes should, we believe, offer the option for simplification to some 300,000 small and medium-sized retailers, while removing anomalies which affect mainly larger businesses or others which are not retailers in the usual sense of the term. The system of retail schemes is not affected by the draft 22nd Directive.

A proposition which has been put forward by some small business representative bodies is the abolition of VAT on transactions between registered traders. This proposition was examined in 1978 by an independent working party, including various business interests, which decided by a clear majority that this proposal should not be recommended. We believe their conclusion is still correct. Our reasons for not recommending such a system are set out in the Annex to this paper.

#### Representations and comments

4. No firm decisions will be taken until comments in response to this consultation document have been received and considered. The Government's original target was for the review of VAT and small businesses to be completed by mid-1987 but, through the early publication of this consultation document, it would like this date to be brought forward if possible. Comments, including any on the draft 22nd Directive, or other suggestions relating to accounting and record-keeping requirements for small businesses, should be sent in writing to David Brampton, Customs and Excise, Room 322, Knollys House, Byward Street, London EC3R 5AY (telephone 01-382-5365) by 31 December 1986. Copies of the draft Directive can also be obtained from him.

#### Implementation

5. In the light of the comments received the Government will consider further whether legislation to implement the possibilities discussed in this consultative paper should be included in the 1987 Finance Bill, with a view to implementation as soon as practicable. In some cases, eg retail schemes, changes to primary legislation are unlikely to be required. In the case of annual returns with payments on account it should be noted that, because of the complexity of the changes required to the Customs and Excise computer system, implementation would not in any case be practicable before the end of 1988 at the earliest and possibly not until a later date.

## SUMMARY OF MATTERS DISCUSSED IN CHAPTERS 1-5

### Chapter 1: Cash accounting

A possible scheme, open to all businesses with turnovers below £100,000, whereby VAT would be accounted for on the basis of cash paid and received - paragraph 1.2.

### Chapter 2: Annual returns with payments on account

A possible scheme, open to all businesses with turnovers below £100,000, with 9 payments on account and a final payment with the annual return - paragraph 2.2.

### Chapter 3: Records and accounts

Customs and Excise to engage an independent consultant - paragraph 3.5.

### Chapter 4: Registration and deregistration requirements

#### Proposals:

- time to notify liability to register extended to 1 month - paragraphs 4.3 and 4.4
- eligibility to deregister to be based on future turnover only - paragraph 4.5
- turnover for deregistration to be tax exclusive - paragraph 4.6
- notification of cessation of trade increased to one month - paragraph 4.7
- deregistered businesses will not be liable to registration only because of turnover before deregistration - paragraph 4.9
- specific time limit of one month to notify material changes by businesses exempted from registration - paragraph 4.10.

### Chapter 5: Retail schemes

#### Proposals:

- introduce a replacement/alternative to Scheme B, removing the "50% rule" and introducing an annual stock adjustment - paragraph 5.7
- amend "Adaptation 1" to provide for varied but fixed mark-ups based on type of goods. Increase turnover limit to £500,000 - paragraph 5.8



- increase Scheme C turnover limit to £90,000 - paragraph 5.10
- revise Scheme C fixed mark-up levels - paragraph 5.11
- increase Scheme D turnover limit to £500,000 - paragraph 5.16
- amend "Adaptation 2" to operate on standard-rated goods only - paragraph 5.17
- review the level of the Scheme G 1/8th uplift - paragraph 5.18
- abolish the Scheme G minimum turnover limit - paragraph 5.19
- incorporate the working methods of the available Scheme J adaptations within the scheme "How to work" pamphlet - paragraph 5.20
- withdraw the "standard" method of reckoning gross takings - paragraph 5.24
- withdraw use of schemes from "non-retailers" - paragraph 5.26
- withdraw use of schemes in respect of non-retail supplies - paragraph 5.28
- clarify eligibility for use of mixtures of schemes - paragraph 5.30
- clarify the meaning of "separate parts" of a business - paragraph 5.31
- amend Regulation 3 of the retailers regulations to clarify the Commissioners' powers to refuse the use of retail schemes - paragraph 5.32.

## CHAPTER 1: CASH ACCOUNTING

### Introduction

1.1 The current VAT system is largely invoice based. The issue of a tax invoice obliges the supplier to account for output tax and enables customers to claim input tax. It may, however, be helpful to many small traders if they were to have the option to account for VAT on the basis of cash received and paid out. A significant number of traders operate in commercial circumstances which require them to provide lengthy credit facilities to customers. "Cash accounting" would improve the liquidity of many small traders who have to account for VAT due on invoices for which they have not received payment. It would also remove for them the problem of VAT on bad debts.

### General features of a cash accounting scheme

1.2 We are therefore considering a possible scheme for cash accounting whereby VAT would be accounted for on the basis of cash paid and received. The main features of such a scheme would be that:

- a) it would be an optional alternative to the normal method of VAT accounting, ie cash accounting would not be compulsory;
- b) it would cover both input and output tax;
- c) it would be available to small traders with turnovers up to the maximum outlined in the draft European Community 22nd Directive, in the region of £100,000 per year.

### Operational features

1.3 We envisage that the scheme would embody the following operational features:

#### a) **Joining the scheme**

i) Newly formed businesses would be allowed to adopt the scheme, on application, as part of routine VAT registration procedures. Existing registered traders would need to make a written application to their local VAT office. A pre-condition would be that businesses were up to date with returns and payments.

ii) When applying, businesses would need formally to confirm their agreement to comply with a number of conditions, including adequacy of records and accounts. Having opted to join the scheme a business would normally have to remain in it for two years before it could choose to leave.



### **Leaving the scheme**

i) To prevent steadily growing small businesses having to adopt normal VAT accounting at a premature stage of their development, we suggest that a tolerance of, say, 25 per cent could be applied to the turnover limit. This would also reduce excessive movement between the normal VAT scheme and cash accounting. Businesses with turnovers over the limit but within the tolerance would remain ineligible to adopt cash accounting.

ii) Those cash accounting scheme businesses whose turnovers exceeded certain periodic limits would be obliged to adopt normal accounting at the start of their next accounting year, unless they could show that turnover was unlikely to exceed the tolerance during the year as a whole.

### **c) Records and accounts**

i) Existing requirements concerning records and accounts would need to remain as explained in Section VIII of "The VAT guide" Customs and Excise Notice 700. Scheme users would have to keep satisfactory cash records either by adapting existing summary records of sales and purchases by including settlement details or by setting up a cash book which fulfilled the dual role of summarising both transactions and individual cash movements. No particular format for such records would be laid down but a clear audit trail would have to be maintained from the summary record back to the normal commercial evidence of the transactions (ie purchase and copy sales invoices, and evidence of receipts and payments). Businesses would still have to issue tax invoices for sales to registered customers.

ii) Cash purchases would need to be supported by receipted tax invoices before input tax credit could be claimed.

### **Views of trade associations and small businesses: Consultation and feedback**

1.4 Views are invited on the cash accounting scheme, and on the method of operation as broadly outlined above. Comments are also invited on any alternative features you would wish to see included, and on the following points which would seem to be potential areas of difficulty:

a) Special VAT accounting arrangements would be necessary for businesses moving between the cash accounting scheme and the normal invoice-based method, and also for those businesses deregistering. On adoption of the cash accounting scheme registered traders would have to separate receipts and payments for transactions previously accounted for under normal arrangements. Similarly, businesses moving from cash to normal accounting would have to account, on their first normal return, for sales for which they had not been paid; but they would be able to claim back the tax on purchases even if they had not been paid for. As far as deregistration is concerned, we suggest that the due date for sending in the return might be extended from one month to two months after the effective date of deregistration and all outstanding tax be accounted for whether or not cash has been received or paid.

b) Where payments or receipts cover more than one invoice or represent part payment of an invoice, special provisions would be needed. Where multi-rated supplies of goods or services are involved, a fair and reasonable pro rata formula could be worked out. Cash received or paid for on sales or purchases could be allocated on the basis of the proportion, by value, at each tax rate on either:

- the original order, or
- the related statement, or
- the demand for payment,

to which the particular cash movement relates.

### Legislation

1.5 Significant amendments to existing legislation (in the VAT Act 1983) would be required.



## CHAPTER 2: ANNUAL RETURNS WITH PAYMENTS ON ACCOUNT

### Introduction

2.1 For some time many small businesses have felt that, to help their cash flow, they should be allowed to make their VAT returns and to pay the tax due on a different basis to that currently in use. A suggestion in a previous consultative exercise that returns might be made annually with annual payments of tax was not generally favoured, primarily because of the problem of ensuring that money to pay the tax was available at the end of the year. Also, we believe that the present experimental scheme for allowing the monthly submission of returns with monthly payment of tax is not likely to be of general benefit to the majority of small businesses.

### General features

2.2 We are now considering a scheme whereby returns could be made annually with nine payments on account with a final (tenth) payment being made together with the annual return. The scheme would strike a reasonable balance between assisting small businesses in making their payments of VAT and the effect on revenue control and resources, and would be a further option available to small businesses, whether or not they used cash accounting. It would require some amendment to existing legislation.

### Operational features

2.3 We envisage that such a scheme would embody the following operational features:

#### a) **Joining the scheme**

The scheme would be open to any business with a turnover of £100,000 or less. Its use would not be compulsory, businesses would be allowed to enter or leave the scheme once a year. A business electing to join the scheme would contract with Customs to remain in it for a full year, making nine agreed payments, on predetermined dates, by direct debit. The contract would stipulate that Customs could terminate the arrangements in the event of a default on any instalment, the business then being required to account for tax on a quarterly basis.

#### b) **General procedure**

The procedure would be as follows:

i) **Annual assessments.** We would establish a tax debt for the coming year by issuing an assessment based on the net VAT paid in the preceding year. In calculating this assessment, it would be necessary to allow for anticipated changes in turnover, trading and inflation. It would also be necessary to allow for a subsequent adjustment if tax rates were to change. The scheme would be open only to businesses with a full year's trading experience. This would preclude newly registered businesses but would be necessary because of the need to make a proper assessment.

ii) **Payment by instalments.** The annual assessment would be divided by ten and payment would be made by nine monthly instalments by means of direct debit, plus a final tenth payment (not by direct debit). This last payment, including any adjustment necessary to cover the tax liability for the whole year, would be sent together with the annual VAT return - two months after the end of the accounting year.

c) **Transition to the new system**

To ease the transition from quarterly to monthly payments, the business would start to pay by instalments four months after the end of the last quarterly accounting period ie at the time the next quarterly payment would have been due. The position is illustrated below:

Start of Acctg Period													End of Acctg Period		
0	1	2	3	4	5	6	7	8	9	10	11	12	13	14 (months)	
				1st	2nd	3rd	4th	5th	6th	7th	8th	9th			Final payment (balance) with annual return
				Payments by			direct debit								

So the business would make its final balancing payment for the first year by the end of month 14, and two months later would make the first of the regular payments on account for the second year.

d) **Failure to comply**

A default in respect of any one of the nine instalments would **not** be a default for the purposes of the Default Surcharge regime. However, late submission of the annual return would count towards surcharge and any business which defaulted on its annual VAT return would be reverted to the normal quarterly accounting system. Equally, if businesses were to fail to make the agreed payments, they would be reverted to quarterly VAT returns and payment of tax and would consequently be brought into the normal surcharge enforcement regime for those future quarterly returns.



## CHAPTER 3: MAINTAINING AND PRESERVING RECORDS

3.1 Generally speaking, the records and accounts which a business maintains are for it to decide. Our only requirement is that they should be in sufficient detail for the tax that is to be paid or claimed to be correctly calculated, for complete and accurate VAT returns to be compiled, and for our officers to be able to check the returns. We do not insist that these records are maintained in any particular form, except for the VAT account, and we will normally agree to them being held on microfilm, microfiche, magnetic tape, disc etc subject to there being satisfactory audit trails.

3.2 Our requirements on records and accounts are set out in Section VIII to Notice 700, "The VAT guide". Once a business has decided on the records it wishes to maintain the law requires it to preserve them for six years. The period for preservation was extended from three to six years by the Finance Act 1985, following a recommendation made in 1983 by the independent Keith Committee which examined the enforcement powers of the two revenue departments. This extension was recommended because we have always been able to assess tax for the previous six years and because control visits to many businesses are now made less frequently than the once in three years originally envisaged. This brings our requirements more closely into line with direct taxation and company law.

3.3 We have always sympathetically considered requests for earlier disposal of ancillary records where retention causes storage problems or is inordinately expensive. However, the disposal of records does not exonerate businesses from their potential liability to further assessment of tax for the accounting periods to which the records related.

3.4 It is neither possible, nor desirable, to offer any general easement on which records need not be preserved for six years. In our view the best and least burdensome system is the current one where decisions are made on an individual basis. We shall continue to accept reasonable proposals for early disposal of records and will publicise the availability of this dispensation.

3.5 However, while written representations about the extension from three to six years have been relatively few in number, we are aware of an understandable concern that the rules should not be too inflexible for small businesses. In order, therefore, to examine further our practice in this area we **propose** to engage an independent consultant whose terms of reference will be:

"To consider the effect on small businesses of the requirement to preserve VAT records for a maximum of six years; the records that need to be covered by these requirements; and to make recommendations consistent with Customs and Excise's needs in respect of the revenue control of the tax."

We expect that the consultant, when appointed, will wish to approach trade organisations, representative bodies and a cross section of small businesses.



## CHAPTER 4: REVIEW OF REGISTRATION AND DEREGISTRATION REQUIREMENTS

### Introduction

4.1 The legal requirements governing registration and deregistration for VAT have remained largely unaltered since the start of the tax in 1973. Over the years it has become apparent that there are a number of areas where change is needed. With the introduction of civil penalties for late registration we decided to see how the law could be simplified to benefit the business community.

4.2 As part of the review a range of interested trade and professional organisations were consulted earlier this year. The many constructive suggestions received form the basis for the proposals in this chapter. There are two main elements: an increase in the time allowed to register for VAT and a number of minor, but significant, changes mostly intended to make it easier for small businesses to cancel their VAT registration.

### REGISTRATION

#### Time limit for notification based on past turnover

4.3 We recognise that the requirement to notify liability to registration within ten days of the end of the quarter/four quarters in which the liability arose may appear an unreasonably short period in which to comply with the law. It can be especially difficult for small businesses. The natural delay between the quarter end, consultation with advisers, and application for registration inevitably exhausts the ten day time limit. This problem has been brought sharply into focus with the introduction of a civil penalty for failing to notify at the proper time. Following careful consideration of the comments made and our own revenue control requirements, we **propose** that the time limit be extended from ten days to one month. This accords with the majority of representations received. Registration would be effected from the day following that month unless an earlier date is requested and agreed.

#### Time limit for notification based on anticipated future turnover

4.4 The law requiring notification based on future turnover is different from that relating to past turnover. It requires a person to notify immediately if there are reasonable grounds for believing that the registration threshold will be exceeded in the coming year. In theory, this requirement allows no time for consultation before a trader risks incurring a civil penalty for late notification. In practice, however, a person setting out in business will usually have given some thought to his prospects before starting to trade. Equally a person already in business will know if his turnover is climbing or whether he is expecting a dramatic upturn in trade because of a forthcoming contract or the like. Nevertheless, we share the general feelings expressed by business and feel that a person applying for registration because of future turnover should have the same period of grace allowed to applications based on past trade. We **propose**, therefore, that one month be allowed in which to notify. Registration would be effected from the day following that month unless an earlier date



is requested and agreed.

## DEREGISTRATION

### Deregistration based on past turnover

4.5 A person who is continuing in business, but who wishes to deregister because of diminished turnover, must satisfy two tests before deregistration can be allowed. The first takes account of the turnover achieved in each of the past two years; the second has regard to the anticipated turnover in the year then beginning. Although past turnover can be an indication of the level of trade that might be expected in the future it is largely a superfluous test. When considering an application to deregister it is the level of future turnover that matters. With this in mind we propose that the past turnover test be abolished.

### Value of supplies for deregistration purposes

4.6 When a person wishes to deregister because he anticipates that the next year's trading will be below the deregistration threshold he has to work out his expected turnover on a VAT-inclusive basis. If this produces a figure above the threshold, deregistration is not permitted. Those applying for deregistration in such circumstances will usually be operating around the registration/deregistration threshold levels and the need to include output tax in the calculation often causes the threshold to be breached. The result is that many otherwise non-registrable businesses are required to remain registered. This puts them at a disadvantage compared with unregistered competitors of a similar size. To resolve this problem we propose that the law should be amended so that output tax can be excluded from these calculations.

## MISCELLANEOUS

### Time limit for notifying cessation of trade

4.7 Currently a person who ceases to trade is required to notify us within ten days. As with the time limit for notifying liability to be registered, ten days might be thought to be too short. We propose that this requirement be brought into line with the other time limit proposals by extending the period to one month.

### Liability to registration arising after deregistration

4.8 Once a person has been deregistered because of reduced turnover his liability to further registration is the same as for any unregistered person. It is possible for a person to be deregistered because the level of anticipated future turnover will not exceed the deregistration threshold, only to find almost immediately that he is liable to register again by virtue of past turnover, either wholly or in part, prior to the date of deregistration.

4.9 Provided the trader gave us the correct information when making his application to deregister, and if there has been no significant change in the pattern of trade since deregistration was allowed, it seems unreasonable to require him, in such circumstances, to re-register. As the law stands we have no discretion in the matter; we are obliged to register the trader. To avoid this harsh and unintended effect we **propose** that the law be amended so that turnover prior to deregistration may be ignored when determining further liability to be registered.

#### Material changes arising after exemption from registration

4.10 When a person has been granted exemption from registration, eg because he makes only zero-rated supplies, he is required to notify us "without delay" of any material change in the nature of supplies being made. This allows us properly to consider whether or not the person should continue to be exempted from registration. The lack of a firm timescale creates an uncertain situation and we **propose** that a specific time limit of one month be introduced for notifying material changes, so that a trader is left in no doubt as to his obligations.

#### Compulsory deregistration of traders with turnover below the registration threshold

4.11 There are currently about 250,000 registered traders whose turnover is below the registration threshold. The cost of controlling these traders exceeds their total revenue yield and they impose a considerable burden on our resources. Significant savings could be made if such businesses were not allowed to register or remain registered unless they satisfied the tests for obligatory liability to register, based on annual or quarterly turnover. The many small businesses which did not satisfy those tests would, by being excluded from the register, be relieved from VAT accounting and record-keeping requirements, although some would suffer other disadvantages from not being registered.

No decision has yet been made. Moreover any such change would need to be examined in the context of European Community law and we would have to discuss it with our Community partners.



## CHAPTER 5: RETAIL SCHEMES

This chapter, which sets out our proposals for change to the present retail schemes, will concern those businesses which now use a retail scheme and are therefore familiar with the workings of the schemes.

### Introduction

5.1 The intention of the retail schemes is for each scheme to give a 'tax due' result which equals or closely approximates to that given by the normal method of VAT accounting. In general terms, the simpler schemes can be less accurate than the more complicated schemes and thus there has to be a restriction on their use, normally by applying turnover limits above which the simpler schemes cannot be used.

5.2 The various turnover and other limits associated with the schemes have been regularly reviewed since 1973. Such a review was due in 1986, but we decided on this occasion to widen it and include it as one of the subjects on which we would, as part of our 'deregulation' activities, review our policy, especially as regards small businesses and the practicability of any further special arrangements for them. Our review has not been limited to retail schemes as they affect small business; we have considered their impact on all retail businesses with a view to producing a balance as between the interests of the revenue and businesses.

5.3 To achieve a proper balance we have examined the fundamental concepts of the retail schemes package as a whole, and also the requirements of each individual scheme. We are seeking to identify those schemes or aspects of scheme accounting which cause particular difficulties for businesses, and especially small ones, or for our control, or lead to inordinate effects on the revenue, and where possible propose solutions to these problems which are fair to all interests.

5.4 The following paper is written in two parts. **Part 1** looks at each scheme, while **Part 2** looks at other general aspects which affect the package as a whole. Several specific proposals are made in the paper and we would welcome comments regarding these as well as any other suggestions for improvement of the schemes.

### **PART 1: THE INDIVIDUAL RETAIL SCHEMES**

#### Retail schemes A, F, H and J

5.5 The working methods of Schemes A, F, H and J are in our view well founded and we have no proposals to change them.

#### Retail scheme B

5.6 The working method of this scheme is based on the assumption that all zero-rated goods purchased in a tax period are sold in that same period. This is seldom likely to be the case, but any inaccuracies which this method causes are usually ironed out over a period of time by consistency in a trader's purchasing patterns. Nevertheless, if the scheme were freely available for use by seasonal businesses, the true value of standard-rated supplies made in a tax period could be considerably distorted. To prevent



this, use of the scheme has to be restricted, through the rule that zero-rated goods must not exceed 50% of the total taxable turnover.

5.7 Because Scheme B is basically very simple to operate we propose, as a further option, or as a replacement, an adaptation which would make its use more widely available. This adaptation would not have a 50% rule, but would require an annual stock adjustment to take into account the difference in zero-rated stock levels at the start and end of each year.

5.8 A further adaptation, which is already available to retailers with a turnover not exceeding £325,000 is based on a standard fixed mark-up (Notice 727, paragraph 20). The present standard mark-up of 14% is unrealistic and could be unfair to some traders. We therefore propose that varied but fixed mark-ups based on types of goods should be introduced, as follows:

<u>Type of goods</u>	<u>Fixed mark-up (%)</u>
Food	20
Children's clothing & footwear	35
Books, maps etc	40
Newspapers & magazines	33
Goods not elsewhere specified	15

These proposals will provide a more accurate scheme which can be made more widely available. As the scheme will still be somewhat inaccurate, a turnover limit is still necessary, but to assist medium-sized businesses who would like to use the scheme an increase in the turnover limit from £325,000 to £500,000 is proposed.

#### Retail scheme C

5.9 This scheme can be used by most retailers supplying goods, but only where their total taxable turnover does not exceed £75,000 a year. It is a simple scheme, but it can be the most inaccurate in practice because diverse businesses are banded together by their common trade classification and one fixed mark-up is applied to all goods sold. The scheme takes no account of important factors such as different purchase and sales mixes of individual businesses, and there is inevitably an element of arbitrariness in the interpretation of the trade classification bandings eg similar stores might be regarded by one businessman as general grocers (fixed mark-up 20%), and by another as a general stores (fixed mark-up 50%).

5.10 The turnover limit is an essential factor in limiting the possible adverse effects of the scheme on the revenue, and we consider that the restriction of use to only small businesses must continue. However, the present limit was fixed in 1983 and, to keep it in line with the movement in the Retail Price Index, we propose that it be increased from £75,000 to £90,000.

5.11 Because the scheme is simple to operate and can be particularly useful for small retailers, fundamental changes are not proposed. However, we have re-examined the fixed mark-ups, in the light of available statistical information, with the aim of retaining the present basic simplicity of the scheme while setting the fixed mark-ups at more realistic levels. The following



revised mark-ups are proposed.

<u>VAT trade classification</u> <u>in bands</u>	<u>Type of business</u>	<u>Fixed mark-up</u>
Band 1	8207 Off-licences 8214 Confectioners, tobacconists, newsagents	) 15.1/2%
Band 2	8201 Grocers 8202 Dairymen 8203 Butchers 8204 Fishmongers & poulterers 8206 Bread & flour confectioners	) 20%
Band 3	8205 Greengrocers & fruiterers 8222 Radio & electrical goods 8225 Cycle & perambulator shops	) 40%
Band 4	All classifications from 8201 to 8239 not otherwise mentioned	) 50%
Band 5	8215 Footwear shops 8218 Retail furriers 8233 Florists, nurserymen and garden shops	) 60%
Band 6	8213 General mail order houses 8231 Leather goods, sports goods, toys & fancy goods shops	) 70%
Band 7	8229 Jewellers	) 85%
Band 8	Specified businesses	Healthfood & wholefood shops* ) 90%

\* only healthfood and wholefood shops have so far been identified.

5.12 A note would be inserted in the pamphlet 'How to work Scheme C' to advise users that the mark-ups applicable to 'specified businesses' in Band 8 take precedence over any other trade classification mark-ups in Bands 1 to 7, and must be used if appropriate to the type of business.

5.13 Further types of businesses could be added to Band 8 in due course, especially where the mark-up appropriate to their normal trade classification band is found to be significantly inaccurate.

#### Retail scheme D

5.14 This scheme assumes that the same mark-up applies to both standard and zero-rated goods. A business whose mark-up on zero-rated goods is higher on average than that on its standard-rated goods will pay more tax than it would by using the normal method of VAT accounting (this danger is clearly explained in the 'How to work' leaflet). Conversely, a business whose standard-rated mark-up is greater, on average, than its zero-rated mark-up will pay less tax than by using the normal VAT method.



5.15 If unrestricted use of this scheme were allowed, these inaccuracies and the possibilities for selected 'hiving-off' of standard-rated goods with low mark-ups could result in unacceptable effects on the revenue. A turnover limit restricting use of the scheme to small and medium-sized businesses is an essential factor in limiting these possible adverse effects.

5.16 The present turnover limit of £200,000 was set in 1983 and is now due to be revised to keep it in line with the Retail Price Index. However, given the limited range of zero-rated goods and the mark-up normally applied to those goods, we now feel that in practice the possibilities for manipulation of the scheme exist only for the larger businesses. To make the scheme more widely available, we therefore propose that the limit should be raised to £500,000.

#### Retail scheme E

5.17 We have no proposals for changing this scheme in its usual form, but paragraph 20 (c) of the retail schemes Notice 727 contains a description of "Adaptation 2". This adaptation is very close to Scheme E but allows takings for either standard or zero-rated sales to be established, and requires account to be taken of opening and closing stocks each quarter. The proposed amendment to Scheme B (see paragraph 5.7 above), would make the facility in Adaptation 2 to calculate the expected selling prices of zero-rated goods unnecessary. We therefore propose that Adaptation 2 should be modified to provide for the calculation of expected selling prices of standard-rated goods only, and that there should be no restriction on its use. This would provide a useful and very accurate alternative to Scheme E for those prepared to take stock quarterly.

#### Retail scheme G

5.18 The scheme is very similar to Scheme D, in that it assumes that the same mark-up applies to both standard and zero-rated goods. A business whose mark-up on zero-rated goods is higher on average than on its standard-rated goods will pay more tax than it would by using the normal method of VAT accounting (this danger again being clearly indicated in the scheme 'How to work' pamphlet). Conversely, a business whose standard-rated mark-up is greater on average than its zero-rated mark-up will pay less tax than by using the normal VAT method. These inherent mark-up inaccuracies and the possibility of selected 'hiving-off' of standard-rated goods with low mark-ups, can result in unacceptable losses to the revenue, especially as the scheme may be used by very large businesses. The scheme incorporates a 1/8th (12½%) uplift in order to limit these adverse effects. We will review the level of this uplift.

5.19 Any upward movement in the maximum turnover limit applying to Scheme D would allow Scheme G users, whose turnover is within the new limit, to change to the simpler, and possibly more beneficial, Scheme D. If a large proportion of Scheme G users change to Scheme D it may be possible to cancel Scheme G. In the meantime we propose that the Scheme G minimum turnover limit be abolished.



## Retail scheme J - Adaptations

5.20 We have no proposals for changing Scheme J in its usual form, but there are currently two minor adaptations of this scheme which are explained in paragraph 19 of the main retail scheme Notice 727. Both of these adaptations are designed to help businesses which sell zero-rated goods with a short shelf-life, and which would otherwise pay too much tax until the normal scheme's annual adjustment corrected the situation. The first adaptation allows a three-monthly stock evaluation instead of the annual adjustment. The second adaptation allows the omission of opening stock until the annual adjustment. Both of the adaptations are simple to operate and we do not propose any changes to their working methods; but we do **propose** that the working explanations be moved from the main retail scheme notice to incorporate them instead into the Scheme J 'How to work' pamphlet, as an aid to better understanding of them.

## **PART 2: GENERAL ASPECTS OF THE RETAIL SCHEMES**

### Methods of reckoning gross takings

5.21 There are two methods of establishing the sum of gross takings in any period: the 'standard' method, based on total payments received in the period, including payments received from finance houses providing credit facilities for the business; and the 'optional' method, based on the total value of all supplies made in the period. The intention is that either method should provide similar results of the value of supplies, and thus tax due, in any tax period. The standard method requires the inclusion of cash paid in respect of instalments for credit supplies made in previous periods as well as cash paid in respect of supplies made in the current period. With businesses making self-financed credit supplies, the cash based standard method gives bad debt relief automatically in respect of self-financed credit supplies. Also, newly registered traders using the standard method have their supplies undervalued for a period equal to the length of their normal credit period. Otherwise the methods give more or less the same results.

5.22 While bad debts are automatically relieved under the standard method, the extent of this benefit is commonly overstated. As cash sales, including payments by cheque and credit card, are treated identically under the standard and optional methods, the only benefit from bad debt relief is in respect of self-financed credit supplies, a system which is normally used only by the larger retailers.

5.23 The advantage accruing to a newly registered business involved in self-financed credit and using the standard method is often described as no more than a legitimate cashflow advantage, but we believe that such a specific advantage, limited to this particular set of businesses, is unwarranted. A cashflow advantage, however temporary, is an unintentional rather than a conscious effect of the retail schemes and can result in unfair competition between similar businesses. Moreover, there have been instances where changes from the optional method to the standard method, involving the transfer of business between different but related legal entities, has been used as a tax manipulation ploy to gain inordinate and unwarranted cashflow advantage.



5.24 To remove the inequities, to simplify the overall package and also to stop the system being used for unjustified tax avoidance purposes, we **propose** that the standard method of reckoning gross takings should be withdrawn. Current users of the standard method would be given a period of grace to make any adjustments necessary to their accounting systems. We would emphasise that this would not affect the wholly cash-dealing business; it would affect only those businesses providing self-financed credit facilities. The change will therefore have little or no impact on small and medium-sized retail businesses.

#### Eligibility to use retail schemes

5.25 The eligibility rules for using the schemes, given in the retail schemes Notice 727, are intended to restrict the use of the schemes to "anyone (not just a shopkeeper) who deals mainly with the public and who cannot, by the nature of his business, issue a tax invoice for each sale". Since only two of the schemes, when properly operated, always provide the same results as the normal method of calculating VAT, we consider it essential that the schemes should be available only to those who actually need to use them, and then only in respect of retail supplies.

5.26 Some businesses like solicitors, accountants, estate agents etc, who can and do issue tax invoices, have been allowed to use retail schemes in the past. We **propose** that the retail scheme facility be withdrawn from such businesses, current users being allowed a period of grace to make any necessary adjustments to their accounting systems. The cash accounting facility proposed elsewhere in this document would cushion the effect on small businesses so that their position in respect of output tax would remain unaffected.

5.27 Some businesses make mixed retail/wholesale supplies, and where turnover is derived mainly from retail sales we have allowed a retail scheme to be used for all sales. In respect of its wholesale supplies, such a mixed business has a large cashflow advantage over its competitors because, although it must issue a tax invoice for wholesale supplies made to other registered traders, it will not account for output tax until receipt of payment. Other wholesalers must account for output tax on issue of invoices.

5.28 To remove this inequity of treatment we **propose** that retail schemes should in future be used only for retail supplies and that their use for non-retail supplies should be withdrawn. Again, we would allow a period of grace for current users to make any adjustments necessary to their accounting systems. We would repeat that, given the introduction of a cash accounting facility, any detrimental effects of this proposal would be minimised for small traders.

#### Mixtures of retail schemes

5.29 The main retail scheme Notice 727, Section 3, describes permitted mixtures of schemes which are available for use. They



may be used provided that:

- a) a business is prevented from using a scheme only because it supplies services, or makes and/or grows its own goods; or
- b) a business is split into separate departments or shops.

There are separate rules according to whether **different** schemes are to be used for separate parts of a business as opposed to the **same** scheme being used separately in each part of the business.

5.30 The introduction to Section 3 of the retail scheme notice says that a business may be able to use more than one scheme or account for tax on some of its supplies in the normal VAT way. The introduction then goes on to say, "one or other of these options might help if ....." and states conditions (a) and (b) as above. This basic eligibility statement is somewhat misleading. The intention is that, because scheme mixture can be used to manipulate tax liability, a mixture of schemes **may only** be used if either of the conditions at (a) and (b) above exist. We **propose** to amend this statement of eligibility to make this clear.

5.31 The meaning of 'separate part' of a business is not defined and in order to help dispel ambiguity we **propose** that condition (b) above be amended to read, "your business is split into separate parts, (a part is to be taken as a separate department or a separate shop)". This amendment would clarify the degree of separateness that is required.

5.32 Because the scheme mixture provisions have been used to manipulate tax liability we **propose** amending Regulation 3 of the VAT (Supplies by Retailers) Regulations 1972 (SI 1148/1972) in order to give us clear powers to refuse the use of retail schemes where such use does not give a proper reflection of a retailer's tax liability. Such a refusal would, of course, be open to appeal to the independent VAT Tribunal under Section 40 of the VAT Act 1983.

### Conclusions

5.33 The large majority of the 15 changes which we propose to the various retail schemes would be of benefit to retailers. Higher scheme turnover limits and new variations will increase choice. Some schemes would in future be more accurate in their operation and in others the rules would be easier to understand. Three proposals are aimed at stopping the schemes being used for unwarranted tax gain or avoidance, but these changes would have no effect on the tax liability of the vast majority of scheme users. The overall balance of the package would be beneficial to small and medium-sized retail businesses.

## ABOLITION OF VAT ON CREDIT TRANSACTIONS BETWEEN REGISTERED TRADERS

1. It has sometimes been argued that the administrative burden of VAT would be eased if tax were abolished on credit transactions between registered traders. In effect, all the tax would be collected at the point of sale to the final consumer.

2. A version of this proposal was studied in 1978 by a working party consisting of the Consultative Committee of Accounting Bodies, the CBI, the Retail Consortium, the Federation of Wholesale and Industrial Distributors and Customs and Excise. The working party concluded (the CCAB dissenting) that the balance of advantage lay with retaining the present system.

3. A number of very significant difficulties remain with the proposal. We believe that it would be incompatible with Community law and there would be major problems in ensuring the revenue-neutrality and in controlling such a scheme. Moreover, we remain unconvinced that there is substantial support for the idea within the business community as a whole or that there would be any substantial administrative saving to small businesses in its adoption.

4. From the point of view of the small business:

- all businesses would have to be registered and this authorisation renewed probably on an annual basis;
- records would still be required of their supplies;
- tax would be called for on all sales to non-registered customers and on appropriation of stocks to their own use;
- they would have to ensure the credentials of all their customers who claimed to be registered and bear responsibility for any improper tax-free sales;
- similarly, that sales were for the business use of registered customers;
- responsibility would rest for the whole of the tax yield with the retailer, from whom more frequent VAT returns might have to become mandatory;
- retail schemes would have to be reviewed since most of the special schemes for retailers would be incompatible with the operation of a tax-free ring.

5. Complex measures would be necessary for all businesses to ensure that the present £2,300 million revenue yield from "sticking" input tax on cars, business entertainment and partial exemption was maintained.



6. We also cannot foresee any savings in our administrative costs. To suggest that the staff currently employed on controlling the tax could be redeployed elsewhere, either because no tax would change hands in many transactions or because there would be no input tax frauds is, in our judgement, an oversimplification. Our experience in administering purchase tax (which was restricted to 75,000 wholesalers) showed there are considerable opportunities for evading the tax, particularly when there is not the incentive to declare purchases so that input tax may be reclaimed. Furthermore, a register of the majority of the 1.5 million businesses would have to be maintained and returns collected and processed from them; and we would have to be satisfied that supplies being made tax-free were to bona-fide business registrations.

7. To sum up, superficially attractive though the proposition may be, we do not believe that there are sufficient benefits to justify such a major upheaval to the present system.



10 DOWNING STREET

LONDON SW1A 2AA

*From the Private Secretary*

5 September 1986

I am writing on behalf of the Prime Minister to acknowledge your letter dated July 1986 which was received in this office on 4 September. I shall show your letter and the first Annual Report of the Small Firms Service to Mrs. Thatcher when she returns from Scotland.

(P. A. BEARPARK)

David Trippier, Esq., RD, JP, MP.



SMALL

Firms Service Report sent to Policy Unit

JA

Report  
19/9

checked Pol. Unit  
23/9.

PROFESSOR GRIFFITHS

I should be grateful for the views of the appropriate member of the Policy Unit.

ASB

ANDY BEARPARK

5 September 1986

File

086

MR. WARRY

INTERNATIONAL SMALL BUSINESS CONGRESS

The Prime Minister has said she would like to consider at the next diary meeting on 1 September the idea of persuading the Small Firms Merit Awards at this Conference. The diary over the period is tricky, but does not rule out her attending for a short while.

I am letting you know this simply for information. You said you did not in any case need to go back to those who were lobbying you on the matter. If they tackled you again, I think it would be unwise to make any optimistic noises at this stage.

Mark Addison

6 August 1986

DG2BHV





Parliamentary Under  
Secretary of State

DAVID TRIPPIER RD JP MP

Rt Hon Margaret Thatcher MP  
House of Commons  
LONDON SW1A 0AA

July 1986

R419  
Department of Employment  
Caxton House Tothill Street London SW1H 9NF  
Telephone Direct Line 01-213 4884  
Switchboard 01-215 3000

Dear Prime Minister,

... I enclose a copy of the first Annual Report of the Small Firms Service. We propose that this should now be issued each year because I believe that the Service offers a highly sophisticated and professional service to the small firms sector, of which we can be justly proud and which we should publicise as much as possible.

As you know, the Small Firms Service provides information on a wide range of subjects to those setting up and running small businesses. Through experienced businessmen and women on contract to the Department it also provides a counselling service to give practical advice and guidance. I am particularly pleased that when you and Ministers receive letters from small businesses, we are able to react positively by arranging for the Service and its counsellors to offer assistance.

As you will see, the demands upon the Service for both enquiries and counselling have shown a marked increase in recent years. I hope you will agree that by continuing to offer and promote a service of this kind we are giving practical demonstration to the Government's policy of encouraging small firms to set up and flourish. For this reason I have arranged for the report to be distributed widely to those connected with small firms.

Yours ever  
David

DT3AAH

Account for  
small items  
p. 6





MR NORGROVE

9 May 1986

ACCOUNTING AND AUDIT REQUIREMENTS FOR SMALL COMPANIES

There are three minor but important deregulation issues: the Revenue (wrongly) object to them all, while the DTI are against eliminating statutory audit.

1. Reducing detailed accounting requirements for firms with a turnover less than £2m. This is a thoroughly sensible measure and the Revenue have had great difficulty in particularising exactly what information they would lose. The Revenue already ask firms for more information than is required by the Companies Acts, accountants produce this automatically. There is no reason why the changes in accounting requirements should disturb this arrangement.
  
2. To study how disincorporation of small companies can be facilitated. This would be a useful measure although there may be major difficulties in achieving it, but it is surely wrong for the Revenue to pre-judge the issue.
  
3. Statutory Audit

Most small companies keep totally inadequate records and then hire an accountant to 'construct' the accounts relying heavily on assurances and explanations from the directors. It is the same accountant who also 'audits' his own figures. Such an exercise is not only misleading but also (according to DTI) costs between £200 and £400. It is unlikely to reduce fraud - indeed it may increase it because the accountant can act as a convenient buffer between the directors fib and its public dissemination. The best argument against abolition is that it would give the wrong signal to our commitment to eliminate fraud in large companies. But this need not be so:

- a. the exemption will only apply to companies with turnover less than £0.25m where the shareholders

are also the directors of the company (typically husband and wife companies);

- b. a qualified accountant will still be required;
- c. the directors would sign a statement as per the annex to the E(A) paper to forcefully bring home to them their own legal liability for honest and proper accounting (which should be more effective than statutory audit);
- d. the situation is not comparable with large companies because they use an external independent auditor whereas small company directors hire an accountant, who is then required to assume an auditor's role. This sort of dual capacity was done away with for solicitors long ago.

The Revenue claim they would need an extra 400 tax inspectors because the PAC would require the number of company accounts investigated increased from 1% to the 3% that is currently applied to unincorporated businesses. This is totally unnecessary, but if the Revenue were to give in to PAC pressure then surely the right answer would be for them to investigate 2% of each. And in any event E(A) discussions over the last year have given a partial green light to Departments increasing their head count where they can show there is a Revenue saving to be made.

Abolition of statutory audit for small companies is strongly recommended by the Institute of Chartered Accountants who really ought to know. We believe it is important if the deregulation initiative is to be sustained, and the published recommendations of the DTI's own Rayner scrutiny are to be honoured, that the audit should be abolished.

PETER WARRY

- 2 -

CONFIDENTIAL



RESTRICTED



DEPARTMENT OF TRADE AND INDUSTRY

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Secretary of State for Trade and Industry

PS/

7 May 1986

RESTRICTED

David Norgrove Esq  
Private Secretary to the  
Prime Minister  
10 Downing Street  
LONDON  
SW1

*B/f for 12/5. /BF*

*Dear David,*

The EA meeting on 13 May will consider a paper by my Secretary of State on accounting and audit requirements for small companies.

I attach a copy of a report prepared by officials here on the outcome of the consultation exercise carried out by the Department last year which those responsible for briefing the Prime Minister might find helpful as background.

If those briefing Ministers for the meeting would like any further background, the contacts here are Ann Wilks (215 6088) and Stephen Spivey (215 6542).

Copies of this letter and the report go to Private Secretaries to members of E(A) and Sir Robert Armstrong.

*Yours ever,  
Michael*

MICHAEL GILBERTSON  
Private Secretary

RESTRICTED

DW1BEM

## ACCOUNTING AND AUDIT REQUIREMENTS FOR SMALL COMPANIES

### REPORT BY DTI OFFICIALS

#### 1. INTRODUCTION

1.1 The 'Burdens on Business' report published in March proposed that, subject to consultation and further consideration by Ministers, the Government should:

(a) eliminate the present statutory audit of accounts for 'shareholder-managed' small companies (ie companies where all the shareholders are directors); and

(b) reduce and simplify the content of accounts currently required from small companies in general.

The Department of Trade and Industry subsequently issued a consultative document on 4 June inviting comments on both points (including the option of abolishing the audit for all small companies) and related proposals for increasing the thresholds used to define small and medium sized companies for Companies Act purposes. Comments were requested by 30 September.

1.2 The consultative document was sent initially to over 40 representative organisations and made available free of charge to others on request. In all, over 4000 copies were issued, mostly to individual small companies and firms of accountants. By 30 September, 185 responses had been received. A further 19 were submitted after the deadline and have been taken into account in preparing this report. Overall, views on the audit requirement were more or less evenly divided though most of those who favoured dispensing with it either wished to do so only in relation to shareholder-managed companies or couple abolition with the introduction of new rules governing the preparation of accounts. On accounting requirements, there was a clear majority for simplification, though a significant minority thought present requirements should be maintained and, in some cases, strengthened.

1.3 Section 2 of this paper summarises the views expressed in the various responses to the consultative document. Section 3 analyses the arguments against which policy decisions need to be assessed. Section 4 discusses two additional issues - whether currently available forms of incorporation are best suited to the needs of small companies and the rules relating to the filing of accounts at the Companies Registration Offices (CRO) - which were raised by consultees and which are relevant to the overall package. Section 5 sets out our conclusions.

1.4 For convenience, sections 2 and 3 consider audit and accounting requirements separately. However, there is a trade-off between the two and the related issue of thresholds. Accounting rules obviously affect the scope



and cost of audit. And decisions on thresholds will determine the number of companies which benefit from any changes in present requirements.

- 1.5 Whilst we have taken account of all the responses, we have paid particular attention to the comments received from small companies themselves and from organisations representing their own interests. A separate summary of these comments is at Annex A. 60% of this group favoured abolishing the audit requirement at least for shareholder-managed companies but in general terms there was no significant difference between their views and those of respondents as a whole. Where views are divided, the division of opinion runs across the various interest groups, not between them.

## 2. SUMMARY OF RESPONSES

### AUDIT

- 2.1 The purpose of the statutory audit requirement is to check that the accounts have been properly prepared and give a true and fair view of the company's position. In the course of the audit, the auditor will generally also consider the adequacy of the company's financial controls and bring any material defects discovered to the attention of the directors. The audit thus assists the management of the company as well as protecting the interests of shareholders, employees and anyone considering investing in or doing business with it by giving them some assurance about the quality of the accounts. In addition, small company auditors normally provide a wide range of non-audit services. In particular, it is common practice for the accountant concerned not only to write up the books and prepare the basic accounts but to deal with regulatory returns and VAT, PAYE and other tax matters, as well as providing basic financial advice. Situations where the annual audit represents the sum total of an auditor's involvement with a small company are very much the exception rather than the rule.
- 2.2 Against this background, the consultation document invited comments on:
- (a) the quality of small company audits;
  - (b) their value to management;
  - (c) their value to shareholders;
  - (d) their value to third parties - banks and other suppliers of capital, trade creditors, potential customers and Government departments, particularly the Revenue; and
  - (e) the cost of the audit in relation to the benefits it provides.



## The Quality of the Small Company Audit

- 2.3 Small companies by and large do not have elaborate internal accounting systems. In practice, this means that the auditor necessarily has to take much of the information he is given on trust which, in turn, often results in use of the so-called 'Example 6' Audit Report. This makes it clear that the auditor has relied on assurances from the directors about the accuracy and completeness of the company's records and that the auditor's opinion as to the truth and fairness of the accounts should be seen in that light. There is no reliable information on the extent to which Example 6 reports are used but the biggest recent survey of company accounts suggests that as many as 25% of small company audit reports may be qualified in that way. Some of the responses to the consultative document suggest the proportion may be even greater. Over 50% of the auditors who participated in research by the Scottish Institute into small company audits indicated that they used it 'either almost always or usually'. And some firms of accountants claimed its use was 'common and almost standard'.
- 2.4 The views expressed by consultees reflected the division of opinion within the accountancy profession on this issue. Some considered that small company accounts, and particularly those of companies with turnovers of less than 250,000, were so frequently qualified in material matters that the audit report 'serves no useful purpose other than to indicate that (such) accounts are unauditable'. In much the same vein, the Scottish Institute considered that 'as matters stand, we are continually stubbing our toes in an attempt to perform audits' and that it should be admitted that in many small companies the evidence available to auditors is such that they can do no more than say that as far as they can see the accounts are not misleading. On the other hand, the proponents of audit rejected any suggestion of unauditability and pointed out that the auditor's task is to form and express a reasonable opinion on the accounts, not to certify their accuracy. The non-existence of reliable internal controls may add to the work involved in forming such an opinion but even where an auditor is forced to seek assurances from management he can assess its value by analytical review of the company's accounting records and against his own knowledge of the business; inspection of documentation is only one method of obtaining audit evidence. Some accountants also thought that the extent to which Example 6 reports are used reflects the inadequacies of auditors rather than the audit itself.
- 2.5 Whilst arguing for retention of the audit requirement, a number of accountants thought that small company audits could be made more cost-effective, for example, by reducing their scope or relating them more directly to management's needs and concerns. They also believed that the profession should tighten up the guidelines on the use of Example 6 reports with a view to ensuring that they are used much



less frequently and only where justified.

#### Value to Management

- 2.6 Those in favour of abolishing the audit requirement ('pro-abolitionists') argued that audited accounts are largely irrelevant to the management of the business in that they deal with past rather than current events. Management decisions require timely information presented in a way which meets the working requirements of those concerned whereas audited figures may be received months after the year-end and are prepared in a rigid format prescribed by statute. On that basis, most of the small companies which commented claimed that for management purposes their audited accounts were 'just so much waste paper'. Some accountants also said in so many words that they gave their clients short and simple sets of accounts showing them exactly how the business was performing as well as audited accounts produced to Companies Act specifications which served no purpose other than satisfying statutory requirements. Those claims do not altogether square, however, with the results of the various surveys commissioned by accountancy firms during the consultation period and of earlier academic research. A study done for Ernst & Whinney, for example, found that 70% of small companies surveyed saw the audit as an important element in the management of the company, thus broadly confirming the outcome of a 1984 survey by Page of Southampton University which found that 84% of small businessmen sampled believed audits help to improve the efficiency of the business. Against that, similar research by Professor Carsberg for the English Institute suggests that more than 90% of small companies base decisions on their own management accounts rather than on the annual accounts.
- 2.7 Notwithstanding these points, those against changing the status quo ('anti-abolitionists') contended that the audit - and the management letter which is a by-product of it - produces information directly relevant to management decisions. Their case focused primarily, however, on the value of the audit in terms of ensuring that small companies have proper financial management systems and controls and in getting small businessmen to focus on such matters. Their central theme was that the audit provides a framework and imposes a sense of discipline without which standards of financial management amongst small companies would be even lower than they are at present. A large number of respondents ranging from the English Institute to individual small firms and small business clubs considered that if the audit requirement were abolished companies would pay less attention to financial controls and that standards of accounting would inevitably suffer as a result.
- 2.8 A number of respondents argued for retention of the audit requirement on the grounds that it provides the only



certain means of ensuring that companies obtain professional accountancy advice at least once a year. Some went further and suggested that without audits some directors of small companies would be incapable of meeting their statutory obligations. Conversely, a number of accountancy firms argued that abolition would give them the opportunity to offer alternative and additional services to clients and generally make a more positive contribution to the running of the business. Touche Ross spoke for this group in presenting the audit as a barrier to its providing 'a much more constructive service which could be of substantial benefit to (small) companies and, indirectly, to the community as a whole'. The majority of respondents, however, thought it unlikely that small companies would use savings on audit to buy in financial advice. Responses from small companies themselves tended to confirm that view.

#### Value to Shareholders

- 2.9 The proposal put forward in the Burdens on Business report was based on the proposition that where all the shareholders of a company are directors the audit serves no useful purpose so far as they are concerned since they have direct access to information about the company's financial position. Responses from individual small businessmen largely echoed this view. Others pointed out, however, that family businesses are normally run by one or two of the directors and that even where all the directors are actively involved there can be no guarantee that all will have equal access to financial information or be able to evaluate it. The Association of Independent Businesses, for example, believed that audited accounts were a useful re-assurance for the working director not involved in financial management and generally desirable from the point of view of those not playing an active part in running the company. In the event of abolition, it and others also considered that practical problems might arise in relation to family owned shares held by nominees; the sale of shares to independent third parties; resignations as a result of family disputes; and retirements, deaths and divorces.
- 2.10 For those reasons, even pro-abolitionists considered that shareholders' rights to audited accounts should be preserved. Various proposals were put forward for achieving this but most consultees favoured making any decision to dispense with audit conditional on the annual agreement of all shareholders. It was suggested, however, that even this might be insufficient protection since individuals might be pressured into agreement against their better judgment.
- 2.11 Many of those who supported abolition for shareholder managed companies were against extending it to small companies generally. By and large, this was because they drew a distinction between the position of shareholder - directors and that of shareholders not directly involved in



the management of the business. On the other hand, it was argued that there is no fundamental difference between the two cases and that all shareholders in small companies should be given the opportunity to decide for themselves whether they wished to have an audit. Both sides were agreed, however, on the need to safeguard the interests of any minority opposed to dispensing with the audit. As with shareholder-managed companies, the general view was that this meant making any such decision conditional on the unanimous agreement of all shareholders on an annual basis. Others thought that it should be subject to approval by majority vote; suggested majorities ranged from 65%, (the Institute of Cost and Management Accountants) to 90% and 95%.

#### Value to Third Parties

- 2.12 Those opposed to abolition rested their case as much on the value of the audit to third parties dealing with a company as on its value to its managers and shareholders. In particular, they stressed the importance of audited accounts to creditors and government agencies, especially the Inland Revenue. Other interests identified were those of potential investors and customers. These points are discussed further in paras 2.14 - 2.21 below.
- 2.13 Underlying those points was the basic argument that the audit requirement is the price of limited liability status and that abolition would further open the way to abuse of that status. The pro-abolitionist tacitly accepted this whilst arguing that there was no point in requiring that price to be paid by way of performance of an otherwise unnecessary activity. Their view was that companies could best discharge their responsibilities to society as a whole by maintaining proper accounting records and preparing annual accounts giving a true and fair view, and that company law should focus on those activities rather than on audit. Both the Institutes of Chartered Accountants in (ICAEW) England and Wales and Scotland (ICAS) and numerous other organisations made specific proposals to that end. Some went further and suggested that there should also be a direct price for limited liability in the shape of a minimum share capital requirement of £5,000-£10,000 for all private companies.
- 2.14 The pro-abolitionists doubted whether banks and other providers of loan finance need audited accounts since they usually have access to up to date information about a company's cash position and, where necessary, can - and do - take security in the form of charges or personal guarantees. They also noted that the lack of audited accounts does not seem an obstacle to loans to partnerships and unincorporated bodies. The British Bankers Association and other banking respondents, however, were opposed to abolition. They acknowledged that audited accounts have weaknesses but they regarded them nonetheless as an important source of information for the lending banker in



that they provide a point of reference against which information supplied by prospective borrowers can be checked and give a historical perspective which is useful in establishing a firm's track record. In the absence of a statutory audit requirement and reliable up-to-date accounting records, they considered that banks might well require their own independent audits; and that given the costs involved and the consequent delay in finalising the loans, the net result might well be that companies found themselves worse rather than better off. The 3i Group and other venture capitalists took the same line.

- 2.15 On the same basis, some anti-abolitionists argued that without audited accounts companies would find it extremely difficult to raise new equity capital. Potential investors would be deterred by the additional costs involved in researching their financial position and those wishing to go public would face enormous costs in bringing their accounting records into line with listing requirements. Other respondents, however, considered that small companies were perfectly capable of arranging their affairs in such a way as to avoid such problems. In any case, the number of companies potentially affected by them must be extremely small.
- 2.16 Trade creditors were even more strongly opposed to abolition than the banks. For all the inadequacies of audited accounts, the Institute of Credit Management, the Finance Houses Association, and individual credit management agencies all regard them as an essential tool of their trade in that taking one year with another they reveal trends and provide a reference point for more sophisticated analytical techniques. The fact that the accounts are verified as conforming to common and recognised standards is considered especially important in that it provides a basis for comparing one company with another. They uniformly said that abolishing the audit requirement would make it more difficult and expensive for small companies to obtain credit and thereby penalise the very people it was intended to help. Comments from individual firms and trade associations reiterated that view. Generally, their position seemed to be that relative to the banks and other secured creditors, trade creditors are already in a very exposed position and that they would have even less protection if the accounts were not audited.
- 2.17 Some small companies were equally worried about the possible effects of abolition on their ability to compete for business. Local authorities, for example, place a good deal of reliance on audited accounts in placing contracts and considering requirements for performance bonding. Some large firms, eg British Telecom, operate on a similar basis whilst financial viability is also a factor in government procurement decisions, particularly in relation to large contracts or contracts large in relation to the size of the company concerned. The Ministry of Defence, for example, were opposed to abolition since they believe it would



increase the time and cost involved in judging the viability of small companies applying for inclusion in the Defence Contractors list. Other firms pointed out that it is common practice in some trades for buyers to be asked to make a payment before goods are received. In such cases, information about the viability of the supplier is just as important as information about any other trade debtor.

- 2.18 Views differed about the implications of abolition for the Inland Revenue and other Government departments which make use of audited accounts for tax and other financial purposes. Many firms believed that, whatever the outcome of the consultation, the Revenue and HM Customs and Excise would continue to insist on their producing audited accounts, or at least require them to employ an independent accountant qualified to audit to prepare their accounts. They saw little point in abolition on that basis. The anti-abolitionists claimed that there was no prospect of the Revenue accepting unaudited accounts and that abolition would lead inexorably to loss of tax revenue; and to the Revenue taking specific powers to carry out its own detailed investigations which would impose a greater burden on business than present audit requirements. Some respondents considered that abolition would also make life more difficult for firms seeking selective financial assistance (SFA), whether from central or local government.
- 2.19 Revenue officials made it clear to us that they regard full and reliable accounts as essential for their purposes. They also believe that the involvement of the auditor means that audited accounts are inherently more reliable than unaudited accounts. In policy terms this is reflected in the fact that whereas they aim to investigate annually 3% of the accounts submitted by unincorporated businesses, they aim to investigate only 1% of audited accounts (though the results of such investigations suggest that there is not much difference in the extent to which both types of accounts understate tax liability). They would therefore prefer to see the audit retained for its own sake and, more particularly, because they believe abolition would reduce the general reliability of accounts or at least be interpreted as a signal that reliability is less important than cost. The implication is that abolition could lead to tax losses and an increased level of company investigations (with consequent knock-on effects on staffing levels) but no attempt has been made to quantify these at this stage.
- 2.20 VAT returns are not audited but Customs and Excise consider audited accounts 'an essential tool' in verification of returns in that they help to put a company's trading position into perspective. If the audit were abolished, they too believe that officers would often need to spend more time in checking basic commercial records; that the number and duration of control visits would consequently have to be increased; and that staff resources, already under strain, would be stretched even further. Since control visits would be no substitute for audits, they also



believe that revenue could be put at risk.

- 2.21 Those responsible for SFA in this Department considered that the abolition of the audit could make the appraisal process more difficult and would require an increase in the input from professional accountants. However, the proportion of small firms likely to seek grants of a size which require a detailed assessment of a company's on-going viability is very small and where firms have full and accurate accounting records it should be possible to make such assessments without imposing any additional burden on companies. In principle, other Departments and local authorities should be able to operate on the same basis.

#### Cost of Audit

- 2.22 Most of the responses received from small companies complained about the high level of audit fees. It was clear, however, that these complaints related not to the cost of the audit as such but to the cost of accountancy services as a whole. In practice, the evidence suggests that pure audit costs typically represent no more than 10-20% of the total accountancy bill and where the auditor also prepares the accounts may well be even less. The position varies from company to company since the case with which the audit can be performed obviously depends on the quality of the company's accounting records and information systems and the extent to which management co-operates with the auditor. The corollary of this is that a high proportion of the accountancy bill represents the cost of preparing the basic accounts or, where they are prepared in-house, reformulating them in accordance with Companies Act requirements. In terms of reducing the cost burden, many respondents suggested therefore that it would be more appropriate to think in terms of reducing accounting requirements rather than abolishing the audit.

#### Accounting Requirements

- 2.23 The provisions of the Companies Act drawing a distinction between accounts prepared and accounts filed by small companies were introduced as a compromise measure following a consultation exercise prior to implementation of the Fourth EC Company Law Directive. The Directive introduced the concept of modified accounts for small and medium sized companies, permitting member states to allow them to produce abbreviated information both for circulation to shareholders and for publication (ie filing at CRO). Respondents to the Department's Green Paper 'Company Accounting and Disclosure' were split over the question of how far the UK should go in taking advantage of those provisions; the majority felt that shareholders had the right to continue to receive full information about the affairs of their company whilst small companies wanted to file less information in order to protect their competitive



position. Ministers took the line of trying to satisfy both these views by allowing small companies to file modified accounts, consisting of an abbreviated balance sheet and notes, but requiring them to continue to prepare full accounts for their shareholders.

- 2.24 This decision has received considerable criticism since the law first came into force in 1982. Small companies, particularly those which are shareholder-managed, have complained that far from easing their position, the provisions have in fact made them worse by requiring the preparation of two sets of accounts, thus increasing their accounting bills. Furthermore, they have argued that the full set of accounts for shareholders contains much detail which is irrelevant to their situation.
- 2.25 The consultative document therefore invited comments on the following questions:
- a) Should there be a relaxation of the accounting requirements for small companies in line with the provisions of the Fourth Directive?
  - b) Should a relaxation be made subject to shareholder approval?
  - c) Should relaxation be permitted for only a sub-category of shareholder-managed companies?
  - d) Are filed modified accounts as permitted at present adequate for their purpose?
  - e) Would relaxation of the accounting requirements result in a general lowering of the standard of the financial records kept by small companies?
  - f) How far should any relaxation go?

Should there be a relaxation?

- 2.26 The vast majority of respondents were strongly in favour of allowing small companies to produce one set of accounts both for circulation to shareholders and for filing. It was generally considered that there could be savings in time, effort and money if small companies were able to take full advantage of the Fourth Directive exemptions.
- 2.27 Those few who argued against relaxation suggested that not many small companies currently filed modified accounts, and used this as a basis for arguing that there is little real interest in simplification. Their main argument, however, as in 1980, was that shareholders would continue to want the detailed information currently provided; and that protecting shareholders' interests by giving them the right to demand fuller information would destroy the benefit of any relaxation. It was also suggested that the



existing requirements did not impose an undue burden on companies and that those who did not want to comply should reconsider their status as a limited liability company.

- 2.28 More significant objections came from the British Bankers' Association and the Inland Revenue. The banks saw little scope for simplifying accounting requirements and claimed that a significant reduction in the information available would give them difficulties in credit assessment. Revenue officials said that accounts which gave no more than the minimum information required by the Fourth Directive would not contain sufficient detail for their purposes. The Revenue could demand further information but the net result of their making specific inquiries, rather than receiving information automatically as part of the statutory accounts, would be to increase the overall burden on small companies. The Revenue's workload would also increase. At present, they investigate only a very small proportion of company accounts (1% a year producing a revenue yield of some £30m) but technical adjustments are made to the tax computations of an additional 22%. The Revenue believe that if they did not receive detailed information as at present these figures would almost certainly increase. They also believe that if full accounts were no longer available, they would find it much more difficult to identify those computations requiring investigation or adjustment and that operational efficiency and the revenue yield would suffer as a result.

#### Shareholder approval

- 2.29 One of the arguments against permitting the further relaxation available under the Directive is that it would lead to a significant loss of information to shareholders, but it was suggested in the consultative document that this could be overcome by making the decision to prepare only modified accounts subject to shareholder approval.
- 2.30 Most respondents did not comment on this point, suggesting that they thought the relaxation should be available to all small companies automatically. Those who did comment, however, were clear that if small companies were to be allowed to prepare only modified accounts, then the decision to do so should be taken by the shareholders. Most felt that the approval should be of 100% of shareholders, or 100% of all traceable shareholders but others thought that this would give too much power to minorities in the company and so suggested 90% or 'near unanimous' approval. A smaller number thought it would be sufficient simply to give individual shareholders the right to receive full information on request while some emphasised that individual shareholders should retain this right even if as a body they had voted for modified accounts. Some linked the question with the audit requirement, suggesting that companies which elected not to have an audit should be automatically entitled to prepare modified accounts for shareholders. Several thought the



decision from shareholders should be reviewed annually.

#### Restriction to shareholder-managed companies

- 2.31 Complaints about current accounting requirements for small companies have tended to come mainly from directors of shareholder-managed companies arguing that it is nonsensical for them to have to draw up a full set of statutory accounts in the required format when they can obtain all the information they need from their accounting records. However, while it was generally recognised that a relaxation of the accounting requirement would be of particular benefit to shareholder-managed companies, only a small minority of respondents felt that the relaxation should be limited to this group. The general view was that any decision to create a new sub-category of company would be arbitrary and that there were no good reasons for departing from the categories in the Fourth Directive.

#### Adequacy of filed modified accounts

- 2.32 Another criticism of the existing requirements is that in their present form modified accounts are too brief and uninformative comprising as they do, only an abbreviated balance sheet and notes to the accounts. The argument is that this, coupled with the fact that they do not have to be filed until 10 months after the year end, makes them virtually worthless to creditors and competitors.
- 2.33 There was considerable support for this view. A number of those against relaxation took the line that creditors and other users of accounts were no less entitled to full information than shareholders and that the facility for small companies to publish modified accounts should therefore be abolished. This view was in particular reflected by the credit agencies who suggested that companies filing modified accounts would generally be offered more restrictive credit terms than those who had not. However others, including the CBI, felt that creditors needed only a simple record of the company's financial structure and that modified accounts were sufficient for that purpose. These respondents did nonetheless place some emphasis on the importance of the filed modified accounts being audited.
- 2.34 Some accountancy firms felt that small companies appreciated the privacy afforded by the facility to put on the public record less information than they gave to their shareholders, but others felt their clients did not think the extra cost worth consideration. This quite marked divergence of views suggests that small companies are undoubtedly influenced in such matters by the view taken by their accountant.



### The influence of a relaxation on the standard of accounting records

2.35 The consultative document suggested that it was possible that a further relaxation of the statutory accounting rules for small companies could result in a lowering of the standard of the financial records kept by them. Most commentators who took up this point felt that there was no evidence to link the standard of book-keeping with statutory disclosure requirements; the general view was that the records kept were determined by the statutory requirement to keep accounting records and by what management believed to be useful to them in the running of the business. A number, however, emphasised that any reduction in the disclosure requirements should not be at the expense of the quality of accounting records. Others felt that any relaxation would lead to a decline in standards.

### How far should the relaxation go?

- 2.36 Under the Fourth Directive, the minimum requirements for prepared (as opposed to published) accounts are that they must contain a modified balance sheet, profit and loss account, and notes to the accounts. A directors' report is also required. The modified balance sheet essentially gives only the main headings (ie Tangible Assets, Intangible Assets) with no further breakdown, while in the profit and loss account a number of headings are combined with the result that details of turnover and gross profit margins need not be disclosed. The notes too may be abbreviated, omitting information on such items as the geographical breakdown of turnover, numbers of employees and directors' emoluments. Models of modified accounts prepared in Companies Act form are attached at Annex B.
- 2.37 Views on the extent to which any relaxation should go fell into three categories: those who felt the minimum allowed by the Directive was adequate; those who felt certain extra disclosures should be required; and those who felt the minimum itself was still too burdensome and that small companies should be allowed to prepare accounts in the way best suited to the nature of the business. This last line would, of course, require amendment of the Fourth Directive and indeed some respondents, notably the Institute of Directors, felt that the UK should take the initiative in demanding not only further relaxation of the requirements on preparation of accounts but also exemption from filing for small companies.
- 2.38 Some of those who felt that disclosure above the minimum was desirable pointed out that a number of requirements of the Companies Act derived from legislation which predated the Directive and suggested that these ought to be examined with a view to deciding whether or not disclosure was necessary in the interests of the members. Some gave



definite suggestions for the information which should be disclosed in the profit and loss account and notes. Most popular among these were information on directors' emoluments which, it was felt, was something shareholders had a right to know, and the company's turnover. However, even those who wanted extra disclosure felt that there was scope for eliminating some of the existing requirements. In particular, a number felt that the directors' report should be shortened by abolishing the requirement to show salaries of higher paid employees and political contributions.

- 2.39 The Law Society was happy with the minimum requirements for the profit and loss account but felt more detail should continue to be required in the balance sheet, for example, some breakdown for debtors, creditors and provisions.
- 2.40 A few commentators expressed concern about the requirement for modified accounts to give a true and fair view. The Directive requires the accounts of small companies to give a true and fair view and implies that they will still do so even if prepared in modified form. Although a number of respondents accepted this, it was also suggested that small companies should be specifically exempted from the true and fair view requirement if they opted for modified accounts. This, of course, would not be possible under the Directive.
- 2.41 One further suggestion was that small companies which were wholly-owned subsidiaries should be entirely exempt from the preparation of accounts provided certain conditions, such as the parent guaranteeing their debts, were met. This is in fact an option under the Seventh Directive on consolidated accounts and is covered by the consultative document dealing with that. Accordingly, it is not taken any further here.
- 2.42 Another issue which attracted much comment was the application of accounting standards to small companies. Many people considered that standards are more burdensome than statutory requirements. In particular, SSAP10, which calls for a statement of source and application of funds from all companies with a turnover above £25,000 came in for criticism. Government was urged to pursue this matter with the accountancy profession. In fact as a result of this exercise and work previously carried out by Professor Bryan Carsberg, the Accounting Standards Committee has already decided to review the application of standards to small companies.

### 3 ANALYSIS

- 3.1 There are between 300,000-400,000 active small independent companies on the register. We can only guess at what they pay in audit fees but small company accounting bills range from a few hundred pounds to £2-3,000 and above. Even if pure audit costs are no more than 10% of the total, the



gross cost adds up to some £60-80 million. If one also includes the opportunity cost of management time spent with the auditor, the total figure rises to over £100 million.

- 3.2 This is a significant sum and it is right to consider whether it is being spent to the best advantage both from the company's point of view and that of society as a whole. We do not believe, however, that the abolition or relaxation of present audit requirements can be justified on cost grounds alone. An annual bill for £200 is obviously significant but the evidence from this consultation and recent academic research suggests that small companies do not regard the audit as a burden in that sense. Only 4% of the companies sampled by Carsberg, for example, saw financial reporting as a major problem and company law requirements ranked well down the list of burdens perceived by participants in the Burdens on Business study. The real question is whether the value derived from the audit is worth the cost involved and whether, if it is retained, the return can be increased, particularly so far as companies themselves are concerned.
- 3.3 The case for abolition is strongest in relation to the value of the audit to management and shareholders. It rests on the proposition that there is no justification for imposing on them a requirement to purchase a service they neither need or want. The rights of minority shareholders obviously need to be protected. But provided that protection is wholly adequate - and in practice that probably means giving each individual shareholder the right to require an audit - there seems to be no reason in principle why shareholders should not be allowed to dispense with the audit where they consider it in the best interests of the company to do so. Equally, whatever the rights and wrongs of the arguments about the value of audited information - and a priori it is difficult to believe that financial statements prepared six or more months after the end of the financial year contribute significantly to management decisions - if management consider that it is not cost effective then they should be free to do away with it.
- 3.4 The survey evidence suggests that if they were given the choice most companies would retain the audit for external reasons, primarily to satisfy the Revenue, the banks and other sources of finance. But even if only a minority of companies did take advantage of abolition, that in itself is no good reason for retaining the present statutory requirement. The minority would still constitute a significant number of companies which otherwise would continue to be penalised for the benefit of others. Moreover, those companies which continued to commission audits would be able to tailor the auditing process to their own particular needs.
- 3.5 The weakness of these arguments is that they discount the possible consequences for third parties. On the face of it, it seems unlikely that these would be as dire as those



foreseen by the banks, the credit organisations and other anti-abolitionists. Third parties would be in no worse a position than they are in when dealing with unincorporated firms with no published accounts or companies in breach of their filing obligations. Some companies may choose not to trade with such businesses but there is no evidence to suggest that they experience insuperable difficulties in obtaining finance or trade credit. It is clear, however, from the consultation that the banks and, more especially, trade creditors do attach substantial importance to the accounts being audited since this provides some assurance about the quality of the financial information they contain. The fact that the audit requirement is universal is particularly important to them. Given the extent of inter-trading between small companies, many consider audit fees well worth paying for just that reason; as one commented, bad debts are a far greater burden than any audit.

- 3.6 To the extent that companies chose to retain the audit, abolition would obviously cause third parties no difficulties. For the rest, some companies could be expected to produce accounts which met all the market's needs. There is a real risk, however, that others would abuse the freedom given to them, either deliberately or out of ignorance. The problem is that given the fact of their limited liability the consequences of any abuse would be felt primarily by others. The banks and other large creditors could protect themselves by taking more security, increasing their charges or commissioning their own independent audits at borrowers' expense. Similarly, the Revenue and Customs & Excise could seek to limit the extent of tax evasion by carrying out their own investigations, though this would obviously have resource implications and involve transferring any burden created by the audit requirement from those companies to HMG. Unsecured creditors, however, would have to choose between not trading with such companies or carrying the risks involved on their own shoulders.
- 3.7 The case against abolition rests on the view that the audit requirement provides a basic measure of protection for third parties. It operates at two different levels. The argument of principle is that small businesses already have a fundamental right of choice in that they can choose to trade as limited liability companies or in some other form. Having exercised that choice and opted for the privileges of limited liability, they should then accept the obligations that go with it, including the obligation to make available via the audit financial information on which the public can rely. They should not be given the benefits and then allowed the further choice of not paying for them. The argument of practice is that abolition would give companies a licence to abuse limited liability at others' expense and by removing the discipline of the audit would lead to a general lowering in the standard of accounting records which would do nobody, least of all small companies themselves, any good.



- 3.8 There is no means of knowing how far abolition of the audit requirement would constitute a rogue's charter. Some respondents were convinced that it would lead inexorably to increased fraud and tax evasion and the expansion of the black economy. But, others doubted whether the audit was an effective mechanism for detecting fraud in small companies and it is plainly not sufficient in itself to prevent financial irresponsibility. That does not mean, however, that it has no deterrent effect. Moreover, what is clear from the consultation is that abolition of the requirement would be seen as a step in the direction of lower financial and commercial standards. It is also clear that for that reason it would be criticised as wholly inconsistent with Government policies to encourage private investment in the small business sector; with the provisions of the Insolvency Act bearing on directors' responsibilities and wrongful trading; and with the general fight against commercial fraud. Ministers would be presented as bolting the back door of the stable whilst throwing the front door wide open.
- 3.9 In the final analysis, the balance of the argument turns on the likely effects of abolition on companies' financial management and the reliability of their accounting records. Proper accounting procedures are an essential requirement of business and, in our view, abolition could not be justified if, as a result, the quality of financial reporting was significantly reduced. It is arguable that if companies wish to manage their financial affairs in a way which jeopardises their own future, then provided they accept the possible consequences they should be allowed the freedom to do so. But this ignores the possible consequences for third parties, and particularly those who are unable to protect themselves. We also believe that the benefit derived from making all companies subject to common standards and procedures outweigh the cost penalties imposed on those companies capable of satisfying those standards without the need for an independent audit.
- 3.10 Having defined the critical question, we find there is no way in which, on the basis of the consultation, we can give a definitive answer to it. There is no consensus for change and nothing more than conflicting views on what the consequences of abolition might be. Since weaknesses in their financial management are evident and widespread, it is clear that the audit requirement in itself does not guarantee that small companies have proper financial systems. But equally experience suggests that many small companies would not implement such systems without the involvement of a professional accountant and that they cannot be relied on to take professional advice unless they are compelled in some way to do so. Experience also suggests that the companies least likely to seek advice or those most in need of it.
- 3.11 It is this uncertainty about the effects of abolition which led many pro-abolitionists to suggest that it should be coupled with the introduction of an alternative requirement



providing some assurance as to the credibility of companies' published accounts and the quality of their basic accounting records. Three possible approaches were proposed. These would involve:

(a) underlining directors' existing statutory responsibilities for accounts by requiring them to sign a statement certifying that the accounts had been properly prepared in accordance with Companies Act requirements. The English Institute favoured this approach and produced a draft statement which is attached at Annex C;

(b) going one step further than (a) by making directors personally liable for any losses incurred by third parties in the event of their making such a statement without reasonable grounds for doing so;

(c) requiring an independent qualified accountant to be involved in the preparation of the accounts and to certify that, in his opinion, they comply with Companies Act requirements. The Scottish Institute was the main supporter of this approach and provided a draft statement which is attached at Annex D.

In addition, the consultative document put forward the option of following practice in other countries, particularly the United States, and requiring an independent review of the accounts as opposed to an audit.

- 3.12 The consultation revealed virtually no support for the review. It was seen by pro and anti-abolitionists alike as an unacceptable halfway house which would cost much the same as an audit whilst giving the users of accounts no more than a negative assurance as to their reliability. The accountancy profession as a whole was also concerned that the basic difference between a review, which does not involve the independent verification of information supplied by the client company, and the audit would not be appreciated and that in consequence people would place more reliance on a review than it actually offers. Given this almost unanimous response, we see no point in pursuing the review option any further.
- 3.13 As regards the alternatives, we have discussed options (a) and (c) with the English and Scottish Institutes. In essence, they are very similar. In both cases the basic idea is that a professional accountant should examine the accounts and satisfy himself that they are presented in the right form and that the assumptions on which they rest are soundly based. This would not involve the cross-checking and detailed investigation which is carried out as part of the audit but if he were to do the job properly the accountant concerned would need to probe any figures which he considered questionable. The deeper he probed, the more like an audit the process would become.
- 3.14 The Scots approach would provide a greater measure of assurance in that it would require this process of



examination to be carried out by an independent qualified accountant. It would also ensure that small companies took professional accountancy advice at least once a year, though the extent to which they benefitted from this would depend on the quality both of the accountant concerned and of his relationship with his client. The main problem with it is that in appearance at least it would be not much different to the present audit requirement. The cost should be less because the reporting accountant would be taking a lesser responsibility but it might well be criticised as change for change's sake. The English Institute approach is more deregulatory in appearance but it rests on the assumption that no responsible director would sign the relevant statement without taking professional accountancy advice. To the extent that such advice was taken, the cost would be much the same as if the accountant had made the statement on his own account, but since his involvement would not be apparent third parties would tend to discount the value of the assurance given. To the extent that they did not, its worth would be even more open to question. That objection would be met at least partially if directors were made personally liable for subsequent losses. Such an approach would be consistent with that adopted in the Insolvency Act but small businessmen might well regard it as more burdensome than the audit requirement and, in any case, it raises issues which go beyond the scope of this exercise.

- 3.15 We do not find either of these alternative approaches attractive. Neither could be introduced without a great deal of further work both on refining the concepts involved and the precise nature of the assurance given, and in terms of developing appropriate operational procedures and professional guidance. The accountancy profession would also need to put its full weight behind the initiative since otherwise there would inevitably be scope for wide differences in interpretation. Equally, the Scottish option in particular is open to the same objections as the review in that people could easily place more reliance on the accountant's report than it actually offered. More important, we do not believe there is any sensible half-way house between the status quo and abolition of the audit requirement. If company law is to give third parties some basic form of assurance about the quality of a company's accounts, the full audit is the most cost-effective option. Politically, any alternative would also be difficult to present in a positive light. Substituting one requirement for another would look indecisive and might well attract criticism from pro and anti-abolitionists alike. But against that, abolishing the audit requirement without putting anything in its place would fly in the face of most of the comments made in the consultation.

#### Accounting Requirements

- 3.16 The decision in 1981 to allow companies to file modified accounts was based on the judgment that the interests of



third parties would not be seriously impaired if companies filed less information. This view was challenged at the time and some still regard it as mistaken. But small companies themselves generally appear to value the facility and about a third currently file accounts in modified form. What they do find burdensome, however, is the additional cost involved in producing different sets of accounts for shareholders and for filing purposes. We think their complaints about this are well justified and that the objective should be to put small companies in a position where they are able to produce one set of accounts which can be used for both purposes.

- 3.17 One way of achieving this would be to require companies to prepare and file a set of accounts fuller than those currently filed but less detailed than those now prepared for shareholders. We think it likely, however, that small companies would oppose this on the grounds that it both imposed an additional burden, psychologically if not physically, and went back on the original aim of enabling them to keep certain information from competitors.
- 3.18 If this approach is ruled out, the only way of achieving the objective is to give companies the option of reducing the amount of information they provide to shareholders. In principle, this approach is attractive: if shareholders are content to receive less information, then they should be allowed to do so. However, the accounts prepared for shareholders are also used by third parties, and particularly by the Inland Revenue. If, as Revenue officials told us, reducing the amount of information in shareholders' accounts would simply mean that small companies would be subjected to a greater number of requests for information from tax inspectors, then the overall burden on small companies would not be reduced and might well be increased.
- 3.19 However, companies already provide the Revenue with a considerable amount of additional information over and above that produced for shareholders. We could, therefore, reduce Companies Act requirements and leave the Revenue to specify any additional information they required in the same way. This would reflect the long established position in the UK whereby disclosure requirements are in no way influenced by the requirements of the tax authorities, unlike many other countries where the two are inextricably linked. Company law disclosure requirements would be placed on a more logical footing, but there might still be resource implications for the Revenue as a result of the information in the new schedule no longer being audited. If changes in Companies Act requirements were coupled with abolition of the audit requirement, the implications for Revenue procedures and manpower - and the revenue yield - would be correspondingly greater.
- 3.20 We doubt that any change in present accounting rules will produce any substantial saving in accounting costs. Even if the Revenue did not demand extra information, the



difference in cost between preparing full and modified accounts would be very small because of the need to assemble the detailed information before making the modifications. The main saving would derive from there being no need to prepare separate accounts for filing purposes but the best estimate we can get is that this would represent no more than £100-200 at most. Nonetheless, given the large majority in favour of a relaxation, a decision to do nothing would certainly be subject to criticism, no matter how persuasive the arguments of the Inland Revenue may be.

- 3.21 If the requirements were relaxed, we consider that it would be important to ensure that shareholders' interests were full protected and that a reduction in disclosure was not achieved at the expense of the standards of accounting records. The first point could be resolved by taking steps to ensure that shareholders could receive fuller information if they wanted it. This could be done either by requiring a resolution of the shareholders before a company could take advantage of the relaxation or by giving individual shareholders a specific statutory right to receive full information on demand, or a combination of these two.
- 3.22 Individual shareholders already have the right to demand more information of the directors at a company's general meeting, but it is often suggested that in practice it is very difficult for them to exercise that right. A specific provision enabling any shareholder to receive on request any information which would otherwise have been included in the full accounts would certainly resolve that problem though to the extent that it resulted in companies receiving ad hoc requests it might be regarded as simply replacing one burden with another. If, however, companies were keeping proper accounting records the provision of any such information should present at least no greater effort than is currently involved in producing full accounts. The alternative would be to make a decision to produce modified accounts for shareholders subject to unanimous approval by shareholders or approval by a specified majority, say 90% or 95%. We do not favour this approach. A 100% requirement would put too much power in the hands of an individual shareholder whilst any lesser requirement would open up the possibility of abuse. The right course, it seems to us, is to give shareholders the right to receive information and leave the onus on them to use that right as and when they consider it necessary to do so.
- 3.23 The question of maintaining the standard of accounting records is more difficult to resolve. It is essential that accounting records should not suffer as a result of any relaxation of statutory disclosure rules, but present requirements on the maintenance of accounting records would be very difficult to enforce without the involvement of a professional accountant in the business. This reinforces the case for retaining the audit requirement.



- 3.24 The question of how far the relaxation should go raises its own difficulties. One approach would be to adopt the maximum exemptions permitted under the Fourth Directive but there is a case for requiring certain extra information, in particular details of turnover and directors' emoluments which are of particular interest to shareholders. In addition, there are requirements in the Companies Act which have no connection with the Directive, for example, the disclosure requirements of the directors' report relating to such subjects as political contributions. On the face of it, there seems little scope for eliminating any of those requirements in relation to small companies alone, but it should be noted that many do not in practice apply to small companies.
- 3.25 Further work needs to be done in order to establish precisely how far present requirements should be cut back. In principle, however, there would seem to be little problem in asking for information above the minimum in the profit and loss account and directors' report, since they do not have to be filed, nor would it be very onerous to require certain extra information in the notes for shareholders, for example, on directors' emoluments and turnover. It could be argued though that if shareholders are to have the right to demand extra information, then companies should be allowed to take maximum advantage of the exemptions and left to supply the extra as necessary. However, it might well be less trouble and cheaper in the long run to require disclosure of such additional items as directors' emoluments rather than subject companies to the possibility of repeated requests for the same information.

#### 4 RELATED ISSUES

##### The Corporate Form

- 4.1 One of the features of the consultation was the number of responses which questioned the general suitability of present forms of incorporation so far as most small firms are concerned. Organisations representing small firms, the CBI, the English Institute and individual accountants all took the line that to look at accounting and audit requirements in isolation was to look at symptoms rather than causes. Those in favour of change considered that whilst it would be of some marginal benefit, what was really required was a new form of incorporation which relieved small companies of many of their existing Companies Act obligations. Those opposed to change believed that in focussing on accounting and audit requirements the burdens exercise was shooting at the wrong target and that what would really help small companies was action both to discourage incorporation and encourage disincorporation. According to this group, there is nothing illogical in small limited liability companies being subject to the same requirements as larger companies; that is a function not of their size but of their limited liability status. What is illogical is that they should



have that status in the first place and should effectively be prevented by the tax structure from shedding it when otherwise it would be in their best interests to do so.

- 4.2 Officials in this Department have recently considered whether there is a case for commissioning a further study of possible new forms of incorporation for small firms (a Green Paper issued in 1981 revealed a wide range of opinions but no agreement on the need for change or the form it should take) and measures to facilitate disincorporation. They concluded that there would be no advantage in doing so, at least for the time being. Although a simpler regime would have some benefits for small companies, it is far from certain that, if faced with the choice, they would want to change their present status, particularly if change meant the loss of, or a partial reduction in, their limited liability. They also felt that any study was best left until current work aimed at reducing the amount of information companies are required to file at the Companies Registration Offices is complete and something is known about the practical effects of the provisions in the Insolvency Act dealing with wrongful trading and the disqualification of directors.
- 4.3 The CRO exercise is clearly directly relevant to any future work in this area but we believe the points made by consultees should not be lost sight of in announcing Ministers' decisions on accounting and audit requirements. Even substantial changes may well be presented by some members of the small firms lobby as little more than cosmetic whilst those opposed to change, particularly as regards the audit requirement, are likely to regard them as the wrong solution to the wrong problem. In either cases, there may be advantage in indicating that Ministers are considering the scope for further work on new forms of incorporation and disincorporation.

#### Rules on Filing of Accounts

- 4.4 Section 242 of the Companies Act gives private companies 10 months in which to file their accounts starting from the end of the relevant accounting period. Public companies are allowed 7 months. Many respondents considered these periods too long and believed that published accounts would be more useful all round if they were produced and filed more promptly. Respondents generally considered that the rules on filing should also be more strictly enforced.
- 4.5 Action to improve compliance levels is already in hand. As regards the period allowed for filing, any change in the present rules would effectively put an additional burden on companies generally. But we think that factor is outweighed by the advantages to be derived from quicker filing and that action to achieve it would be a logical part of any package amending present rules on accounting and audit. Some respondents suggested that all companies, public and private, should be required to file within 3



months of their year end. We think that would impose too great a burden on companies and accountants alike: a 6 month deadline applied to all companies seems to us to strike the right balance. This is a point which should be considered further in the current market research survey of the requirements of those using the search facilities at the Companies Registration Offices.

## 5 CONCLUSIONS

### Nature of Changes

- 5.1 On accounting requirements there is a clear majority for relaxation. The major objector is the Inland Revenue. Given their comments, it is possible that any relaxation of the statutory disclosure requirements would not in practice result in any net reduction in the amount of information required from small companies. There might be some reduction in costs but this is likely to be small. The indications are, however, that the current disclosure requirements of the Companies Acts are seen by small businesses as burdensome and that some relaxation would have a psychologically beneficial effect, if not a physical one. On balance, therefore, we would favour a relaxation of the requirements in line with the Fourth Directive subject to the possibility of certain extra disclosures. This should be accompanied by a provision giving shareholders' a specific right to demand further specified information, eg that which would be included in full accounts. With a view to making published information available on a more timely basis, we also consider that the rules on filing should be reviewed in the light of the user survey.
- 5.2 On the audit requirement there is no consensus and no single factor which sways the balance of the argument for or against change. The consultation process has created an expectation in some quarters that the audit requirement will be abolished. A decision to leave things as they are will disappoint those people and may be used as a basis for querying the Government's commitment to the general principle of deregulation. But Ministers will be just as heavily criticised if they go for abolition, particularly on the grounds that the decision is inconsistent with the policy of cracking down on commercial fraud.
- 5.3 We do not find any of the suggested alternatives to the audit requirement attractive. The Scottish Institute's approach would effectively reintroduce the audit requirement under another name. The English Institute's approach is more deregulatory in appearance but in substance little different. Neither could be introduced without a great deal of further work, both on the concepts involved and in terms of educating both individual accountants and potential clients.
- 5.4 If the audit requirement is abolished, the rights of

minority shareholders should be protected by making a decision to dispense with an audit subject to the unanimous approval of shareholders voting in general meeting. The decision should be subject to annual confirmation.

#### Scope of Changes

5.5 We believe that any changes in accounting and audit requirements should apply to small companies generally, not just to shareholder managed companies. Provided the interests of minority shareholders are adequately protected, there is no reason to distinguish between different sorts of small company. And as a matter of general policy, it is desirable to avoid complicating company law by creating another separate class of company.

5.6 For Companies Act purposes, a company is deemed to be small or medium sized in a financial year if in that year two or more of the following conditions are satisfied:

(i) turnover does not exceed £1.4 million (£5.75 million for medium sized companies);

(ii) its balance sheet total is not more than £700,000 (£2.8 million);

(iii) the average number of persons employed by the company in the year in question does not exceed 50 (250).

A recent EC directive gives member states the freedom to raise the turnover and balance sheet thresholds for small companies to £2 million and £975,000 respectively. The equivalent figures for medium sized companies are £8 million and £3.9 million.

5.7 If the audit requirement is retained, we believe that the UK should take full advantage of these increases and amend the Companies Act definition accordingly. If, however, the audit requirement goes, there is an argument for using the thresholds to limit the extent of abolition on the grounds that a company with turnover of £1.4 million is far from being a 'small company' for trading purposes. Even if it only applied to companies with an annual turnover of less than £250,000, over two-thirds of all the companies on the register would still benefit. Whatever the decision on this point, the thresholds for medium sized companies should be increased in line with the directive.

Companies Division  
Department of Trade and Industry  
January 1986



## ANNEX A

### VIEWS OF SMALL COMPANIES AND THEIR REPRESENTATIVE ORGANISATIONS

1. Sixty-three responses were received from small companies or organisations representing their interests, whether trade associations, chambers of commerce, or broader groupings like the CBI, the National Chamber of Trade and the Association of Independent Businesses. Thirty-nine of these favoured abolition of the audit requirement, at least for shareholder-managed companies; 24 were against. The 15 respondents who commented on accounting requirements all supported relaxing the present rules to the maximum extent permitted by the Fourth Directive.

2. The membership of the National Chamber of Trade was divided. Some saw good reason for the audit requirement to be retained whilst advocating relaxation of the rules on accounts. Others fully supported the idea of removing the audit requirement but wondered whether there would be any saving if they had to produce the same sort of information for the Inland Revenue. What was significant was that the Chamber saw any changes in accounting and audit requirements as marginal in terms of relieving burdens on small companies and argued instead for more fundamental action via the introduction of a new form of incorporation; two-thirds of its response was given over to this topic. Similarly, the Institute of Chartered Secretaries and Administrators (ICSA) saw a new form of incorporation as the real solution to small companies' problem, though it favoured both abolition of the audit requirement for shareholder managed companies and simplifying accounting requirements to the maximum extent possible.

3. The Association of Independent Businesses saw advantages and disadvantages in an audit requirement which on the one hand could be 'invaluable' and on the other was 'frequently superfluous'. It came down in favour of abolition but felt the involvement of an independent accountant in companies' affairs to be desirable at all times. It concluded therefore that the audit requirement should be replaced by rules governing the preparation of accounts on the lines suggested by the Institute of Chartered Accountants of Scotland. The CBI Small Firms Council was clear that there should be an option for small companies to adopt a less burdensome form of annual financial reporting but the majority favoured retaining the audit requirement and focussing attention instead on reducing and simplifying the content of accounts and balance sheets. Like the National Chamber and ICSA, however, it regarded changes in accounting and audit requirements as incidental to the main problem which it saw as reducing the number of incorporated businesses. In contrast, with one exception, members of The Association of British Chambers of Commerce were unanimous that the audit should be retained. They considered that present requirements 'got the balance of cost and benefit more or less right' and that the fact that they imposed 'chores and financial costs which in an individual case it would have been safe to



avoid' did not justify 'any general relaxation of the regulation of small companies in this area'.

4. Those small companies who argued for abolition regarded the cost of the audit as out of all proportion to the value derived from it. According to them, audited accounts are 'just so much waste paper', irrelevant to management needs and of no benefit to potential creditors, Dancon Insulations Ltd, a firm in West Yorkshire, spoke for this group in presenting the audit requirement as 'a great hindrance to small businesses. Large fees have to be paid for the production of accounts in a form which is determined by a profession totally out of touch with the requirements of the businessmen. The routine adopted by ourselves and by others of our acquaintance is to let the auditors get on with it and [then] produce our own figures to assess the progress of the business'. Kenton Display Ltd similarly thought audit 'a total waste of money and effort' and commented that small companies would be better off if accountants spent less time auditing and concentrated more on giving them financial guidance. The responses did not suggest, however, that many small firms would buy in professional accountancy advice if the audit requirement were abolished. This point worried even pro-abolitionists who produced various alternative suggestions for maintaining the quality of accounts and accounting records. These ranged from Government action to encourage businesses to prepare management accounts (the Durham Small Business Club) to financial penalties for producing false or misleading accounts with loss of limited liability if accounts were not filed on time (K S Paul Ltd). Some companies also considered that abolition should be limited to very small companies with annual turnovers of £500,000 or even £250,000.

5. By contrast, those small companies opposed to abolition saw the cost of an audit as insignificant in relation to the benefits derived from it. Benefit was defined, however, primarily in terms of companies' interests as potential creditors of other small businesses rather than in terms of the use made of the audit for internal management purposes. Greenup & Thompson Ltd, for example, thought that 'companies such as ourselves would be much more nervous about trading with small companies if the audit requirements were relaxed', whilst Abbey Quilting Ltd thought abolition would be 'very little short of disastrous' for trade creditors. Underlying this view was the belief that audit fees were a small price to pay for the benefits of limited liability and that abolition would lead to 'corporate anarchy'. Thus, Greenups believed that 'any respectably run business should expect its financial affairs to be audited annually [and that] only disreputable and dishonest managers would welcome a relaxation'. Members of the British Printing Industries Federation saw it as a recipe for a 'fiddler's paradise'. Others were concerned about the practical effects of abolition on their relationship with the banks and, more particularly, the Inland Revenue and Customs & Excise.

6. Those companies which commented on accounting requirements mainly complained about the additional burden involved in producing one set of accounts for filing and another for



shareholders. The general view seemed to be that the introduction of modified accounts had made reporting 'more complicated and costly' and that what was required was a return to a position where one set of accounts satisfied both purposes. Beyond this general prescription, few views were expressed on the form simplification should take. At the general level, the suggestion was that the format of small company accounts should be made appropriate to the size and nature of the business and that their content should be related more closely to management needs. At a more detailed level, this became a call for a simple balance sheet and profit and loss account, minimal notes, a general relaxation of accounting standards and the scrapping of the directors' report.

Good Practice Limited  
**Modified balance sheet**  
 at December 31, 19X1

Annex B.

	Notes	19X1 £	19X0 £
<b>Fixed assets</b>			
Tangible assets		96,510	73,110
Investments		11,250	13,625
		107,760	86,735
<b>Current assets</b>			
Stocks	48,250		45,000
Debtors	62,500		52,500
Cash at bank and in hand	17,887		12,012
	126,637		109,512
Creditors: amounts falling due within one year	101,787		97,667
<b>Net current assets</b>		24,850	11,845
<b>Total assets less current liabilities</b>		132,610	98,580
Creditors: amounts falling due after more than one year	2	(15,000)	(17,500)
Provision for liabilities and charges		(1,045)	(1,340)
Accruals and deferred income		(7,000)	(4,000)
		£109,565	£75,740
<b>Capital and reserves</b>			
Called up share capital	3	43,750	37,500
Share premium account		5,000	2,500
Revaluation reserve		12,500	—
Profit and loss account		48,315	35,740
		£109,565	£75,740

In preparing these modified accounts:

- (a) we have relied upon the exemptions for individual accounts under Section 5 of the Companies Act 1981.
- (b) we have done so on the grounds that the company is entitled to the benefit of those exemptions as a small company.

J.N. Smith *Director*  
 J. Archer *Director*  
 June 25, 19X2

The notes on pages 98 to 99 form part of these modified accounts



Good Practice Limited  
**Modified profit and loss account**  
at December 31, 19X1

	Notes	19X1	19X0
		£	£
Gross profit		236,175	205,930
Staff costs			
Wages & salaries	109,355		98,670
Social security costs	21,520		19,230
Other pension costs	3,500		3,100
		134,375	121,000
		101,800	84,930
Depreciation		11,125	9,750
		90,675	75,180
Other operating charges		64,750	64,780
Operating profit		25,925	10,400
Income from investments		1,250	1,000
		27,175	11,400
Interest payable		1,400	1,400
Profit on ordinary activities before taxation		25,775	10,000
Tax on profit on ordinary activities		7,015	4,000
Profit on ordinary activities after taxation		18,760	6,000
Extraordinary charge	4,685		—
Tax on extraordinary charge	2,435		—
		2,250	—
Profit for the financial year		16,510	6,000
Dividends		3,935	3,680
		12,575	2,320
Retained profit brought forward		35,740	33,420
Retained profit carried forward		£48,315	£35,740

The notes on pages 00 to 00 form part of these modified accounts

Good Practice Limited  
**Notes to the modified accounts**  
at December 31, 19X1

**1. Accounting policies**

**Accounting convention**

The accounts are prepared under the historical cost convention, modified to include the revaluation of freehold land and buildings.

**Depreciation**

Depreciation is provided on all tangible fixed assets, other than freehold land, at rates calculated to write off the cost or valuation, less estimated residual value, of each asset evenly over its expected useful life, as follows:

Freehold buildings	—over 50 years
Leasehold land and buildings	— over the lease term
Plant and machinery	—over 5 to 15 years

**Deferred government grants**

Government grants on capital expenditure are credited to a deferral account and are released to revenue over the expected useful life of the relevant asset by equal annual amounts.

Grants of a revenue nature are credited to income in the period to which they relate.

**Stocks**

Stocks are stated at the lower of cost and net realisable value as follows:

Cost incurred in bringing each product to its present location and condition:

Raw materials	— purchase cost on a first-in, first-out basis
Work-in-progress and finished goods	— cost of direct materials and labour plus attributable overheads based on the normal level of activity.

Net realisable value is based on estimated selling price less further costs expected to be incurred to completion and disposal.

Long term contract work-in-progress is stated at cost (as defined above) plus attributable profits, estimated to be earned to date based on the stage of completion, less provision for any known or anticipated losses, and payments on account received and receivable.

**Research and development**

Research and development expenditure is written off as incurred.

**Deferred taxation**

Deferred taxation is provided on the liability method on all short term timing differences. Provision is also made for long term timing differences, except for those which are not expected to reverse in the future.

**Foreign currencies**

Assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the balance sheet date.

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction.

All differences are taken to the profit and loss account.



## 2. Bank loan

The long term bank loan bears interest at 8% per annum and is repayable in annual instalments of £2,500 commencing October 31, 19X2.

	19X1	19X0
	£	£
Amounts repayable within five years	12,500	10,000
Amounts repayable after five years	5,000	7,500
	£17,500	£17,500

The current portion of the loan amounting to £2,500 is shown in current liabilities.  
The loan is secured on the freehold property.

## 3. Share capital

	Authorised		Allotted, issued and fully paid	
	19X1 No.	19X0 No.	19X1 £	19X0 £
Ordinary shares of £1 each	50,000	37,500	31,250	25,000
10% (now 7% plus tax credit) preference shares of £1 each	12,500	12,500	12,500	12,500
	62,500	50,000	£43,750	£37,500

During the year 6,250 ordinary shares of £1 each, with an aggregate nominal value of £6,250, were issued fully paid for cash of £8,750 to help finance the purchase of plant and machinery.

## 4. Debtors

Included in debtors is a quasi-loan to a director, J. Archer. It is an interest free season ticket loan repayable in monthly instalments.

	19X1	19X0
Amount outstanding at end of the year	£850	£820
Maximum outstanding during the year	£910	£800

ANNEX C

Draft Statement by Directors as proposed by the Institute of Chartered Accountants in England and Wales

The statement would be signed by all the directors, acknowledge their responsibility for the accounts and state in particular that:

- (a) they are entitled to rely on sections        to        of the Companies Act        which permit unaudited accounts to be laid before the members in general meeting and to be delivered to the Registrar of Companies in the format prescribed for small companies;
- (b) the accounts have been prepared from the company's accounting records so as to be in accordance with schedule        of the Companies Act        ;
- (c) for the year ended        the company's accounting records have been kept in accordance with section 221 of the Companies Act 1985, and in particular include all its transactions;
- (d) the accounts were prepared to give a true and fair view and in particular, all reasonable steps have been taken before the accounts were made up to:-
  - (i) ensure that all known bad debts have been written off and that adequate provision has been made for doubtful debts;
  - (ii) ascertain the stocks and work in progress;
  - (iii) include all assets and liabilities, other than those of a contingent nature which are shown in note        ;
  - (iv) value the assets and liabilities in accordance with the accounting principles and valuation rules set out in Part II of Schedule 4 to the Companies Act 1985.

Making the statement recklessly would be an offence.



ANNEX D

Draft Statement by Reporting Accountant as Proposed by Institute  
of Chartered Accountants of Scotland

"ACCOUNTANT'S REPORT TO THE MEMBERS OF .... LIMITED

The financial statements on pages to have been prepared (by me) from the company's accounting records and other information supplied by the directors.

On the basis of the information supplied to me by the directors the company is, in my opinion, a small owner-managed company as defined in Section .... of the Companies Act 1985 and the members have resolved that no audit is required, as permitted by Section .... of that Act.

I have not carried out an audit and thus restrict my opinion to report that on the basis of the information supplied to me by the directors the form of presentation of the financial statements, which are in accordance with the accounting records, and the accounting policies adopted are consistent with the requirements of the Companies Act 1985."

CCBG



DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
LONDON SW1H 0ET

TELEPHONE DIRECT LINE 01-215 5422  
SWITCHBOARD 01-215 7877

Secretary of State for Trade and Industry

5 November 1985

The Lord Young of Graffham PC  
Secretary of State for Employment  
Department of Employment  
Caxton House  
LONDON  
SW1H 9NF

NBPM

D Davis,

**GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES**

Thank you for sending me a copy of your recent minute to the Prime Minister in which you enlarged on the proposals contained in your previous minute of 16 September.

I welcome your proposals as a constructive means of helping in the provision of support and advice to small businesses. I note that the scheme will be administered by your new Regional Enterprise Units which will be taking over a role which it was originally intended should be undertaken by the DTI's Regional Directors. I am sure the units will provide an admirable means of drawing together the various threads of assistance to the small business sector. I do hope however that in doing so they will not overlook the broader economic picture, and that they will work closely with my Regional Directors as well as with the various bodies referred to in paragraph 7 of the note attached to your minute in helping to co-ordinate the Government's activities over the whole range of assistance to industry.

I am copying this letter to the Prime Minister, members of EA, John Moore, and Sir Robert Armstrong.

*Handwritten signature/initials*

LEON BRITTAN

DW1AAI



Econ Pol: Small Firms

Pt 6



Briefing provided to Lord Young.

Secretary of State

#### SUPPORT FOR LEAs

Bull points to make;

- E(A) agreed the principle on 15 May. Your remit was to go away and "consider further what minimum level of government support will be needed to establish viable agencies in areas where the local resources of finance and entrepreneurship have found to be inadequate".
- You have now done this and have agreed the funding with the Treasury.
- the current package is the best you can get
  - the richer agencies will not qualify (only about 180 out of 300 will) and these will need to provide a good business plan.
  - money will be levered out of the private sector by the principle of matching funds and public support will be phased out over a 5 year period
- the current line being taken by the Policy Unit is mischievous. They were on MISC 108 and signed up to the package like everyone else without dissent. Their idea of using BES is a nonsense
  - LEAs are not equity based companies and their sponsors would not qualify for BES relief
  - LEA sponsors already get tax relief on their support
  - their further idea of privatising LEAs is also a non starter. They are not profit making and that is one of the reasons why private sector companies put time, money and people into them. Profit making bodies would ~~be less~~ not likely to attract such sponsors.
- the need to give the LEA movement a clear signal that it has a long term future is now urgent



Poive Minister 2

CF  
B/F for  
meeting with Lord  
Young please. Please  
PRIME MINISTER  
tell DEMP that this will  
be on the agenda.

DLW  
28/10

I suggest you discuss this at your  
next bilateral with Lord Young, rather than  
on 7 November. That meeting ought to be  
more strategic.

23 October 1985

DLW  
24/10.

Yes  
m

LOCAL ENTERPRISE AGENCIES

If we understand David Young's plan correctly, it would have the following effect:

- Enterprise Agency A is highly successful, and has a private sector income of £100,000 pa. It therefore receives no Government support.
- Enterprise Agency B is lousy, and has total non-Governmental revenue of only £40,000, of which £20,000 comes from the local authority. But it hires a good consultant to produce a plausible 'business-plan', sufficient to dupe the overworked Principal running the relevant Regional Enterprise Unit. It therefore receives £20,000 of government support.

This sounds unfortunate.

We continue to doubt whether Local Enterprise Agencies are worth subsidising at all. As E(A) originally recognised, those that provide a useful service are likely to attract sufficient funding from the private sector. Giving Government money to those which do not attract such private funding avoids 'deadweight' only at the cost of providing alms for deadbeats.

Very much  
doubt that  
this is a  
matter,  
but worth  
discussing perhaps.

A more sensible step might be to relax the conditions of the Business Expansion Scheme, making it easier for Local Enterprise Agencies to raise venture capital from private investors and to use this in support of new businesses.

We recommend that you should raise these points with David Young at the jobs meeting on 7 November, and that you should not agree to his proposals unless he can produce a plausible argument at that meeting.

*Oliver Letwin*

OLIVER LETWIN



*24/10.*



*Prime Minister  
You were concerned  
about*

- costs*
- deadweight*
- administration and possible overlap with the Small Firms Scheme.*

PRIME MINISTER

GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES

*DLW  
24/10.*

1 Your Private Secretary in his letter of 23 September set out a number of questions on the proposals in my earlier minute of 16 September. Very briefly the answers to your questions are as follows; the attached note sets out my reasoning in more detail.

2 Only Agencies with an income of less than £60,000 will be eligible for support and the level of individual funding will be further dependent on the private sector support they receive and the quality of their business plans. On this basis we would expect no more than between 160 and 180 Agencies (out of the current 300) to be assisted with grants of up to £20,000 each initially. This should deal with the main aspects of deadweight which concerned E(A).

*An odd statement. The E(A) programme has been cut, overall.*

3 I am allocating to this policy £2½m a year in 1986/87 and 1987/88 out of the additional bids agreed during the PES round; I fully expect it to be sufficient but if demand were to prove stronger than envisaged, the grants would be rationed more tightly to keep within that figure. The assistance would terminate after five years, with lower levels of expenditure in years 3-5 in order to lever money out of the private sector.



4 The scheme will be administered by my new Regional Enterprise Units, which I announced at the Party Conference. Overall, the Units will cost about £400,000 p.a. but only a small amount of that will be attributed to LEA funding since the Units will have wider responsibility for promoting our small firms, tourism and enterprise policies in their region.

5 On the Small Firms Service (SFS), I recommend that we should review its activities once our funding policy has been running for two years and has had an opportunity to build up the LEAs. This accords with the policy agreed in MISC 108. In the meantime, I will be encouraging the SFS and the LEAs to work more closely together. I would not want to make any public announcement at this stage about the future of the SFS since it would run the risk, as Norman Tebbit recognised in his letter of 18 September, of giving the wrong signals to the small business sector.

6 I would be grateful for your agreement to these proposals although I would propose leaving any public statement until after your review with myself and Kenneth Clarke on 7 November of new measures for encouraging enterprise and employment.

7 I am copying this minute to members of E(A), to John Moore and to Sir Robert Armstrong.

D Y

22 October 1985

CONFIDENTIAL



**CONFIDENTIAL****GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES**

1 The MISC 108 report, discussed at E(A) in May, set out the basic rationale for the scheme - that the Local Enterprise Agency (LEA) movement has proved a successful grass-roots approach to supporting local businesses, that the best LEAs have been very effective in job creation, but that too many of them remain limited in their capabilities or uncertain of their future because of the difficulty of securing sufficient private sector backing. DTI's pump-priming funds (some £175,000 for the whole of England was budgeted for the current financial year) have helped to establish a wider LEA network but are not enough to secure its continuity or to persuade the private sector to play its full role.

2 MISC 108 concluded that what was needed was the provision of a higher level of Government funding for enough time and with enough inducements for private sector matching to create by the end of the period a viable national network which would then survive without further support. Within that, the dual aim was to ensure the continuing viability of the stronger agencies and to bring the most promising of the weaker agencies to the point where they could offer a service good enough to attract adequate local private sector funding.

3 The scheme outlined in the paper sent with my minute of 16 September is intended to meet those objectives, while at the same time introducing the greater element of additionality which E(A) wanted to see. In particular it concentrates support on those agencies whose current annual income is insufficient to support the range of services which they should be able to supply if they are to be fully effective in meeting the needs of small business within their territory.

**CONFIDENTIAL**

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Funding

4 In more detail, within an annual ceiling of £2½ million, up to £20,000 a year initially would be provided to those LEAs in England which meet the criteria proposed - that is, that their total annual operating budget does not exceed £60,000; that they can at least match the sum provided by Government from private sector sources; and that they have put forward an effective business plan and future funding strategy. The business plan would need to cover the range of services to be provided by the agency - such as initiatives to bring together potential investors and small firms - and it would not be sufficient to offer only basic advice and counselling. On this basis, the LEAs which could qualify for the full £20,000 would be those with not more than £40,000 annual income from other sources, of which at least £20,000 was from the private sector. Qualifying LEAs with an income between £40,000 and £60,000 or with private sector support of less than £20,000 would have the Government's contribution reduced from the £20,000 level accordingly - in the one case to keep the total income below the £60,000 level (otherwise it would be unfair to LEAs precluded from support by the £60,000 limit), in the other because of the matching principle.

5 Present information suggests that about one-third of the 300 agencies currently identified by the Department will be ineligible for support either because their current income is in excess of £60,000 (and thus they are in less need of support) or because their structure and funding puts them outside our new arrangements, even as special cases. (See Para 8). However, a number of potentially qualifying agencies will be in Scotland, Wales or Northern Ireland where different arrangements apply. It is therefore expected that only some

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160-180 English LEAs will be in the running for support initially. Given that some are likely to fail to produce adequate business plans and that others will not qualify for the full £20,000, the maximum cost should not exceed £2½ million in any year. This is the level for which PES cover was obtained for 1986/87 and 1987/88 in this year's bilateral discussions, with lower figures for subsequent years, as described below. If demand were to exceed provision in any year I would expect grant levels to be rationed accordingly.

Deadweight

6 This approach aims to deal with the main aspect of the dead weight problem which concerned E(A) - ie the fact that some LEAs are obviously well supported and do not need help. It also deals with the need, which concerned the Financial Secretary in particular, to ensure as far as possible that Government support is matched by new private sector money. The proposal to taper the Government funding over the five years (a maximum of £20,000 per agency in the first two years, falling to £15,000 in the third year and to £10,000 in the fourth and fifth years), and to increase the gearing of matching funds at the same time, aims to ensure that new money is drawn out of the local community as the Government commitment reduces. Total expenditure should therefore be contained within lower figures after 1987/88 - about £1.9 million in 1988/89, falling to £1.25 million for 1989/90 and 1990/91 and then ceasing completely.

Administration

7 In my minute of 16 September, I said that the arrangements for vetting and approving applications for support were being considered as part of the review of the effects on DE structure of taking over DTI's small firms activities. That work is now completed. As I announced at

CONFIDENTIAL

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the Party Conference, I am setting up Regional Enterprise Units to support the seven MSC Regional Directors who act as my representatives in the English regions. The Units will be led at Principal level and their role will be to promote our policies for small firms, tourism, enterprise and deregulation at the regional level, working closely with local industry, Tourist Boards, Chambers of Commerce and so on.

8 They will therefore be well placed to administer the support to Local Enterprise Agencies and to advise the Regional Directors who will normally take the final decisions on funding. (As the note with my minute of 16 September explained, in cases where assistance to an LEA might be justified exceptionally in spite of a shortfall in private sector funds - eg in some inner cities or rural areas - the Regional Director will be required to pass his recommendation to Ministers here for decision.) I expect the administrative costs of the Regional Enterprise Units to be some £400,000 a year. However, only a small part of this cost will be attributable to the administration of support to LEAs.

Business in the Community (BIC)

9 I believe that BIC will be able to play a substantial role in getting this scheme off the ground, both nationally and regionally. In particular, I would hope that their regional staff could help LEAs prepare their business plans and I will look to them to take the lead in encouraging local support from the private sector on a rising scale. Stephen O'Brien's recent letter to you (while it contained some rather over-optimistic estimates of the amount of public support currently going to LEAs) may nevertheless offer the opportunity to set BIC this challenge for the future.

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The future of the Small Firms Service

10 It is clearly right to look again at the role of the Small Firms Service in the light of the support offered to LEAs, which have a similar role in advice and counselling. Once established on the more professional basis that Government support is intended to achieve, they should in the longer term provide the main support for small firms in England and they should then become the natural focus for a wide range of local services - financial, advisory and so on - which other people or organisations can offer. But, as was agreed at E(A), it would not be appropriate to run down the Small Firms Service immediately since at present the LEAs provide only patchy coverage of uneven quality and immediate run-down would therefore leave a considerable gap in the provision of advice to a sector that Government is most anxious to encourage. Such action would also send entirely the wrong signal to the small business world. It is proposed therefore to proceed, as MISC 108 recommended, to a review of the provision of small business advice at the end of the second year of Government support for LEAs, with a view to identifying what the future role for the Small Firms Service might then be. Meanwhile no announcement should be made about the Service's future, beyond encouraging the two networks to operate in the closest co-operation.

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2 MARSHAM STREET  
LONDON SW1P 3EB  
01-212 3434

My ref:

Your ref:

NSP7.

24 September 1985

*In Transit.*

Thank you for copying me your minute of 16 September to the Prime Minister covering your latest proposals on Local Enterprise Agencies.

You have my letter of 20 August commenting on an earlier draft and you will have seen my exchange with John Moore. You therefore know my concern that we should incorporate sufficient flexibility in working up the proposals. I accept that the provisions of paragraphs 18-21 provide an important element of that flexibility. But, more generally, I suggest that the operation of the scheme should be kept under regular review to ensure that it is meeting our objectives.

You refer to your forthcoming PES bilateral. In the case of my Department's spend, the current procedures for Urban Programme support for LEAs will be maintained in 1986/7 and therefore a proportion of UP resources will be committed accordingly.

I am copying this to the Prime Minister, E(A) Colleagues, John Moore and Sir Robert Armstrong.

  
KENNETH BAKER



ECON POL

ENTERPRISE PROPOSALS

PT 6





10 DOWNING STREET

From the Private Secretary

23 September 1985

*Dear Leigh,*

GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES

The Prime Minister has seen your Secretary of State's minute of 16 September, with its attachments.

*RJ/F*  
The Prime Minister would be grateful for a more comprehensive and detailed explanation of the revised proposals for Government support for Local Enterprise Agencies. This should, among other things, include proposals for the administration of the new scheme, together with detailed costings. It would also be helpful to have a fuller explanation of how the new proposals will avoid the problems of dead weight identified by E(A).

The Prime Minister recalls that the proposed national network of LEAs would increasingly take over from the small firms service the function of providing the basic advice and counselling for small businesses. She has asked how the revised proposals on LEAs are intended to fit in with the small firms service and what plans there are for phasing out the service.

I am copying this letter to the Private Secretaries to the members of E(A), the Financial Secretary (H.M. Treasury) and to Michael Stark (Cabinet Office).

*Yours sincerely,*  
*David Norgrove*

DAVID NORGROVE

Leigh Lewis, Esq.,  
Department of Employment.



PRIME MINISTER

GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES

Lord Young's minute of 16 September (flag A) seeks your endorsement for revised proposals for a network of Local Enterprise Agencies (LEAs). You need only read the covering minute itself and perhaps the summary of recommendations.

Several colleagues have written in support (letters below - no need to read) though the Treasury and to a lesser extent Mr Tebbit are doubtful about the extent of the Government financial assistance which Lord Young proposes.

The Policy Unit (flag B) have more fundamental doubts.

I believe this has now advanced to the point where fundamental doubts are too late: E(A) has already endorsed the recommendation that a national network of LEAs should increasingly take over from the small firms service the function of providing the basic advice and counselling for small businesses.

The main doubt now is about the total cost and where the money will come from. Lord Young's minute does not give a total cost: he knows the public sector game and is looking for endorsement of the policy by today, without figures, leaving money to be discussed with the Chief Secretary at his bilateral on Monday.

DE put the cost of Lord Young's proposals at £3m. in each of the next two years, declining thereafter. The Treasury want to put a limit of £2m. In your summing up in May you pointed to the urban programme, MSC, and DTI programmes as potential sources of the necessary funds.

I suggest you might:-

DE knows they won't have the time for you.



- i) Agree that the proposals are an improvement on those discussed by E(A) in May;
- ii) Ask for a further report in due course on how the scheme will be administered (the Policy Unit are concerned that it might be administered in DTI because that would bias it towards manufacturing industry);
- iii) Note that the extent of resources to be made available, and their source (for which some possibilities were mentioned in your E(A) summing up) will fall to be discussed in the Survey.

Content for me to write as above?

DW

David Norgrove  
20 September 1985

- I think
- ① the proposals are far too sketchy
  - ② the administration has not been worked out
  - ③ the idea was that the small firms fund should be phased out. How are the money proposals going to fit in with this fund and what are the plans for phasing out the fund. If we are not careful we shall finish up with 2 sets of arrangements

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20 September 1985

LOCAL ENTERPRISE AGENCIES

We believe that it would be rash to agree to David Young's uncosted proposals in advance of the public expenditure round. To do so would be, in effect, to sign a blank cheque which the Chief Secretary could not prevent David Young from drawing.

We have, in any case, severe doubts about the efficacy of Local Enterprise Agencies. Before being allowed to proceed with any scheme, Department of Employment should be asked to produce both detailed costings for the entire operation and evidence that Enterprise Agencies have actually been effective in creating new jobs.

But E(A) has already agreed to a national network.

It would be absolutely catastrophic to give control over the funds to DTI's Regional Directors: this will virtually ensure a bias in favour of big manufacturing business and against the job-creating service and small business sector. A sensible system of administration needs to be worked out before approval is given for the policy.

Yes, but this is not a foreigner exclusion

There is also no evidence that the new proposals will actually avoid the deadweight problems identified by E(A). Further details are needed.

I am not sure how further details will help matters.

We recommend that you should:

1. write to David Young, requesting further specification of the proposals; and
2. make clear that any consent will depend on the outcome of the Public Expenditure Survey.

*Oliver Letwin*

OLIVER LETWIN



DEPARTMENT OF TRADE & INDUSTRY



GENERAL POLICY DIVISION

Room 635 1 Victoria Street London SW1H 0ET

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---

To all recipients of copies  
of speech material on competition  
policy

Your reference

Our reference

Date

---

There was a typographical error in topic no. 9 of the speech material circulated under cover of Mr Fletcher's letter to the Chancellor of 28 June. The figure for investment in the penultimate sentence of that item should read £100m not flm.

A corrected sheet is enclosed for substitution in your sets of material.

A handwritten signature in dark ink, appearing to read 'R E Allen'.

R E Allen

Enc.

Small Firms

Central to the development of a more efficient, competitive and prosperous economy is the Government's policy of encouraging the setting up and growth of small firms. Small firms are a major force for competition and flexibility. They provide diversity of supply, and broaden the choices available to consumers. The Government has therefore sought to help small firms overcome the disadvantages of smallness by removing those distortions in the economy which have discriminated against small firms. A major plank in this policy is the reduction of burdens imposed on firms by legislation and bureaucracy. Employment legislation has been eased, planning procedures have been simplified, and a major review of burdens over 7 Government Departments has just been completed. Small firms also benefit particularly from the measures we have taken to improve the flexibility of financial and capital markets. Of particular relevance to small firms is the Business Expansion Scheme which encourages small equity investments. Last year more than half of £100m invested under the scheme went to new or young companies. The encouragement of small businesses is also important because of their major potential for employment creation.

Contact: Roger Allen DTI

Tel: 215 4049

July 1985





2 MARSHAM STREET  
LONDON SW1P 3EB

01-212 3434

My ref: J/PSQ/15830/85

Your ref:

25 July 1985

Dear Annabel

SMALL FIRMS SEMINAR BY MPs

(P90) My Secretary of State has now seen a copy of your Minister's letter of 4 July and the draft letter to MPs. I have also received a copy of Alex Galloway's letter of 12 July.

We fully support the approach outlined, but we would like to make a suggestion for inclusion in the proposed letter to MPs. It would be useful to mention, for those MPs with rural constituencies, the work of the Council for Small Industries in Rural Areas. CoSIRA, as the main agency of the Development Commission, offer a comprehensive range of technical, managerial and financial advice and assistance, together with training courses, for small rural firms in England, and can act as a lender of last resort. They operate through a network of County offices and their County organisers might well be able to attend appropriate locally-organised seminars and describe the services they offer.

Perhaps you could incorporate a suitable entry among the list of contacts in the fourth paragraph of your draft letter on the lines of:

(ix) In rural areas, a representative of the Council for Small Industries in Rural areas (CoSIRA) - who offer a wide range of services particularly technical, managerial and financial advice and assistance to small rural firms. A list of CoSIRA county offices is attached.

Officials here are in touch with the Development Commission to alert them to this.

I am sending copies of this letter to Alex Galloway and the recipients of his letter of 12 July.

Yours sincerely  
Alex Davis

A H DAVIS  
Private Secretary

Miss Annabel Goulding

### County Committee of CoSIRA and County Offices

CoSIRA has established over a number of years thirty four county based Committees of voluntary members with suitable expertise, local interest and influence who support and promote the work of CoSIRA. There are also Sub-Committees for the Isle of Wight and Cleveland. Liaison with the Board of Directors is maintained through the Board member with special responsibility for the county.

CoSIRA's thirty one offices are grouped into regions for administration. Each region is managed by a Regional Controller based at one of the County Offices.

<i>North</i>		
<i>County</i>	<i>Chairman</i>	<i>Address of County Office</i>
*Cumbria	Mr M E O'Brien MA CEng MI Mech E	CoSIRA, Ullswater Road, Penrith, CA11 7EH Tel: (Penrith) 0768-65752/3
Durham	Mr T Swan (Mr P G Woodward JP FRICS until September 1984)	CoSIRA, Morton Road, Darlington, Co Durham, DL1 4PT Tel: (Darlington) 0325-487123.
Cleveland Sub-Committee	Mr J B Robertson	
Humberside	Clr S Blackburn AMIBA MIRTE	CoSIRA, 14 Market Place, Howden, Goole, N Humberside, DN14 7BT Tel: (Howden) 0430-31138
Lancashire	Mr E P Sharp The Lord Shuttleworth (until September 1983)	CoSIRA, 15 Victoria Road, Fulwood, Preston, PR2 4PS Tel: (Preston) 0772-713038
Northumberland	Mr J Festing JP  (Lt Col H Crossman (until October 1983))	CoSIRA, Northumberland Business Centre, Southgate, Morpeth, NE61 2EH. Tel: (Morpeth) 0670-58807 or 514343 (via Business Centre)
North Yorkshire	Mr M G Foster JP	CoSIRA, The Lodge, 21 Front Street, Acomb, York, YO2 3BW Tel: (York) 0904-793228
West Yorkshire	Mr H Buckley	CoSIRA, Council Offices, York Street, Barnsley, South Yorkshire, S70 1BD Tel: (Barnsley) 0226-286141 Ext 481 See West Yorkshire
South Yorkshire	The Hon Neil Turner MBIM PGrad, Dip FGA ARICS	
<i>East</i>		
*Leicestershire	Clr R R Angrave	CoSIRA, Chancel House, East Street, Bingham, Notts, NG13 8DR Tel: (Bingham) 0949-39222/3
Cambridgeshire	Mr I M Purdy RIBA, MRTPI	CoSIRA, 24 Brooklands Avenue, Cambridge, CB2 2BU Tel: (Cambridge) 0223-354505
Lincolnshire	Mr V R Hedley-Lewis, FCA	CoSIRA, Council Offices, Eastgate, Sleaford, Lincs Tel: (Sleaford) 0529-303241
Norfolk	Mr R E T Gurney JP ARICS	CoSIRA, Augustine Steward House, 14 Tombland, Norwich, NR3 1HF Tel: (Norwich) 0603-24498
Northamptonshire	Mr J R Dove FCA ATII (Mr P Chapman OBE until September 1984)	CoSIRA, Hunsbury Hill Farm, Hunsbury Hill Farm Road, Northampton, NN4 9QX Tel: (Northampton) 0604-65874
Nottinghamshire	Mr C R Bear LLE	See Leicestershire
Suffolk	Mr W J Bridge DL (Mr D J Sarginson until January 1984)	CoSIRA, 28a High Street, Hadleigh, Ipswich, IP7 5AP Tel: (Ipswich) 0473-827893



South East

County	Chairman	Address of County Office
Bedfordshire & Hertfordshire	Mr J Broomfield (Mr R Corbett until August 1984)	CoSIRA, Agriculture House, 55 Goldington Road, Bedford, MK40 3LU Tel: (Bedford) 0234-61381
Essex	The Hon R H C Neville DL MA (Mr N V Pedley until July 1984)	CoSIRA, Bees Small Business Centre, Hay Lane, Braintree, Essex, CM7 6ST Tel: (Braintree) 0376-47623
Hampshire	Mr R Chester MA (Mr M A H Walford until October 1984)	CoSIRA, Northgate Place, Staple Gardens, Winchester SO23 8SR Tel: (Winchester) 0962-54747
Isle of Wight Sub-Committee	Sir John Nicholson Bt KBE CIE	CoSIRA, 6-7 Town Lane, Newport Isle of Wight, Tel: (Newport) 0983-528019
Kent	Mr D G W Barham FRICS DL JP (Mr G L Hooson (until May 1983))	CoSIRA, 8 Romney Place Maidstone, ME15 6LE Tel: (Maidstone) 0622-65222
Oxfordshire, Buckinghamshire Berkshire	Mr D A W Black CA MBIM	CoSIRA, The Maltings, St John's Road, Wallingford, Oxon Tel: (Wallingford) 0491 35523
Surrey	Mr G A M Geddes	CoSIRA, 2 Jenner Road, Guildford, Surrey, GU1 3PN Tel: (Guildford) 0483-38385
Sussex	Lt Col W R H McKee TD JP	CoSIRA, Sussex House, 212 High Street, Lewes, BN7 2NH Tel: (Lewes) 0273-471399

South West

*Devon	Mr E Dancer	CoSIRA, 27 Victoria Park Road, Exeter, EX2 4NT Tel: (Exeter) 0392-52616
Avon	Cllr Mrs S J Marshfield JP	CoSIRA, 209 Redland Road, Bristol, BS6 6YU Tel: (Bristol) 0272-733433
Cornwall	Mr H Calder BA Dip TP FRTPI FRGS (Mr R H Stapleton until May 1984)	CoSIRA, 2nd Floor, Highshore House, New Bridge Street, Truro, Cornwall TR1 2AA Tel: (Truro) 0872-73531 or 73281
Dorset	Mr A Swindall Dip TP FRTPI ARICS (The Lady Digby until December 1984)	CoSIRA, Room 12/13, Wing D, Government Buildings, Prince of Wales Road, Dorchester, Dorset Tel: (Dorchester) 0305-68558
Somerset	Mr P J Field	CoSIRA, No 1, The Crescent, Taunton, TA1 4EA Tel: (Taunton) 0823-76905
Wiltshire	Professor G F McDonic Dip TP FRTPI DPA	CoSIRA, 141 Castle Street, Salisbury, SP1 3TP Tel: (Salisbury) 0722-336255 Ext 252/313

West

*Cheshire	Dr J C Gardner PhD BSc	CoSIRA, Strickland House, The Lawns, Park Street, Wellington, Telford, Shropshire, TF1 3BX Tel: (Telford) 0952-47161/2/3 (w.e.f. 19 November 1984, CoSIRA, 6 Shropshire Street, Audlem, Cheshire, CW3 0DY Tel: (Audlem) 0270-812012
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County	Chairman	Address of County Office
Derbyshire	Mr D C Crowther DLC, CEng, MRAeS	CoSIRA, Church Street, Wirksworth, Derby, DE4 4EY Tel: (Wirksworth) 062982-4848
Gloucestershire	Mr J Workman MA (Mr J D Griffiths JP NCC until July 1984)	CoSIRA, 24 Belle Vue Terrace, Malvern, Worcs, WR14 4PZ Tel: (Malvern) 06845-64506
Hereford & Worcestershire	Mr J M Carpenter	See Gloucestershire
Staffordshire	Mr J G Bamford BA (Cllr Hood until August 1983)	See Cheshire
Warwickshire	Dr I G Gibson PhD BSc (Econ)	CoSIRA, The Abbotsford, 10 Market Place, Warwick, CV34 4SL Tel: (Warwick) 0926-499593

Regional Controller's office



Geom Pol; Small forms Pt 6.



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NORTHERN IRELAND OFFICE  
WHITEHALL  
LONDON SW1A 2AZ

SECRETARY OF STATE  
FOR  
NORTHERN IRELAND

The Rt Hon Lord Young of Graffham PC  
Secretary of State for Employment  
Caxton House  
Tothill Street  
LONDON SW1

20 September 1985

*Dear Secretary of State*

GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES

With your minute of 16 September to the Prime Minister you circulated revised proposals for Government support to Local Enterprise Agencies. I welcome the proposals you have circulated, in particular the emphasis they place on a realistic business plan and on co-funding with the private sector.

I think you are aware that Northern Ireland has had in place for some time its Local Enterprise Programme which has similar objectives to your proposals but which is tailored in its application to the smaller and more dispersed communities in the Province. The Local Enterprise Programme has been very successful in its first years of operation in Northern Ireland.

Copies of this go to the Prime Minister and copy recipients of your minute.

*Yours sincerely*  
*Brian Porter*

TOM KING

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

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Econ Pol: Small Firms



From the  
Minister of State

Ministry of Agriculture, Fisheries and Food  
Whitehall Place London SW1A 2HH

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Rt Hon Lord Young of Graffham  
Secretary of State for Employment  
Department of Employment  
Caxton House  
Tothill Street  
LONDON  
SW1H 9NF

20 September 1985

*David*

GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES

In Michael Jopling's absence abroad I would like to comment on your minute of 16 September to the Prime Minister in which you ask for comments from colleagues on your proposals by today.

Our interests in MAFF relate mainly to rural LEAs and I share Kenneth Baker's concern that the scheme should allow sufficient flexibility to cater for such Agencies. I understand that while some rural LEAs take in small to medium sized country towns, others are entirely rural and have been established by businessmen anxious to assist the development of pockets of local rural industries. Both types deserve our support and could play a vital role in stimulating the rural economy in the areas they serve.

I therefore fully support the proposals in paragraph 19 of the paper attached to David Young's minute. In my view, it is most important that rural LEAs should work in close touch with the Development Commission and CoSIRA.

*Yours  
John Selwyn Gummer*

JOHN SELWYN GUMMER



CC 1/3



Y SWYDDFA GYMREIG  
 GWYDYR HOUSE  
 WHITEHALL LONDON SW1A 2ER  
 Tel: 01-233 3000 (Switslwrdd)  
 01-233 7448 (Lined Union)

*Odd wrth yr Is-Ysgrifennydd Seneddol*

WELSH OFFICE  
 GWYDYR HOUSE  
 WHITEHALL LONDON SW1A 2ER  
 Tel: 01-233 3000 (Switchboard)  
 01-233 7448 (Direct Line)

*From The Parliamentary Under-Secretary*

20 September 1985

*Sir Secretary of State,*

**GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES**

Thank you for copying to Nicholas Edwards your minute of 16 September to the Prime Minister seeking comments on the revised proposals for providing Government support to develop a network of Local Enterprise Agencies in England.

I can confirm the views expressed by Nicholas Edwards in his letter of 21 August 1985 that we would not wish to disturb the system already established in Wales. We shall, of course, watch developments in England to ensure that there is no serious inconsistency of approach. I note that the revised proposals now have sufficient flexibility to cater for exceptional cases.

/ I am copying this letter to the Prime Minister, other members of E(A), to John Moore and Sir Robert Armstrong.

*Yours sincerely*

*Wyn Roberts*

WYN ROBERTS  
 (Dictated by Mr Roberts and  
 signed in his absence)

The Rt Hon Lord Young of Graffham  
 Secretary of State for Employment  
 Department of Employment  
 Caxton House  
 Tothill Street  
 London  
 SW1H 9NF



From the  
Minister of State

Ministry of Agriculture, Fisheries and Food  
Whitehall Place London SW1A 2HH

NBA 7

D J Normington Esq  
Private Secretary to  
The Rt Hon Lord Young of Graffham  
Secretary of State for Employment  
Department of Employment  
Caxton House  
Tothill Street  
LONDON  
SW1H 9NF

20 September 1985

Re: Mr Normington

**GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES**

I am sorry that we omitted to disclose details of copy recipients of my Minister's letter of 20 September to the Rt Hon Lord Young of Graffham.

Copies of my Minister's letter have gone to the Prime Minister, Members of EA and Sir Robert Armstrong.

I have copied this letter to the Private Secretaries to the Prime Minister, Sir Robert Armstrong and Members of EA.

Yours Sincerely

SHIRLEY STAGG (MRS)  
PRIVATE SECRETARY





Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Lord Young of Graffham  
 Secretary of State  
 Department of Employment  
 Caxton House  
 Tothill Street  
 London  
 SW1H 9NA

19 September 1985

*Dev David,*

GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES *with bn?*

Your minute to the Prime Minister of 16 September seeks colleagues' endorsement to a revised approach for encouraging the development of a network of local enterprise agencies.

I welcome many of the features of the revised proposals such as the stipulation that only agencies with an annual operating income below a specified level per annum would be able to apply for funding (and would not automatically qualify for support) and that successful applicants would need to have put forward an effective business plan and a funding strategy to lever funds from the private sector. Clearly careful selection between applications would be necessary to ensure that any Government money that is available is used in the best possible way and is not replacing existing private funds.

Your minute refers to our forthcoming PES bilateral on 23 September. The original proposal in the MISC 108 report had been for £5 million of expenditure on LEAs in the first year. Against the background of the Prime Minister's summing up in the EA minutes that "further consideration be given to what minimum level of Government support would be needed to establish viable agencies in areas where the local resources of finance and entrepreneurship had been found to be inadequate", John Moore wrote to David Trippier (on 22 July) suggesting that £2 million ought to be the maximum limit of financial support in 1986-87 of any scheme. This total would allow 100 out of the about 250 agencies to receive £20,000; more agencies could receive support to the extent that some receive less than £20,000. A ceiling of £2 million per year therefore provides a maximum level of financial support consistent with the EA conclusion. Even a sum rather less than £2 million would allow progress to be made in further developing a network of LEAs. Although your note proposes

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that Government support should not take on LEA's over an annual overall income level of £60,000, I imagine that your judgement about the size of overall income level may depend upon how much money was available for LEA support.

Against the background of identifying maximum possible overall public expenditure savings, if colleagues endorse your proposals, in our bilateral we will need to identify offsetting savings if some additional financial support is to be given to LEAs.

Copies of this letter go to E(A) colleagues and to Sir Robert Armstrong.

*Yours ever,*  
*JH*

JOHN MacGREGOR



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Chancellor of the Duchy of Lancaster

CABINET OFFICE,  
WHITEHALL, LONDON SW1A 2AS

Tel No: 233 3299  
7471

18 September 1985

The Rt Hon Lord Young of Graffham PC  
Secretary of State for Employment  
Caxton House  
Tothill Street  
LONDON SW1

*D. David.*

**GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES**

Thank you for copying to me your minute of 16 September to the Prime Minister, attaching a paper detailing proposals for government support for building a viable and comprehensive network of local enterprise agencies. *with ideas?*

I agree with what is proposed, and I welcome the prospect that, by these means, a self-sustaining network of support and advice can be given to new and smaller businesses.

The level of assistance now proposed reflects that which we discussed at E(A). The annex to your paper indicates that the great majority of Local Enterprise Agencies (LEAs) will be eligible. I hope, therefore, that the level of assistance should indeed be seen as a maximum, rather than as a norm. While I would not wish to see the procedure bogged down by bureaucracy, it is important to make it clear that the assistance is intended to exercise leverage over the private sector funding of LEAs and over some aspects of the way in which they approach their task.

Related to this latter point, I hope that your proposals will also ensure that the fact of government support to LEAs is sufficiently reflected in the publicity and presentational material produced by the Agencies; we don't want the point to be lost that local enterprise and self-help are being pump-primed by Government. Also, if the LEAs are to be as effective as possible, I should be glad to know that sufficient separate help was being planned, perhaps through BIC but also directly, to provide a source of central guidance, material, publications, publicity and advice, which will act as a further means of leverage on the direction and style of LEA activity. While I

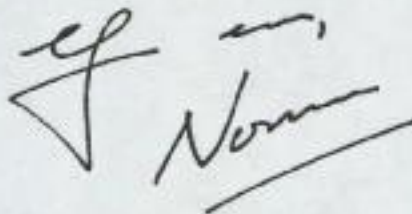
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- 2 -

appreciate that BIC will play an important role, I think that we should keep our own means of ensuring that the Agencies are well-advised and directed.

Finally, your minute does not mention the proposal raised by MISC 108, that the LEA network should eventually take over the functions of the Small Firms Service. I think we have some way to go before it can be clear whether this is the right way of proceeding, and I hope that colleagues will have a further opportunity in due course to consider this.

I am copying this letter to the Prime Minister, other E(A) colleagues, and to Sir Robert Armstrong.

A handwritten signature in black ink, appearing to read 'Norman Tebbit', with a horizontal line underneath the name.

NORMAN TEBBIT





PRIME MINISTER

GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES

When E(A) took the report of the Ministerial group on small firms on 10 May colleagues endorsed the recommendations to develop a network of Local Enterprise Agencies (LEAs). You asked me to consider further with colleagues what minimum level of Government support would be necessary to assist the effective development of such a network and how such support should be applied.

David Trippier has taken the lead in producing a revised approach with other colleagues who served on the Ministerial group. This approach will provide modest funds on a tapering basis to eligible agencies and the attached paper, which I endorse, details our proposals. Only those agencies with an operating income below £60,000 per annum will be able to apply\* for funding, up to a maximum of £20,000 in years 1 and 2, reducing to £10,000 in year 5. Applicants will have to satisfy specific criteria, including putting forward an effective business plan and funding strategy to lever funds from the private sector, as we agreed before. In this way we will ensure that the new policy is not a potential rescue act for agencies in difficulty but a positive approach to building a viable network.

\* This restriction is presumably intended to meet E(A)'s concern that "it was doubtful whether it would be appropriate to offer Government money... [where] agencies were already working effectively without such support." The £60,000 restriction cuts off some agencies - see chart at end of paper.

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In the earlier correspondence, which David Trippier circulated, there were two points of emphasis raised by colleagues, both of which I believe have been met in the paper attached. Kenneth Baker had been concerned that the scheme should allow sufficient flexibility to cater for those agencies in inner urban or rural areas which would have difficulty in meeting too strict criteria on private sector funding but still had an important role in fostering enterprise in their area. I believe the provisions proposed for "exceptional cases" (Paras 18-21 of the paper) should meet this need without weakening the basic criteria. John Moore was very properly anxious that Government support should be used to secure additional funds from the private sector. There may be some difficulty in ensuring this in all cases in the first year of the scheme, but I believe the point is met in substance by the provision that agencies will only qualify if they can show how extra outside funding is to be drawn in as Government support reduces.

One point of detail on which further work will have to be done though without affecting the policy now proposed - concerns the provision for vetting and approving applications for support from agencies. The original proposal had been to use DTI's Regional Directors in this role. The study now in hand of the implications for DE of taking over DTI's Small Firms Service will have to address this as one of a number of consequential organisational issues.

I will of course be taking up the question of financial provision for support of Local Enterprise Agencies in my Department's forthcoming PES bilaterial now arranged for

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23 September. At this stage, therefore, I am seeking colleagues' endorsement of the policy approach as now revised, in the hope that it will be possible to take forward the proposals as outlined in the attached paper as quickly as possible. May I therefore ask for any comments by 20 September.

*DE know  
they will  
not have  
your comments  
by this  
deadline*

Copies of this minute and the attached paper go to E(A) colleagues, to John Moore and to Sir Robert Armstrong.

*ref*  
D Y

16 September 1985

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SUPPORT FOR LOCAL ENTERPRISE AGENCIES

SUMMARY OF RECOMMENDATIONS

1. To be eligible for support, agencies should:
  - i) have an operating income of no more than £60k for the first year of Government support;
  - ii) submit a three year business plan and a five year strategy for funding.
2. There should be a five year programme of Government funding for LEAs. Such funding to be available from DE. *for existing DE funds. and found*
3. The maximum funding for any agency should be:
  - £20k in years 1 and 2
  - £15k in year 3
  - £10k in years 4 and 5.
4. Funding will originally be on the basis of matching private sector financial support, but in later years private sector support will need to be geared up as the Government support decreases in order to maintain the overall income of the agency. Government support should not take the agency over the annual limit for support (ie £60k in the first year).
5. There will be no entitlement to the maximum eligible level of funding. The level of support will be dependent on the needs and justification given in the business plan.
6. Urban Programme funding of enterprise agencies will continue for 1986/7 but thereafter all agencies should come to DE for support although some topping up by the Urban Programme for specific projects or activities may be possible.
7. Enterprise agencies in rural areas will in future apply to DE for support although the Development Commission may in specific circumstances also give additional support.



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8. In areas where the private sector support is particularly weak, account may be taken of local authority support to an agency in addition to the private sector support in order, if appropriate, to trigger the full DE support.

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## GOVERNMENT SUPPORT FOR LOCAL ENTERPRISE AGENCIES

1. E(A) at its meeting on 10 May asked that further consideration should be given to developing a policy of Government support for local enterprise agencies, directed at establishing viable agencies in areas where the local resources of finance and entrepreneurship have been found to be inadequate. The objective of Government support would be to help promote the establishment of a comprehensive viable network of self-supporting LEAs. This paper proposes a policy for the identification of agencies that might merit support and for the application of Government support with a view to achieving viability in the medium term.

2. Agencies should play a vital role at the local level in promoting enterprise and creating jobs. Some agencies will not want or need Government support since they have considerable resources themselves in terms of finance, secondees and other facilities. The London Enterprise Agency (LEnta) is one, Leicester Business Venture, the Director of which recently wrote to the Prime Minister, is another. But there are not many agencies in that category. Other agencies are far weaker especially in terms of financial resources and may well merit support, if such support would lead to viability in the medium term. But how to determine the dividing line and to produce manageable guidelines which will enable the DE and Business in the Community (BIC) to determine whether a particular agency merits Government support or not?

3. What is clear is that simple geographical criteria will not work. Many agencies in assisted areas, particularly where there is a substantial private sector employer behind the agency, may not need support; while agencies in the prosperous South East may well need Government assistance since either they are in a pocket of "relative" poverty or in the absence of large firms in the area, they are finding it difficult to generate sufficient funding from medium sized firms.

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4. The most straightforward indicator of need is the level of funding of an agency. Obviously account has to be taken of the availability of secondees, premises etc which may not feature in the "profit and loss account" of an agency; but it is clear that without a basic level of funding and without an element of continuity in that funding an agency is unable to plan realistically for the future, and it is operating without a sound commitment from its community, especially the local private sector.

5. The right minimum level of funding is not easy to define. However, as a general rule (and there will be some exceptions), it is to be expected that viable agencies need a salaried rather than a seconded director. Secondees generally do not stay more than two years - in many cases for a rather shorter period. The director of an agency should in principle give continuity to an agency and should be expected to stay rather longer; secondees if available can act as support staff. In addition to a "permanent" salaried director, agencies also need sufficient basic resources to get initiatives under way and to act as the focus of their local network of support to small firms.

6. In order to develop a workable policy, it is proposed that a limit should be set on the level of funding received by an agency if it is to be eligible for support. Such a level would take account of the cost of a director and of additional funding to develop various activities. Any level set will involve an element of "rough justice" in that costs may vary significantly between agencies eg

- i) some directors may need a full salary whereas others on substantial pensions from their previous employer may only want "topping up";
- ii) the cost of premises may vary radically from area to area.



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7. Nonetheless, and not withstanding these factors, it is recommended that an operating income of £60k for agencies should be set in the first year as a limit for Government support. An agency with an income over £60k will have to "cut its cloth accordingly"; it can have no strong case for asking for Government support. An agency below £60k would not qualify automatically; but would merit consideration. And if supported, the Government support should not be such as to take income over £60k.

8. The limit of £60k should be adjusted in later years both to take account of inflation and to make allowances for an agency's success in attracting further private sector contributions. It is recommended that the limit increases by £5k/year to £80k in the fifth year. (By way of comparison, the histogram at Annex A illustrates the current distribution of cash income between agencies).

9. Agencies meeting the income limit criterion should not be automatically supported. Government funds should only be available if the agency can demonstrate how those funds will be used and how it will seek to attract additional private sector funding in later years as Government support is withdrawn. It is envisaged that the programme of Government support will last five years only and that the funding to individual agencies will be progressively reduced over that period.

10. In order to merit Government support, it is recommended that, in addition to having to have income below the limit set above, agencies should also be able to submit:

- a) A three year business plan.

This should cover the development of agency activities in that period. Precise guidance will need to be developed in consultation with BIC, but it would be expected that, dependent



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on the level of resources available, some or all of the following would be addressed:

- i) development of enquiry and counselling services. This should include projected numbers of clients and promotional activities to achieve those targets. It should also address co-operation with the Small Firms Service;
  - ii) initiatives to bring together at the local level potential investors and those who would benefit from receiving equity funds;
  - iii) development of projects and other services in the community eg small business clubs, managed work units, educational links. This will reflect the practical development of the LEA's role as the focal point of the local network of support for small firms.
  - iv) initiatives to involve better availability of professional advice to small firms eg from the banks;
  - v) the development of the Board's role, both in general oversight of the agency and more importantly for fund raising.
- b) A five year strategy for funding.

This should cover:

- i) the prospects for future private sector support from the community it serves;
- ii) a strategy for gearing up that resource, in particular using the leverage of the Government's funding;
- iii) the capacity for developing income generating activities.

These plans will have to be updated each year as a condition for continuation of funding.

11. These plans will need to be examined critically by BIC and the DE. The level of support to be offered will be dependent on the capacity of an agency to demonstrate that such funds can be used. It will need to be made clear that the level of Government grant will depend very much on the circumstances and plans of the agency; there will be no entitlement to the maximum level of grant unless the need is there.

12. In administering this aspect of the new policy, Business in the Community will play an important role particularly at the regional level. It is envisaged that BIC will help LEAs in giving guidance in the preparation of business plans and financial strategies. Furthermore, these documents should be submitted to DE through BIC which will give its assessment of the plans. The Department will be unlikely to support any agency if its plans are not endorsed by BIC. The Department will particularly need to look to BIC for a view on whether agencies with very serious funding problems have a chance of viability on their own or whether they should be encouraged to merge with neighbouring agencies. The Government will want to remain at arms length from decisions on the geographical coverage of agencies although it will want to ensure that it is not trying to promote agencies with too narrow a geographical (and hence private sector) base.

#### FORM OF GOVERNMENT SUPPORT

##### General Principles:

13. The aim is to produce viable agencies in the medium term by encouraging particularly strengthened private sector support to LEAs. It is therefore recommended, as proposed by MISC 108, that Government support should be time-limited and that it should at first be on the basis of matching private sector contributions. In order to give a positive incentive to agencies to find additional private sector support, it is further proposed that funding should reduce progressively over time and that it should only



be maintained if agencies can generate additional support to compensate for the reduction in Government aid.

14. Although in the most straightforward cases, it is proposed that Government funding should at first match private sector funding and that there should be appropriate gearing introduced in later years, there will be certain exceptional cases needing special treatment. These are covered in paras 18-22 below.

Practical Detail:

15. It is recommended that Government funding for LEAs should be available from DE over five years. The maximum funding for any agency should be:

£20k in years 1 and 2  
£15k in year 3  
£10k in years 4 and 5.

Agencies whose funding starts after year 1 will be eligible for funding as set out above; ie an agency applying for the first time for support in year 4 will be eligible at maximum for £10k.

16. As set out earlier, the funding should only be available to agencies which currently have annual funding of less than £60k (a larger amount in later years - see para 7) and which can satisfy the Department that they have a practical and feasible three year business plan (which demonstrates inter alia the immediate need for Government financial support) and five year strategy for financial viability.

17. The funding will be awarded initially on the basis of matching private sector financial support to the agency, but will be geared in later years as follows:

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	PRIVATE SECTOR FUNDING TO TRIGGER £1 OF GOVERNMENT SUPPORT	MAX. GOVERNMENT FUNDING (see note)	PRIVATE SECTOR CONTRIBUTION NEEDED TO TRIGGER MAX. GOVERNMENT FUNDING
1	£1	£20k	£20k
2	£1	£20k	£20k
3	£1.66	£15k	£25k
4	£3	£10k	£30k
5	£3	£10k	£30k

Note: Government funding will be subject to a further limit that it does not take overall agency funding over annual limit for support (£60k in first year rising to £80k in final year).

## Exceptional Cases

### 18. Agencies with Urban Programme funding:

Some inner area agencies receive substantial funding from DoE's Urban Programme funding. It is recognised that the new policy should deliver basic "revenue" funding to agencies from Government through DE. But the lead time needed by local authorities to prepare submissions to DoE under the Urban Programme means that it is impractical to expect the new policy to come into effect until the year after next (ie 1987/8). And even then, given the severe needs of these areas, agencies should be able to seek Urban Programme support, over and above any DE contribution, for specific projects or activities. It is accordingly recommended that:

- i) current Urban Programme commitment should be maintained and in order that local authorities can prepare Inner Area Programmes for submission to DoE in the autumn, current procedures will apply to 1986/7 IAPs;
- ii) thereafter, all agencies seeking support from Government should come to DE which will judge the case for support on DE's general criteria;



- iii) an agency may nonetheless apply to the Urban Programme or other funding sources (eg MSC) for support over and above that provided by DE (if any) in support of additional projects or activities (eg training projects, workshops, ethnic advice).

19. Agencies with Development Commission funding.

A few agencies receive Development Commission funding via CoSIRA. Overall this is very limited (no more than £12k total in 1984/5). Given the very special problems in rural areas and the Development Commission's particular responsibilities it is recommended that:

- i) Enterprise Agencies in rural areas should initially apply to DE for support; they will be judged against the criteria set out in this paper;
- ii) such agencies may nonetheless apply to the Development Commission for support over and above that provided by DE in support of additional projects or activities.

20. Agencies with local authority support but weak private sector support.

It is a fact that the private sector may be fairly weak in a number of areas where neither the Urban Programme nor the Development Commission will be able to provide support. Although generally the aim is to use Government financial support to match private sector contributions, there is a case where the private sector is particularly weak for considering local authority support along with private sector funding as the basis for matching. This is to get LEAs up to a very basic level of funding and it should be undertaken in a way that encourages more private sector support and does not allow the local authorities to reduce their commitment.



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21. It is recommended therefore that where the private sector contribution is less than that needed to trigger full DE funding support (see Table 1), account may be taken of local authority support to trigger the full DE support (if an agency can demonstrate the need for such support in terms of planned and projected activities in their business plan). Some examples may illustrate the principle:

- i) assume an agency for year 1 (or year 2) can find only £10k private sector funds. This would imply DE support of £10k. But if it also has local authority support of say £15k, it would be possible to add £10k of that £15k to the private sector's £10k in order to trigger, if justified, the full DE £20k;
- ii) assume that in year 3, the private sector contribution has risen to £18k, and that the local authority contribution has remained constant at £15k. Then £7k of the £15k can be added to the private sector £18k in order to trigger the DE £15k maximum funding in year 3.

### 22. Local Co-operative Development Agencies.

These can be recognised by the DE as LEAs. A few receive private sector support and the national Co-operative Development Agency (CDA) wants to encourage this development. It is recommended that if local Co-operative Development Agencies satisfy the criteria in this paper, they should be eligible for support, as with any other LEA. But the national CDA should be the advisory body both to those agencies and to DE, rather than BIC.

#### Definition of an LEA

23. Currently there is a difference of interpretation between DE and BIC over what constitutes an LEA. DE has adopted a fairly wide-ranging approach which includes all bodies classified as



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LEAs for the purpose of Section 48 of the 1982 Finance Act, which then entitles their sponsors to claim tax relief on their contribution. BIC has adopted a tighter approach and excludes a number of DTI recognised bodies (eg Small Business Clubs, local Co-operative Development Agencies).

24. Given that the aim of the policy proposed in this paper is to develop viable agencies, which are supported to a large part by the private sector and which will promote the local network approach set out in the report of MISC 108, it is to be expected that a number of bodies recognised by DE as LEAs will not qualify for support - nor would it be appropriate to support them.

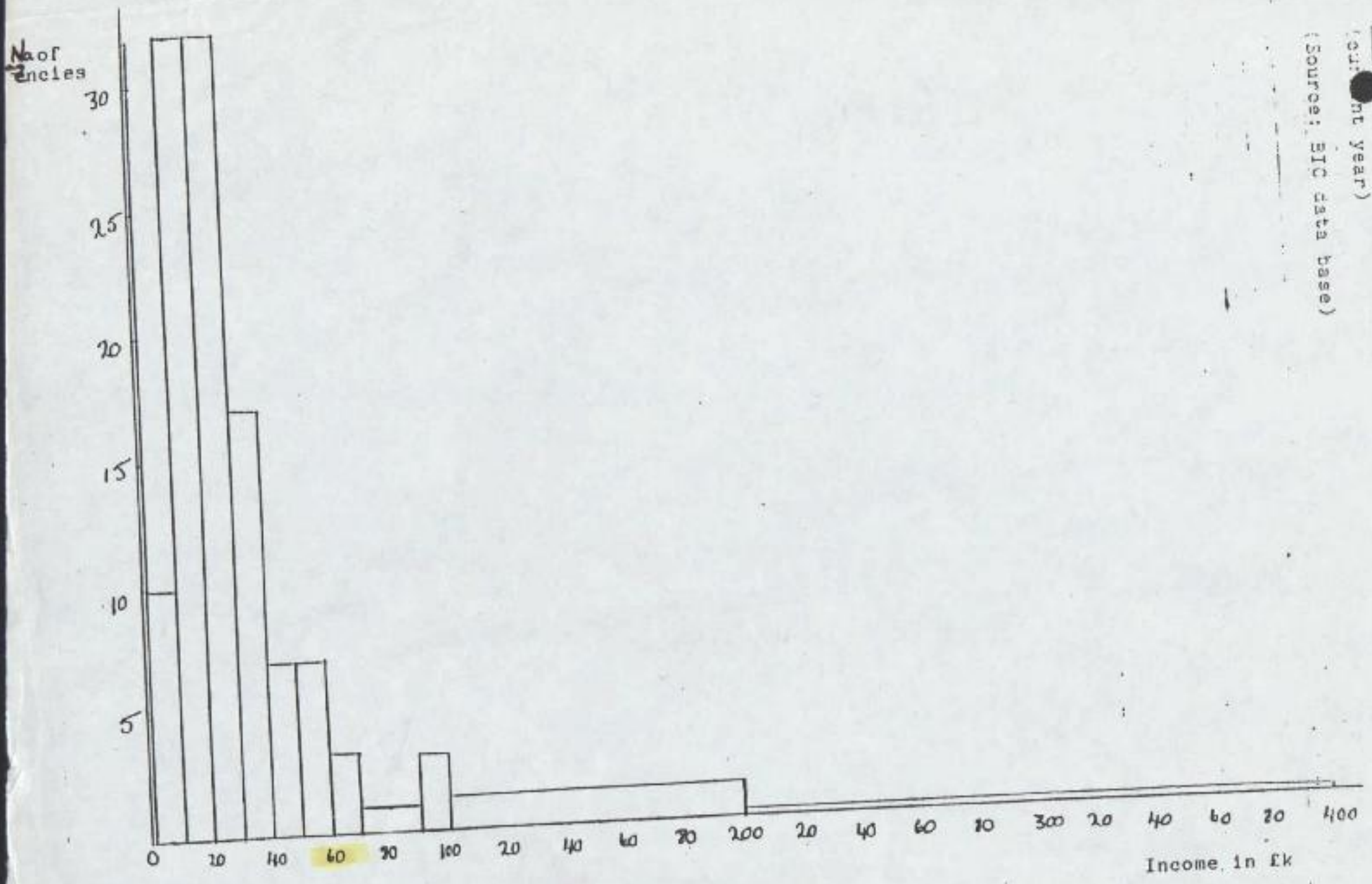
25. It is not recommended that there should be any public recognition of these exclusions. But Ministers should note that by no means will all of the 260 plus agencies recognised by DE be eligible for support.

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DISTRIBUTION OF LEA INCOME

(Current year)

(Source: SIC data base)







20

N. HAM.

NORTHERN IRELAND OFFICE  
WHITEHALL  
LONDON SW1A 2AZ

Minister of State

John Selwyn Gummer Esq MP  
Pay Master General  
70 Whitehall  
LONDON SW1A 2AT

13 August 1985

Dear John,

#### SMALL FIRMS SEMINARS BY MEMBERS OF PARLIAMENT

Your recent correspondence with David Trippier regarding the proposal that Members of Parliament should be encouraged to organise local information seminars in their constituencies to heighten awareness of the services available to assist small businesses has been copied to me.

The importance of small firms in developing the economy of the United Kingdom cannot be overstated and this initiative, which seeks to involve Members of Parliament in English constituencies of all shades of political opinion in a positive and practical way, has my total support.

Whilst the proposal envisages lobbying MPs in England its extension to the rest of the United Kingdom is worthy of consideration. The position in Northern Ireland does not fully reflect that in the rest of the United Kingdom in that there has been greater movement towards developing a single focal point for assisting small business development. The Local Enterprise Development Unit (LEDU), Northern Ireland's Small Firms Agency, is almost unique in this respect within the UK and has developed comprehensive range of assistance, both financial and advisory, designed to meet the needs of this important sector of the Province's economy. LEDU has long recognised the difficulties experienced by the small business sector in understanding the wide range of assistance on offer and actively pursues a strategy designed to increase the awareness of the services available. To this end a regular feature of the Agency's activities is the organisation of information seminar and clinics, analogous to those proposed by David Trippier, aimed at providing small businessmen with a greater understanding of the services that are available to assist them. This coupled with two recent major publicity campaigns undertaken by the Agency has greatly increased awareness of the services available, resulting in a trebling of enquiry rates to LEDU during recent years and as a further consequence a similar uplift in the Agency's job promotion figures.

.... /

...../

In view of this success and the conscious policy we have pursued to focus attention on LEDU as a "one stop shop" for assisting small businesses, I would be concerned that the holding of additional seminars by local MPs, alongside LEDU's carefully planned programme of analogous events, might serve to confuse rather than heighten awareness of the services available. I am also aware from the close involvement of other Ministers and myself in the day to day economic life of the Province that there is already a high level of awareness and this has been re-inforced by the results of a recent market research survey. I have, therefore, come to the conclusion that to replicate David Tripper's proposal and involve MPs from the Province in organising seminars would not significantly add to this level of awareness. I would, however, be very interested in the outcome of the initiative on the mainland and would be happy to reconsider the value of replication in the Province if convinced that it could have beneficial results here in terms of greater economic activity and accelerated growth of the small firms sector.

I am copying my letter to members of E(A) and other recipients of yours.

*All good work*

*Yours*

*Rhe*

DR RHODES BOYSON, MP.



Gen 101  
Small firms  
pt 6



010



NDPM  
AS 127

CABINET OFFICE  
70 Whitehall,  
London SW1A 2AS  
Telephone 01-233 3340

12 July 1985

Dear Annabel,

SMALL FIRMS SEMINAR BY MEMBERS OF PARLIAMENT

*will request if required*

The Paymaster General was grateful for Mr Trippier's letter of 4 July. He has asked me to say that he is content with the approach set out in it.

I am sending copies of this letter to the Private Secretaries to the members of E(A), the Ministers of State at the Welsh Office and the Northern Ireland Offices, the Parliamentary Under-Secretary of State, Scottish Office, and to Richard Hatfield (Cabinet Office).

*Yours sincerely,*

*Alex Galloway*

A. K. GALLOWAY  
PRIVATE SECRETARY



Miss Annabel Gouling,  
Private Secretary to Mr Trippier,  
Department of Trade & Industry,  
1 Victoria Street,  
London, S.W.1.





DA

10 DOWNING STREET

*From the Private Secretary*

1 July 1985

The Prime Minister has seen your Minister's minute of 25 June about local enterprise week. She was very grateful to Mr. Trippier for sending her the encouraging report.

(Mark Addison)

Paul Madden, Esq.,  
Department of Trade and Industry.

SPW

PRIME MINISTER

The attached note from the Minister for Small Firms is a report on this year's local enterprise week. It is an encouraging one, though it is always difficult to establish the lasting impact these initiatives have.

Content that I should reply on your behalf thanking Mr Trippier warmly for the encouraging report.

Yes not

Mark Addison

MARK ADDISON

28 June 1985



cc/PW



PRIME MINISTER

**LOCAL ENTERPRISE WEEK**

Early indications are that this year's Local Enterprise Week (15-24 May) was even more successful than last year. I travelled 3,000 miles and visited over 40 locations during the 10 day 'Week' and I found the interest and involvement shown by local organisations extremely encouraging. Something over 1,000 separate events of various kinds were held throughout the country, virtually all of which were arranged by the local organisations themselves.

2. The Week provided an opportunity to show the extent of community involvement in the small firms sector. Local enterprise agencies, business clubs, local authorities, chambers of commerce and others, supported where necessary by the Department's Small Firms Service, responded well. I am confident that most of them found it worthwhile.

3. A particular theme this year was the importance of links between small firms and the education and training establishments in their area. I was grateful to Peter Brooke and to the DES for their help in launching the Week, and in encouraging schools and colleges to participate. It must be said that some had difficulty in organising and promoting attractive events, but their willingness to become involved was welcome and I think that they learnt a good deal from the exercise.

4. I was unable to visit Scotland myself this year but Allan Stewart undertook a number of engagements covering the full range of his industrial and education responsibilities. Allan tells me that the Week was highly successful in Scotland with over 80 events taking place, including the opening of the new SDA Small Firms Information Centre in Edinburgh.

cont/...

D15AAW



2.

5. As before, the Week was widely covered by the media, particularly at local level. Regional television, radio and newspapers were present at many of the events I was able to attend. The vast majority of the media coverage was supportive and the Week's strong emphasis on local initiatives proved to be an important factor in securing a positive reaction from the local press.

6. I am currently considering how best to keep up the momentum next year. In order to ensure that the initiative is still seen as fresh and vital, we may opt for a slightly different format, rather than simply repeating Local Enterprise Week. Industry Year 1986 presents a very good opportunity to develop a series of regional and national events focusing on small firms issues.

A handwritten signature in black ink, appearing to read 'D.T.', with a horizontal line underneath.

25 June 1985

DAVID TRIPPIER

D15AAW





CABINET OFFICE

70 Whitehall London SW1A 2AS Telephone 01-233 3299

*From the Minister without Portfolio*  
The Rt Hon Lord Young of Graffham

John Mogg, Esq.,  
Private Secretary to the  
Secretary of State,  
Department of Trade & Industry,  
1 Victoria Street,  
London, S.W.1.

15th May, 1985

Dear John

**DEREGULATION**

Lord Young will be speaking about his deregulation responsibilities tomorrow at the annual lunch of the Association of British Chambers of Commerce.

In connection with this speech, he has agreed to contribute a signed article to The Times to appear on Friday. I attach a draft. I should be grateful for any comments which you have on the article by 10 a.m. tomorrow please. I am sorry for the short notice.

I am sending copies of this letter, with a similar request for comments, to Andrew Turnbull (No. 10), Alan Davis (DoE), Peter Ricketts (FCO), Stephen Godber (DHSS), Richard Allan (Department of Transport) and Helen Goodman (Financial Secretary's office).

Yours ever

Leigh

Leigh Lewis  
Private Secretary

## Times Article

Deregulation is in the air. There are articles in the press, debates in Parliament, discussions at the last European Council (at the instigation of our Prime Minister). I am chairing a group of Ministers and there is talk of a White Paper before the summer. Why? Because the real cause for concern today is employment, about creating the conditions that will reduce the number of the unemployed in the shortest possible time.

It is not as if we are not creating jobs - we are, and probably faster than any nation in Europe. It is about encouraging enterprise and creating jobs even faster so that we might share more of the success of the Americans.

So earlier this year I went to Washington to see what it was that they had done to get employment going. And once going to keep it there. For with all their dynamism they were worried that they might slow down. So some years ago they started on a drive to reduce regulation. It was not easy but they did begin to win. If you compare President Reagan's first 23 months with the last 23 months of his predecessor than the rate of increase in what they call the Federal Register, that is the list of new Federal regulations, was down by nearly a third!

This is not just theoretical. The savings in costs across the U.S. economy amounted to some \$9 to 11 billion with a further annual saving of some six billion dollars. But even more important the President was able to report to Congress that in 1982 and 1983 business startups in the deregulated sectors rose at twice the rate of startups in the general economy.

But what is deregulation. Two things essentially. First it is about freeing the market and increasing competition. Do you remember the Trimphone? There was a time when BT gave you a choice - the Trimphone or nothing! Today the vast choice of telephones and services available to you and me are not the fruits of privatisation but of deregulation. Look at Car telephones, although we now call them Cellular radio. Only a few days ago Arthur D Little estimated that there would be over half a million lines by the end of the decade - and by then they will be cheaper than ordinary phones! Once again due only to deregulation.

The deregulation of the long distance coaches has done more to help both the occasional traveller and the distance commuter than any other measure since the war, if not during this century. Prices are often only a fraction of what they were before, and the deregulation of the buses should have the same effect.

Only a few months ago it took weeks to get even simple reading glasses. You could get them in an hour or two in some countries. But not here. Today I see shops advertising glasses in 24 hours. A few more weeks, a little more competition and I do not doubt that we will be back to an hour or two. Once again deregulation.



But deregulation also means lifting the burdens on business and here we still have much to do. Do we still need rent control? We can see shortages of skilled people developing in parts of the South - can we afford to deny the chance of a job to some one who is prepared to "get on his bike" but who just cannot find a place to live because it cannot be rented. Do we need the same system of town planning? The Use Class Order which regulates the use of buildings was introduced just after the War - and was based on Industrial Classifications of 1875. I suspect that we have changed more in the last 10 years than in the hundred before that, but whenever we changed we certainly cannot afford to stand still.

And is it any wonder that our national pastime, it sometimes seems to me, is no longer cricket but Public Enquiries. We had some of the first Nuclear Power stations - the French now have by far the largest industry and are in a position to gain valuable export orders. How long should our road network take to plan? And then build? (Will we ever have an Archway extension, or will the A40 ever be complete?)

Not all of this is regulation, but much of it is. Of course not all regulation should be abandoned, but what we have to ask ourselves is what can we afford to keep? What we must realise today is that we have to strike the right balance between liberty and licence. Enough liberty to let our initiative and enterprise free to create the wealth we need for a truly caring society - but not the licence to abuse our fellow man.

All regulation has a cost. Today, are there too many of our fellow citizens being denied the opportunity to work to justify that cost? That is what I hope to discover during the next few weeks and months. Government, in the shape of Ministers and Officials, are not the best judge of where too many regulations lie. You are, for you live and work with them. The voice of business, both large and small, must be heard. Deregulation is not a panacea for all our ills. But I suspect that too many regulations is one of them.

**CONFIDENTIAL**

## PRIME MINISTER

## REPORT OF THE MINISTERIAL GROUP ON SMALL FIRMS (E(A)(85)23)

I shall not be present when this paper is considered by EA, but you are aware of my interest in the health and increase of small firms, so I am strongly in favour of the report's general approach.

2. Paragraphs 34 and 35 of the report (on page 20) are particularly directed to the education system.

3. The recommendation in 35.1 relates to TVEI and connected in-service teacher training. A number of projects are attempting to link schools with small firms but this is, of course, more difficult than dealing with large employers. We are considering how such developments can be fostered - and I hope to report in the autumn what I intend doing to increase the spread.

4. The new £25 million TVEI-related in-service training scheme, announced on budget day, includes as one of its aims training to promote understanding of industry and commerce. Here again there is scope to encourage greater emphasis on small businesses and we will reinforce this message to MSC.

5. Paragraph 35 (ii) of the report relates to higher education in universities and polytechnics. My imminent Green Paper on Higher Education emphasises the importance of the relationship between higher education and the economy. As you know, we have very different channels of communication with the universities and public sector, but it is already clear that some institutions



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are emphasising to their students the potential of small firms for providing jobs and opportunities for equity participation. This is a message that can be emphasised in the context particularly of any general announcement about small firms.

6. There is also the contribution which sandwich and part-time education can make, particularly in the public sector, by keeping undergraduates in contact with practical approaches towards problem solving at work. Part-time courses are being encouraged through the National Advisory Body for this and other reasons. I am also about to receive the report of a Committee that has been examining the costs and benefits of sandwich education and I will want to consider, in the light of that, whether more can be done in relation to small firms and generally to increase the scope and effectiveness of sandwich courses.

7. I am sending copies of this minute to members of E(A) and Sir Robert Armstrong.

ly

15 May 1985.



P.01539

CONFIDENTIAL

PRIME MINISTER

FLAG A

Report of the Ministerial Group on Small Firms  
(E(A)(85)23 and 27)

FLAG B

BACKGROUND

The Ministerial Group on Small Firms (MISC 108) was established in October 1984 under Lord Young's chairmanship to review the Government support and assistance available to small firms and to make recommendations to E(A) on making this support and assistance more cost effective and about new measure to encourage such firms. The terms of reference extended to both financial and non-financial measures, although only within existing resources.

... Lord Young's Note (E(A)(85)23) covers the Group's report. Its recommendations were fully agreed in MISC 108 apart from (a) Treasury reservations about those directed towards taxation policy, and (b) dissent by the Department of the Environment (DOE) and the Ministry of Agriculture, Fisheries and Food (MAFF) from a recommendation about the future of the Council for Small Industries in Rural Areas (CoSIRA). The recommendations would, however, require £21m to be spent in England over five years, and no off-setting savings were identified.

FLAG C

2. Lord Young's minute of 24 April sought the endorsement of E(A) colleagues to those recommendations which had been fully agreed in MISC 108, so that a package could be announced during local enterprise week (13-20 May). You ruled that no announcement could be made until the method of financing had been resolved (Mr Turnbull's letter of 2 May). Those members of E(A) who did write, however, indicated general support for the agreed recommendations. It therefore remains for E(A) to decide whether resources should be found, and if so from whom, and to resolve the outstanding reservations on certain recommendations.

3. The Secretary of State for the Environment's paper





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..... (E(A)(85)27) explains the reasons why his Department dissented from the recommendation about CoSIRA.

MAIN ISSUES

4. The main issues are:


(i) whether the Group's recommendations are of sufficient priority to warrant their immediate implementation, and if so, whether the necessary finance should be secured through off-setting savings or by drawing on the Reserve (the latter course being in conflict with the Group's terms of reference);

(ii) whether when the Business Expansion Scheme (BES) is reviewed later this year particular attention should be given to the problems of small firms in raising venture capital;

(iii) whether there should be a review of the case for transferring CoSIRA and its parent body the Development Commission from DOE to DTI.

The MISC 108 Report

5. The Group started from the point that small firms represent a flowering of enterprise and are an important potential source of new employment. Their assessment - although the evidence is by no means clear cut - was that small firms are making a substantial and probably increasing contribution to job and wealth creation, but that further encouragement is needed to realise the potential of the small firm sector. The Group reviewed and made recommendations in five areas: the provision of information and advice; finance; education and training; access to public and private sector markets; and the provision of premises.




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6. For the most part the recommendations are unexceptionable. They are aimed at ensuring that small firms are not disadvantaged in, for example, seeking public sector contracts, although they do not go as far as advocating positive discrimination. The Group implicitly recognised that small firms can only prosper if they can produce marketable products or services at competitive prices, and that the Government's role should be limited to providing advice and encouragement and otherwise not getting in the way. MISC 108 covered half the ground; the Group on Deregulation (MISC 114), due to report in July, will produce other measures designed to help small firms.

Local Enterprise Agencies (LEAs)

7. The Group saw the LEA movement as best placed to provide the local focus for meeting small firms' advisory needs. Although some LEAs receive some public funding, they rely mainly on private sector initiative to draw together elements of the local community to support the development of the local economy. There are now 230 agencies in the UK, under the general umbrella of Business in the Community (BIC). The Group recommended that in order to extend and strengthen the network of LEAs the Government should provide funding of up to £20,000 a year for individual LEAs for up to five years, on a tapering scale, and on condition that matching funds were available from the private sector. This would cost £5m in the first two years, falling to £2½m. The Government's own advisory service, the Small Firms Service (SFS), would increasingly operate through LEAs, and would concentrate more on 'up-market' services which are less likely to be immediately available locally in the private sector. The development of a number of specialist services in the SFS and other minor related recommendations would take the total cost in the first year to £6m.





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8. The condition that LEAs would have to raise half their resources from the private sector should oblige them to prove their continuing relevance to their local communities. The initial Government funding should give them the opportunity to become established, but there would be a risk that LEAs would not be able to continue after the initial period without some further Government or local authorities funding.

9. Although all the Ministers who have commented have welcomed this approach in principle, none of them have so far given it sufficient priority to offer to divert resources from existing programmes. In principle, the case for extra support for small firms should be considered together with all other new bids in the Public Expenditure Survey in the Autumn, and the <sup>Trade and</sup> Industry Secretary will be making a bid accordingly. If the Sub-Committee accepts, however, that an announcement of the MISC 108 package should be made now, it will be necessary for members to give guarantees that the funds will be found. Government expenditure on information, advice and training for small firms totals only £25m a year, so the scope for a substantial switch within this part of the DTI programme is not great. It appears, however, that the Minister for Industry will be in a position to offer some contribution from his Department's other programmes towards the total amount needed if the other Departments concerned - DOE, Department of Employment and MAFF - are similarly prepared to offer contributions.

Finance for Small Firms

10. The majority of the Group accepted that very small firms face difficulties in raising equity capital in amounts of £50,000 or less. They therefore suggested that a number of changes in the Business Expansion Scheme (BES) and the Capital Gains Tax (CGT) rules should be made to encourage investment in such amounts.





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The Treasury, however, argued that there was no particular difficulty in raising finance - rather the problem was a shortage of worthwhile ideas. More specifically they objected to a number of the detailed suggestions on the grounds that they would give unintended tax concessions over a much wider field, and that if anything were to be done, the decisions would need to be taken by the Chancellor in the context of the Budget, against competing claim for tax concessions of this kind. Lord Young indicated in his minute of 24 April that he accepted it was inappropriate for MISC 108 to be involved in the BES review, and it is therefore possible that this will not now be raised at E(A).

11. The proposal that the Enterprise Unit should be involved in the future of the Loan Guarantee Scheme (LGS) later this year has been accepted by the Secretary of State for Trade and Industry. It should be noted, however, that there is no PES cover for the LGS beyond the end of this year, and it is therefore an issue likely to feature in the PES round in the Autumn. The other recommendations about finance for small business are generally concerned with Government efforts - without any specific new subsidies or tax concessions - to induce pension funds, life insurance companies, etc to be more active in taking equity stakes in developing small businesses.

#### CoSIRA and the Small Firms Service

12. CoSIRA, part of the Development Commission (DC), provides advice to small firms in rural areas, while the SFS provides advice in the rest of England. MISC 108 suggested, with DOE and MAFF dissenting, that further consideration should be given to improving the arrangements for liason between the SFS and CoSIRA, perhaps through the transfer of the DC, with CoSIRA, to DTI.

13. From the point of view of small firms policy it clearly makes sense for CoSIRA and the SFS to work closely together. But as the Secretary of State for the Environment's

Flag B.





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paper points out, the DC also has a whole range of responsibilities for other rural problems other than industrial development; and it seems unlikely that rural communities would be able to generate the resources need to support the effective LEAs which would be needed to take CoSIRA's place in the longer run. When the problem was last reviewed by DOE and DTI as recently as 1983 it was agreed that the DC should remain with DOE, who have general responsibility for the Countryside Commission and Nature Conservancy Council. It may in practice be easier to achieve effective co-ordination of business advisory services across departmental boundaries than to bring together two separate Departmental approaches to policy towards rural areas. Mr Jenkin has objected even to a reference to a possible review, because it would unsettle the DC and undermine public confidence in the Government's commitment to rural development. He has however conceded (in his letter of 3 May) that there could be a reference in the announcement to an examination of the scope for closer liaison, and this would seem a sensible compromise.

Flog, D...

#### Scotland, Wales and Northern Ireland

14. MISC 108's report is primarily concerned with England. The territorial Secretaries of State will therefore need to review whether any elements need to be implemented in their parts of the United Kingdom. They might be expected to find the necessary resources from their own programmes.

#### Announcement of the package

15. Lord Young wishes to announce the outcome of the work on small firms on the last day of local enterprise week - Monday 20 May. The Sub-Committee will therefore need to review the terms in which any announcement should be made. The Annex to his paper suggests the elements which might be included.

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HANDLING

... 16. You will wish to invite the Minister Without Portfolio to introduce his paper. The Minister of State for Industry might be invited to make general comments and other Ministers (particularly the Secretaries of State for the Environment, and for Scotland and Wales) will have views about the recommendation on local enterprise agencies. The Chief Secretary will want to speak briefly about the need to find offset for any additional expenditure, and you might seek a reaction from the Minister of State for Industry, and perhaps also from the Secretary of State for the Environment and the Minister of Agriculture, Fisheries and Food.

17. You may wish to establish before the meeting whether Lord Young wants to discuss his disagreement with the Chancellor about finance for small businesses. If he does, the Chancellor of the Exchequer should be asked to respond.

18. Lord Young might be asked to set out the case for a review of whether the Development Commission should be transferred to DTI, and the Secretary of State for the Environment, with the Minister of Agriculture, Food and Fisheries, putting the opposite view.

CONCLUSIONS

19. You will wish to reach conclusions on whether

(i) the recommendations of the MISC 108 report (other than those concerned with the BES) should be endorsed, and in particular those relating to the role of LEAs;

(ii) the work of the LEAs commands sufficient priority to warrant an immediate commitment to additional Government spending in advance of the 1985 Public Expenditure survey, and if so from which programmes offsetting savings should be made;

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(iii) (if necessary) any specific guidance should be given to the Chancellor of the Exchequer about the needs of small firms for equity finance, which he would take into account in reviewing the Business Expansion Scheme;

(iv) there should be a review of the scope for closer co-ordination between the SFS and CoSIRA, and if so whether this should extend to the possibility of transferring responsibility for The Development Commission from the Department of the Environment to the Department of Trade and Industry; and

(v) the Minister Without Portfolio should announce the agreed features of the package on Monday 20 May.

*PLG*  
P L GREGSON  
14 May 1985

LOCAL ENTERPRISE WEEK

Background

The fact that this is Local Enterprise Week may prompt hostile or favourable questions, as last week from Peter Thurnham.

Points to make might include

i) Small firms employ about 25% of the total workforce, and 36% of private sector employment. They account for some 20% of GNP. But the most dynamic economies eg the USA and Japan have a higher proportion of small firms.

General Point

Under this Government the climate is improving:

ii) Self employment has risen by about 500,000: from 7.5% of the employed work force in mid 1979 to 9.5% in mid 1983 and higher today.

iii) There were over 100,000 more UK firms in 1983 than in 1979.

iv) This Government has substantially reduced the burden on small firms. It has reduced the small firms' rate of corporation tax from 38 - 30% and abolished the National Insurance Surcharge.

v) The Government has a wide range of measures for assisting small firms starting up:

- the Enterprise Allowance Scheme is now helping 1,250 people each week start their own business with a very high success rate.



- some £75m was invested by 10,000 individuals using the Business Expansion Scheme in the first year.
  
- During 1983/84 the small firms service dealt with over 300,000 enquiries and arranged 28,000 counsellor sessions.



Secretary of State

NOR  
BT 1515 C 022  
Northern Ireland Office  
Stormont Castle  
Belfast BT4 3ST

The Rt Hon Lord Young of Graffham  
Cabinet Office  
70 Whitehall  
LONDON SW1

13 May 1985

Dear Minister,

Thank you for sending a copy of your minute of 24 April 1985 to the Prime Minister on the proposals arising from MISC 108.

I welcome the work undertaken by the Group and the positive recommendations to assist small firms made in the Report. I accept that most of these recommendations are aimed primarily at activities in Great Britain and, although the Report acknowledges the greater progress made in Northern Ireland towards the realisation of the "one-stop shop" concept, I would nevertheless wish officials in Northern Ireland to examine the Report carefully with a view to implementing those recommendations which would benefit the Province.

I am content with the recommendations and your proposal to announce the package during Local Enterprise Week.

I am copying this letter to members of E(A), Keith Joseph and Sir Robert Armstrong.

PTS (in E(A) Folder)

hcc:

- PS/SOS (B&L)
- PS/Dr Boyson (B&L)
- PS/PUS (B&L)
- PS/Mr Bloomfield
- Mr Brennan
- Dr Quigley
- Mr Barry
- Mr Parkes
- Mr Fell
- Mr Stutt DED
- Mr Cowling
- Mr Bickham

cc: as last para.

Yours sincerely,

Peter Cleary

(Private Secretary)

(Approved by Secretary of State & signed in his absence)



Ecce in PT 6

Small items

75 MAY 1985

1000

E (A) folder

MR TURNBULL

10 May 1985

MISC 108

Small firms are important: arguably they have been responsible for half the new jobs created over recent years, and produce five times as many new jobs per head employed as do large firms. The MISC 108 report is workmanlike but makes no major discoveries. The important thing is to keep promoting the enterprise culture: in schools, universities and life at large.

The main proposal is greater support for Local Enterprise Agencies (approximately £20 million over next five years). This is good politics and should also result in less bureaucracy and better advice to budding entrepreneurs. It should allow DTI to concentrate on co-ordinating interdepartmental inputs to the LEA's and in providing the more complex advice. In effect the gradual privatisation of the Small Firms Service as presently constituted. It will cost money in the short term but we ought to save it in the long term.

The report also recommends that the Development Commission and CoSIRA should be transferred from the DoE to the DTI. Administratively this may be sensible but would not be worthwhile if it provokes strong departmental opposition.

We recommend you support the LEA proposal, and if necessary be prepared to accept the £6m first year costs as additions to the PES (this can easily be financed by changes to the small firms corporation tax rate) but look for subsequent years to be funded in whole or part by savings within DTI.

*Peter Warry*  
PETER WARRY





SCOTTISH OFFICE  
WHITEHALL, LONDON SW1A 2AU

CENO  
NRP  
AT  
BT

CONFIDENTIAL

The Rt Hon Lord Young of Graffham  
Minister without Portfolio  
Cabinet Office  
Whitehall  
LONDON  
SWA 2AS

7 May 1985

Dear Minister,

MISC 108

with AT?

Thank you for sending me a copy of your minute of 24 April to the Prime Minister about the report of the above Group.

As you have indicated in the report, in the main, the recommendations address the situation in England, and its implications for Scotland will be a matter for discussion between us in due course. However, at this stage I can say that generally speaking I am content with what you propose. The central concept of concentrating support for small firms at the local level is acceptable to me, although I would have reservations about using precisely the same system as you propose for England because of the role in Scotland of the Highlands & Islands Development Board and the Scottish Development Agency (SDA). While the SDA gives funding and other support to a number of Enterprise Trusts, some of the rural areas of Scotland, and in particular the Highlands and Islands, are without Trusts because of the difficulty of raising private sector funding.

On finance, I am particularly pleased to see that you recommend an evaluation of the Enterprise Funds for Youth loan scheme. It is my intention to contact a number of the Local Enterprise Trusts who are involved with the running of the scheme in Scotland, and I shall, in due course, let you have our views to help in that evaluation.

Finally, I note that you will be announcing a number of the report's recommendations during Local Enterprise Week. As you know, we too are involved in a number of promotional ventures during that week and it would be useful if you could let me have advance notice of announcements in order that we can give a Scottish dimension to Ministerial speeches etc.

A copy of this letter goes to members of E(A), to the Secretary of State for Education and Science, and to Sir Robert Armstrong.

E S GOWANS  
Private Secretary  
Approved by the Secretary of State  
and signed in his absence

Small Firms: Leon Pol. Pt 6.

18/10/1958

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4 5 6 7 8 9 10





CONFIDENTIAL

DEPARTMENT OF TRADE AND INDUSTRY  
1-19 VICTORIA STREET  
LONDON SW1H 0ET 5422  
TELEPHONE DIRECT LINE 01-215  
SWITCHBOARD 01-215 7877

Secretary of State for Trade and Industry

7 May 1985

The Rt Hon Lord Young of Graffham PC  
Minister without Portfolio  
Cabinet Office  
Whitehall  
LONDON  
SW1

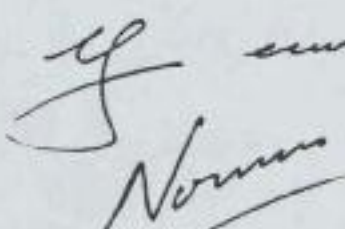
R. David,

Your minute of 24 April to the Prime Minister sought colleagues' agreement to the MISC 108 proposals and to the announcement of a package during Local Enterprise Week.

2 As you know, I endorse the central idea in the report of help for small firms being concentrated at the local level, I am not able to find offsetting savings towards the cost of the proposals. I am submitting additional bids for the forthcoming PES round to accommodate certain of the MISC 108 proposals - notably those for the Enterprise Agency Support and for a Marketing Advisory Service but unless Nigel Lawson is prepared to provide new money for these additional bids without requiring offsetting savings I do not see how an early announcement on the work of your group can be made.

3 You also ask if your Enterprise Unit could be involved in discussions on the future of the Loan Guarantee Scheme. I am content with this but I should make clear that there is no DTI PES provision for any further extension of this Scheme.

4 I am copying this letter to the Prime Minister, Members of E(A), Sir Keith Joseph and Sir Robert Armstrong.

  
NORMAN TEBBIT

JH4BBF

*RL*

MR SHERBOURNE

3 May 1985

PAPER BY PROFESSOR JOHN VINCENT ON ENTREPRENEURSHIP

He is right that entrepreneurship is important. Hence the Small Business Cabinet Committee under David Young and the frequent references in speeches and indeed in the Employment White Paper to the importance of enterprise.

Yes, the EAS needs to be expanded and marketed aggressively - agreement has already been reached to do just that. And yes, starting entrepreneurs need equity, not loans. Then why does he suggest an SBIC type method where borrowings are made available for small businesses - and does he know that the American experience of bad debts has been so bad that they are now contemplating winding up the whole programme. Our own loan guarantee system which mimics the American idea has also been very disappointing and is having to be controlled.

The main problem seems to be the lack of tax relief for people wishing to invest in a venture capital fund. We are working with the Financial Secretary on this taxation question.

DTI have recently re-packaged their measures of assistance to small business and entrepreneurs, and although they have not fully privatised it they have greatly simplified the system. They would be reluctant to go further.

The target group approach has much more novelty and I think is most interesting. I will incorporate these thoughts into a note to the Prime Minister along with Michael's scheme for job creation awards.

  
JOHN REDWOOD



# Small Guns

July 1954

Small Guns

## REPORT OF THE SMALL GUNS COMMITTEE

The Small Guns Committee was established in 1953 to study the problem of small arms in the United States. It has since that time held numerous public hearings and has received many suggestions from interested citizens. The Committee has also conducted extensive research into the various aspects of the small arms problem, including the production, distribution, and use of small arms in the United States. The Committee believes that the small arms problem is a serious one and that it is essential that the Government take prompt and effective action to deal with it. The Committee's report contains a number of recommendations which it believes will help to solve the small arms problem in the United States.

The small arms problem in the United States is a complex one. It involves a wide variety of factors, including the production, distribution, and use of small arms. The Committee believes that the small arms problem is a serious one and that it is essential that the Government take prompt and effective action to deal with it. The Committee's report contains a number of recommendations which it believes will help to solve the small arms problem in the United States.

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cc JR

PRIME MINISTER

MINISTERIAL GROUP ON SMALL FIRMS (MISC 108)

AS

I have read David Young's minute to you of 24 April, outlining the recommendations of the group he chaired on small firms (MISC 108).

I support MISC 108's recommendations and think that the proposals will be generally helpful in contributing to the 'enterprise culture' we are seeking.

I note that David's measures put particular emphasis on improving information and advice to small firms. I accept there is a limit to other measures we can take without incurring unreasonable costs. But by the same token I think that in putting forward our proposals we should not unduly raise expectations on the effects they will have on small firms and the economy generally.

The best contribution we can make is to create as many new openings for small firms as we can. This I am trying to do through bus deregulation, airline policy, and contracting out in Nationalized Industries.

I am copying this minute to members of E(A), to the Secretary of State for Education and Science, to David Young and to Sir Robert Armstrong.

NICHOLAS RIDLEY

3 May 1985

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Small Airmail



-7 MAY 1985

D for ERM meeting D Cgto



2 MARSHAM STREET  
LONDON SW1P 3EB  
01-212 3434

My ref:

Your ref:

3 May 1985

Dear Lord Young

## MINISTERIAL GROUP ON SMALL FIRMS: REPORT TO E(A)

In your minute of 24 April to the Prime Minister you invited colleagues to confirm their agreement to the MISC 108 recommendations (contained in E(A)(85)23) and the package you intend to announce in "Local Enterprise Week", indicating any areas of disagreement.

The Group's recommendations do I believe represent a very positive approach to the problem of small firms, even though as you say the ground has been well tilled.

I welcome particularly the proposal to build up local enterprise agencies, though of course more work still needs to be done to develop the policy fully. Success will depend particularly on local initiatives, encouraged and supported by staff in the Department's Regional Offices. My staff will continue to play an effective role - they have been instrumental in setting up a fair number of agencies in urban areas - but the main burden will fall on others. We must have some assurance that they are willing and able to take this on. It is important also that we do not deny ourselves all reasonable means to help with the problems of establishing effective agencies in some of our inner city and more remote rural areas. Para 9 of Annex F refers to the special difficulties. I cannot therefore go along wholly with the recommendation in para 23(ii) of the Group's report if this would remove the flexibility we now have to use small amounts of money eg from the urban programme or the Development Commission to help in exceptional circumstances where the private sector is weak.

On public procurement, we are also pressing ahead with measures to improve tendering arrangements for small firms.

Work is in hand as you know on simplified planning procedures and improved guidance on setting up a business from home. MISC 114 will of course be looking at a number of these issues in the deregulation context. Also efforts are being made to encourage more private funding of small premises.

I agree that the proposed review of whether or not the Development Commission and the Council for Small Industries in Rural Areas should be transferred to the Department of Trade and Industry will have to be discussed at E(A). Until we have reached agreement



On the way ahead there should be no reference to such a review in any public announcements. To do otherwise would needlessly undermine public confidence in these bodies. I would however have no objection to a reference in the announcement to closer liaison between COSIRA and the Small Firms Service in terms just slightly different from those in your draft:

"- scope for closer liaison between COSIRA and Small Firms Service will be examined. Result to be announced later this year."

I am content otherwise with the proposed text of the announcement.

The Chief Secretary has asked where offsetting savings can be found. As Norman Tebbit proposes, I think we should keep an open mind on this until later in the PES round.

Copies of this letter go to the Prime Minister, other members of E(A), Sir Keith Joseph and to Sir Robert Armstrong.

*Your sincerely*

*Atkin*

*for*

PATRICK JENKIN

Approved by the Secretary of  
State and signed in his absence

ECON POL: Small Firms, Pt 6

5 MAY 1989

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CABINET OFFICE

From the Chancellor of the  
Duchy of Lancaster  
Lord Gowrie

MANAGEMENT AND PERSONNEL OFFICE  
Great George Street  
London SW1P 3AL  
Telephone 01-233 8610

The Rt Hon Lord Young of Graffham  
Minister without Portfolio  
Cabinet Office  
70 Whitehall  
LONDON SW1A 2AT

2 May 1985

*See para 1*

MINISTERIAL GROUP ON SMALL FIRMS: REPORT TO E(A)

In your minute of <sup>in AS</sup> 24 April to the Prime Minister you asked for confirmation of agreement to the package of recommendations on Small Firms set out in E(A)(85)23.

I am sure it is right that we should seek to develop the Local Enterprise Agency (LEA) network on the lines set out by MISC 108. Given the patchy performance of some of these Agencies in the past there is something of a risk in this. But it is consistent with our approach generally that we should seek to encourage a local "self-help" approach to the needs of small firms and it seems entirely appropriate that we should provide pump-priming assistance to such initiative. For best results it will be essential to delegate the administration of the scheme to DTI's regional organisation as proposed in the report.

I note that the Group's recommendations on financial assistance to small firms and on the Development Commission and CoSTRA will be discussed separately.

I am content with the remainder of the Group's recommendations, subject to the following comments in respect of some of those on public purchasing (paras 38 and 39 of the report). As regards the recommendation on departmental databases (para 39 (v)), my own view is that departments are unlikely to be able to make very rapid progress in this area. Our feedback from

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departments on the report on Government Purchasing indicates that departmental databases are generally not yet well developed and it will take some time to make them so. We should be cautious of promising too much too quickly in this area.

Paragraph 39(vii) of the report invites DTI to complete their review of the US Small Business Innovation Research programme (SBIR). I hope that the Central Unit on Purchasing, when established, can be associated with this review. The recommendations in paragraphs 39(i) and 39(x) place requirements on the head of this Unit. The recommendations seem sensible and I anticipate no particular problems in implementing them. Nonetheless, I shall want to discuss them with the head of the Unit, when appointed, to see how they can best be taken forward.

Subject to these points, I am happy for an announcement of the outcome of the Group's work to be made, as you propose, during Local Enterprise Week.

I am copying this letter to the Prime Minister, members of E(A), to the Secretary of State for Education and Science and to Sir Robert Armstrong.

GOWRIE

*Handwritten marks:*  
 A small flourish above the name.  
 A wavy line below the flourish.  
 A large handwritten signature, possibly "Gowrie", written vertically.



Leon Pol: Small Ferry A6.

3 MAY 1985

10 11 12 1  
9 8 7 6 5 4 3 2 1



10 DOWNING STREET

From the Private Secretary

Prime Minister <sup>(2)</sup>

You may be interested to see these papers. I agree with the Enterprise Unit that a degree of caution is needed. The US is ahead of us in appreciating the problem and has set up a number of agencies to tackle the agencies. But the evidence that regulation are actually being cut back is, from these papers, rather sketchy.

AP

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bc P. Wainy

10 DOWNING STREET

*From the Private Secretary*

2 May 1985

*Dear Leigh.*

Ministerial Group on Small Firms:  
Report to E(A)

The Prime Minister has seen Lord Young's minute of 24 April and has also seen the exchange of correspondence between the Chief Secretary and the Secretary of State for Trade and Industry. She believes it is wrong for proposals to be made and decisions announced before the method of financing them has been resolved. She hopes this will now be done quickly.

I am copying this letter to Private Secretaries to members of E(A), to Elizabeth Hodgkinson (Department of Education and Science) and Richard Hatfield (Cabinet Office).

*Yours sincerely*  
*Andrew Turnbull*

(Andrew Turnbull)

Leigh Lewis, Esq.,  
Office of the Minister Without Portfolio.

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*lg*



10 DOWNING STREET

Prime Minister ①

The problem is precisely that Mr. Tebbit will not offer savings on his existing provision for small firms, but seeks additional provision for Lord Young's proposals. Hence the disagreement and the deal reached with the Chancellor.

The choice is (either):

(i) agree to let proposals through on this unsatisfactory basis?

or (ii) hold it up, minus Enterprise Week, while financing is settled?

We must settle

the finance first

no AT  
1/5





NOSP  
AS 2/5

MS

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

PRIME MINISTER

**MINISTERIAL GROUP ON SMALL FIRMS: REPORT TO E(A)**

David Young wrote to you on 24 April about the major recommendations which MISC 108 had put forward to E(A). I fully understand why David would like the Government to make a firm announcement about additional expenditure in Local Enterprise Week. But I do not believe we can contemplate spending additional sums without agreeing that offsetting savings should be found.

2. The cost of the measures proposed amounts to £6m in 1986-87. David mentioned that I would, exceptionally, be prepared to agree to an announcement before we had identified specific offsetting reductions. However, I was speaking to him on the assumption that E(A) would have an opportunity to discuss MISC 108's report. If colleagues do generally indicate in correspondence that they want to increase support to local enterprise agencies - the report's main proposal - then I must insist that before we make any announcement, we are all clear that offsetting expenditure savings have to be found elsewhere.

3. I am copying this minute to all the other members of E(A) and to Sir Robert Armstrong.

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

N.L.

1 May 1985

ECON POL Small Firms

MS

-2 MAY 1985

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PART 5. ends:-

AT 10 AM 30/4/85

PART 6. begins:-

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