MANAGEMENT IN CONFIDENCE

cc PS/Chancellor
PS/CST
PS/EST
PS/MST(C)
PS/MST(R)
Mr Middleton
Mr Bailey
Mr Monck
Mr Burgner
Mr Kitcatt
Mr I P Wilson
Mr St Clair
Mr Morgan
Ms Seammen
Mr Pickering

Treasury Chambers, Parliament Street, SW1P 3AG

Minister of State for Defence Procurement
Ministry of Defence
Whitehall
LONDON
SW1A 2HB

2 June 1983

Dear Minister,

ROFS: FUTURE PENSION ARRANGEMENTS

Thank you for your letter of 16 May.

You propose to announce that employees transferring to the new company should have their pensions index-linked if they so wish. I am not convinced by your arguments.

I recognise the importance that Mr Clarke attaches to this issue, and the need to attract staff. But I am wary on two grounds:

i) Watsons' calculations are encouraging. But I do not see how we can accept them without any comment from our own adviser, the Government Actuary. A buy-out could still be cheaper in practice, and would avoid leaving the company with an uncertain liability.

ii) All previous advice has been that index linked pensions would damage future privatisation prospects. You mention ABP; but there was no doubt in that case that index linking materially affected the price received. Rothschilds' advice to you last July was clear on this point; I am surprised that you have not consulted them again.

I suggest that MOD should now seek advice from the Government Actuary and Rothschilds on the above points.

--

Also I fear that I cannot agree to your proposal that the Government should underwrite the pension fund's performance. Such a guarantee would be objectionable in principle, and could further damage future privatisation prospects. Patrick Jenkin has made the point that an assurance could not extend beyond privatisation. Our liability should cease once an adequate transfer payment has been made in respect of past service. Subsequent contributions policy will be a matter for the ROFs and their employees. Moreover, I would hope that the company could avoid formally committing itself to standing behind or guaranteeing the pension fund.

But all this must be deferred until after June 9!

I am copying this letter to Janet Young, Patrick Jenkin and Michael Havers.

yours sincerely

Martin Donnelly

PP NICHOLAS RIDLEY

(Approved by the Financial Secretary and signed in his absence.)

5776.
PS 6/163/82.

FINANCIAL SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

Geraint Morgan QC

8 JUN 1983

Dear Geraint

You wrote to Geoffrey Howe on 12 May about the capital transfer tax consequences of a hypothetical situation in which part of a farming business was given to his children by the owner. As this is a hypothetical case you will appreciate, I am sure, that I can only comment in general terms.

I am afraid that it is not possible to give a simpler answer to the question you have posed for the reasons explained below. Capital transfer tax is charged on the value transferred by a chargeable transfer ie on the loss to the transferor as a result of the gift less any exemptions due. Whilst this loss is normally the open market value of the property transferred plus any capital transfer tax to be borne, the position is different in the case of property such as that featured in your example. It would be worth more in the hands of the transferor than in the hands of the transferee and in this situation it would be necessary to value the transferor's interest in the farm both before and after the transfer.

In the case of your example it is assumed that the gift would be effected by transferring the legal title to the property into the names of the transferor and his two children as tenants in common in trust for themselves as to 50 per cent for the transferor and 25 per cent each for the children. Applying what I have explained above, the value transferred (being the value of the farm with vacant possession immediately before the transfer less the value of the interest retained by the transferor) would reflect the loss in vacant possession. And so far as the open market value of each interest is concerned this would be a matter for the District Valuer, whose agreed values would determine whether the tax thresholds had been exceeded.

But having said all this the probable answer is that no capital transfer tax would be payable in your hypothetical case given that it involves a farm which on the face of it would be eligible for agricultural relief. For land with vacant possession this relief has the effect of reducing the value transferred by 50 per cent. For let land a 20 per cent reduction is similarly applied.

Yours ever

Nicholas

NICHOLAS RIDLEY

FINANCIAL SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

Teddy Taylor Esq
House of Commons
LONDON
SW1A OAA

9 June 1983

Dear Teddy

I am writing in response to your Question of 13 May (about which we spoke on the telephone) in which you asked what was the average annual increase in gross domestic product for the United Kingdom, and for the nations which formerly comprised the European Free Trade Association which did not join the EEC (a) in the period since the United Kingdom joined the European Economic Community and (b) in the years since 1963. As you know, it was not possible to provide a formal answer in the time available before the House was dissolved.

The information is given below. It has been derived from figures in two OECD publications: "National Accounts Volume 1 Main Aggregates 1952-1981" for the years 1963 to 1981, and "Main Economic Indicators", April 1983 issue, for the year 1982.

Average annual percentage increase in GDP at constant market prices

	1963-1973	1973-1982
United Kingdom	3.2	0.5
EEC (present members, excluding UK)	5.0	2.0
EFTA (members which did not join the EEC)	4.4	1.7

Yours ever
Nicholas

NICHOLAS RIDLEY

CONFIDENTIAL

FROM: FINANCIAL SECRETARY
DATE: 15 June 1983

CHANCELLOR

cc Chief Secretary
Economic Secretary
Mr Middleton
Mr Littler
Mr Unwin
Mr Wilding
Mr Battishill
Mr Lovell
Mrs Hedley-Miller
Mr Edwards
Mr Lennon
Mr Fitchew
Miss Court
Mr Peet
Mr Gray
(without attachment)

EUROPEAN COMMUNITY BUDGET: UK POLICY ON 1983 AND 1984 BUDGETS

If we do not withhold, I would be entirely in agreement with the strategy outlined in the attached note for both the 1983 SAB and the 1984 PDB. It would probably be difficult to achieve all our objectives in Council, and it would no doubt lead to a row with the Parliament - but that would be a long way in the future.

But I fear we will be withholding by July 21 - and if I am tolerated at the Budget Council at all, my position will be, to put it mildly, delicate. I would in effect be talking about how other people should spend their money. In addition the arithmetic will be different, because we will have withheld some of the Community's resources. In those circumstances we might have to re-assess our attitude. Our attitude should perhaps be more propaganda-orientated, and we should concentrate more on the absurdity of uncontrolled agricultural spending, making the point as strongly as possible that above all it is the present CAP that has caused the crisis of our withholding. But that can be re-assessed at the time.

Martin Donnelly
pp NICHOLAS RIDLEY

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CONFIDENTIAL

14 JUN 1983

FROM: T LENNON
DATE: 14 June 1983

1. MR UNWIN 2. Financial Secretary (Not attached)
3. CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Economic Secretary
Mr Middleton
Mr Littler
Mr Wilding
Mr Battishill
Mr Lovell
Mrs Hedley-Miller
Mr Edwards
Mr Fitchew
Miss Court
Mr Peet
Mr Gray

(I think the Financial Secretary will wish to have an opportunity of considering a commentary on this before it goes to the Chancellor)

EUROPEAN COMMUNITY BUDGET : UK POLICY ON 1983 AND 1984 BUDGETS

I attach a note which discusses the UK's policy towards the Commission's 1984 Preliminary Draft Budget and the 1983 Supplementary Budget No. 2. We would welcome Treasury Ministers' general endorsement of the approach suggested.

2. The Cabinet Office wish to hold a discussion by senior officials of the UK's strategy next week. They consider it would then be useful to have an inter-Ministerial meeting on this. There may be some merit in Ministerial discussion given that the FCO at official level do not wholly endorse the suggested strategy.

Yours hennon.

T LENNON

The attached note has been prepared after discussion with the FCO & Cabinet Office. The former will not wish us to adopt such a rigorous approach, but, though precise tactics will need to be framed in the light of developments, I see little alternative in present circumstances. It would be helpful to know whether the Chancellor broadly endorses the line we have taken - viz that we should seek to restrict the 1983 supplementary & make substantial reductions in the

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CONFIDENTIAL

EUROPEAN COMMUNITY BUDGET: UK POLICY ON 1983 AND 1984 BUDGETS

1. This note discusses the UK's policy towards the Parliamentary Draft Budget 1984 (PDB) and the 1983 Supplementary Budget No 2. The Commission have just published the 1984 PDB - a broad breakdown is shown at Annex A - and we have some indication of what the 1983 Supplementary might contain although it has yet to be put forward. A timetable for Community discussion of the 1984 PDB is at Annex B. The timing of the 1983 Supplementary is still uncertain, but it is likely to be considered with the 1984 PDB at the Budget Council (provisionally fixed for 20/21 July). It will almost certainty not be published until after the Stuttgart Council on 17-18 June.

Background

2. Our approach to these budgets is conditioned by our overall objectives for Community finances ie a reduction in the UK's net contribution and the introduction of a 'safety-net' limit on this, the maintenance of the 1 per cent VAT ceiling and a reduced share of the budget being taken by agriculture. Our immediate priority must be to ensure that there is adequate headroom in 1984 (and/or 1983) to finance UK refunds for 1983. The European Council has already agreed that the necessary figures should be entered in the 1984 Draft Budget. Community expenditure is however now so close to the own resources ceiling that there is a real danger of UK refunds being "crowded out". Some other member states are already using this argument to link agreement to further refunds to an agreement in principle to create new own resources. A further priority is to ensure that the 1983 Supplementary Budget No 2 includes provision for the outstanding risk-sharing payments (some 0.5 billion ecus) in respect of 1982.

3. Table 1 indicates in broad terms the necessary gross budgetary provision for our 1983 refunds. On the basis of a net refund of 1.32 billion ecus (the figures in the paper tabled by the Foreign Secretary at Schloss Gymnich), the gross provision would be some 2 billion ecus. A critical variable is the German share of UK refunds - they contributed half their normal share in respect of 1982 and have publicly set their target for 1983 at a quarter of their normal share. The table also assumes that all other member states contribute in full - though letting out Ireland and Greece would not affect the arithmetic much.

CONFIDENTIAL

TABLE 1: GROSS AMOUNTS FOR UK 1983 REFUNDS (Billion ecus)

(i)	Unadjusted net contribution (reference figure)	2.0
(ii)	66 per cent refund (net)	1.32
(iii)	Gross provision assuming all other member states pay full share	1.7
(iv)	Gross provision assuming Germany contributes half her normal share	2.1
(v)	Gross provision assuming Germany contributes a quarter of her normal share	2.4
[(vi)	Saving in gross provision if UK "repays" 250 mecu net for "overpayment"	0.3 to 0.4]

4. An offset to this gross provision will be any ex gratia offer we make in respect of the 1980 and 1981 "overpayment" (line(vi) above). A net restitution of 250 mecu (the maximum figure Ministers have so far agreed) would reduce the necessary gross budgetary provision by between 0.3 and 0.4 billion ecus. The negotiations over 1983 refunds may of course produce an outcome which requires budgetary provision of less than 2 billion ecus. But there are uncertainties operating in the other direction (eg over CAP expenditure and the own resources forecast) and it would be prudent to plan on the basis of a requirement for 2 billion ecus headroom in all.

Prospects for "headroom" in 1983 and 1984

5. Table 2 illustrates the available "headroom" under the 1 per cent VAT ceiling in 1983 and 1984. It is based on what we know of the Commission's current proposals for a 1983 supplementary budget and on their 1984 PDB.

TABLE 2: HEADROOM IN 1983 AND 1984 (billion ecus)

		1983	1984
(i)	Total available resources, up to 1 per cent VAT ceiling	25.8	26.2
(ii)	CAP guarantee expenditure	15.5-16.0	16.5
(iii)	Other obligatory expenditure	2.3	2.3
(iv)	Non obligatory expenditure	5.3-5.7	6.7
(v)	UK and German basic refunds for 1982	1.8	-
(vi)	Total expenditure	25.4-25.8	25.5
(vii)	Remaining headroom	0-0.8	0.7

Notes:

(i) 1983 figure includes surpluses from previous years. The VAT adjustment (-0.2) will probably be offset by a further surplus from 1982.

(ii) 1983 figure includes 1.5-2.0 billion ecus for CAP guarantee supplementary budget.

(iii) Mostly own resources collection costs refunds, food aid and FEOGA guidance.

(iv) 1983 figures includes the possibility of up to 0.4 billion of extra non-obligatory expenditure to be proposed by the Commission in the Supplementary Budget. 1984 figure constitutes an increase of 27 per cent (on present base) compared with 11.6 per cent maximum rate.

(v) 1983 figure includes risk-sharing provision of 0.5 billion in respect of 1982.

6. On the Commission's proposals, the remaining headroom in 1983 is likely to be no more than a few hundred million ecus. Headroom in the 1984 Preliminary Draft Budget is some 700 million ecus, though the Commission has adopted the highest possible estimates of own resources; several member states consider that a yield of 25.8 billion or even less is more likely than 26.2 billion ecus. There will probably be pressure to reduce the revenue estimate or for a safety margin of at least 500 million ecus to avoid the possibility of the own resources ceiling being breached during the year.

7. The Council ought in principle to be able substantially to reduce the expenditure proposals of the Commission when it establishes both draft budgets at the end of July. The nature of the EC's budgetary procedure, in particular the fact that majority voting applies, means that we have to find allies to achieve our aims. This is usually more difficult for obligatory expenditure, including the CAP, than for non-obligatory expenditure. But on the latter, the European Parliament has the last word subject only to the maximum rate provisions of the Treaty. If the Council were to succeed in restricting non-obligatory expenditure to the maximum rate - something which has never happened before - a further 700 million ecus in 1984 might become available.

8. The above estimates show that it will be difficult to cover the gross budgetary provision necessary for our desired 1983 refunds from the two budget years together. To ensure this we should aim to reduce CAP spending by around 1-1½ billion over the two years and hold non-obligatory spending to the maximum rate. There are, however a number of major obstacles in the way:

(i) There will be considerable pressures to accept some of the Commission's proposals for increases in expenditure on energy, research, transport, and the regional and social funds. The Commission, Parliament and several other member states set great store by these efforts to "restructure" the budget. The Parliament's bargaining position will be strengthened because they agreed earlier this year to exclude the 600 million ecus of energy measures from the 1983 base

on non-obligatory expenditure despite its classification as non-obligatory. This undertaking is not legally enforceable, and it is possible that the Parliament may declare themselves no longer bound by it if they feel that a minority of member states is unreasonably squeezing the non-obligatory expenditure provision for 1984.

(ii) Most member states will resist cuts in CAP expenditure. This year's experience shows how rapidly CAP guarantee can increase. Moreover, the provision of 16.5 billion ecus in the 1984 PDB makes no allowance for the 1984 price fixing itself.

(iii) There is a natural aversion in the Community to agreeing to a budget right up against the limit of available own resources. Estimates of revenue and expenditure are too uncertain for this to be regarded as a safe course of action.

Implications for UK policy towards 1983 and 1984 budgets

9. On the above analysis, the scope for achieving our refunds in respect of 1983 through policies at present included in the PDB is inadequate. Our provisional examination suggests that only the youth unemployment proposals are of sufficient magnitude to offer a significant channel for refunds. The Commission has said it sees our refunds being met by their expenditure proposals but member states are unlikely to agree in any case to earmark refunds in this way in advance of a political agreement. Moreover, the UK could not agree that our refunds should not be specifically identified. There is an urgent need, therefore, for the proposals in both the 1983 supplementary and the 1984 PDB to be cut back in order to create the headroom for our 1983 refunds. Provision for our refunds could then be entered in the draft budget at the Budget Council on 21 July. In effect, we would follow a two stage operation: first, to seek substantial cuts in the Commission's present proposals; and, second, to divert the savings achieved towards our refunds. The two stages would move together, depending on the rate of progress of the main refund negotiations.

10. This will pose problems of presentation. It might be considered inconsistent for the UK to oppose many of the Commission's proposed spending increases but it should be possible to do so on broader public expenditure and cost effectiveness grounds rather than just the need to create headroom for UK refunds. The proposed spending increases in the Social Fund (+15 per cent), Regional Fund (+19 per cent), research and development (+43 per cent), information and innovation (+200 per cent), transport (+134 per cent) etc, all massively exceed the increases in domestic public expenditure and the expected general rate of increase in prices in the Community in the coming year (some 7 per cent). In seeking reductions in the proposed levels of increase we can show that just as domestic public expenditure must match what we can afford, so must the Community's spending, which is

only another element of public spending like local authority or nationalised industry spending. We will still be able to show that Community spending is expanding much faster than other areas of public expenditure, even after Council reductions. In addition, we can argue that the need to preserve the 1 per cent ceiling means that only more modest increases than those proposed by the Commission can be afforded. These lines of argument might make it easier to maintain the goodwill of the European Parliament.

1983 Supplementary

11. Our information suggests that the Commission will put forward a supplementary budget containing provision for additional CAP spending in 1983 of some 1½-2 billion ecu, 500 mecu for the risk-sharing element of our 1982 refunds deal, and up to 400 mecu to cover social fund and food aid expenditure. We would obviously prefer to limit agricultural spending as much as possible but it may not be realistic to hope for reductions in 1983 of more than 500 mecu. It would be very difficult to get agreement to change the basic regulations in 1983. Mr Tugendhat himself wants to limit CAP spending to 1½ billion ecu. But to achieve this we will need to support of one other large member state. In fact only the Germans and Dutch are likely to share our views. We will want to limit as much as possible the other spending provisions in the Supplementary in order to create room in 1983 for possible use for our refunds. Other member states may oppose such spending for other reasons so we should not be isolated in this.

1984 PDB

(a) Obligatory Expenditure

12. The difficulties in slowing down CAP spending in 1983 make it all the more important to make reductions in the Commission's proposed CAP spending of 16.5 billion ecu in 1984, although any such savings at the expense of specific UK interests could add to our net contribution. But the Commission and other member states argue that there is an obligation on the Community to enter in the budget the amount which they expect to be spent on current policies, and that to do otherwise would create a serious risk of breaching the own resources ceiling during the year. Against this, we can argue that the Commission should be making specific suggestions for reforms of the CAP in order to keep expenditure within the limits set; that there is in fact worthwhile scope for economies in the running of the CAP even if present policies are maintained; and that the growth in agricultural spending must be markedly lower than the growth in own resources. The Commission have, however, said that they are in effect prepared to treat 16.5 billion ecu for 1984 as a cash limit; and they are apparently intending to bring forward proposals for changes in the CAP regime in time for the consequences to be reflected in the 1984 Budget. There is no reason in principle,

therefore, why they should not set a lower "cash limit" than 16.5 billion ecus. To achieve our objectives, we must certainly aim to reduce the 1984 PDB provision from 16.5 billion ecus.

13. This will not be easy. We shall need the firm support of one other large member state, most likely Germany, if we are to get our way at the July Council. Preliminary discussions indicate that such support may be forthcoming; but it is difficult to assess how reliable it will be in practice. Moreover, their objectives will not always be the same as our own. We may therefore have to accept reductions in some areas which are of benefit to the UK. At a later stage, proposals from the European Parliament to reduce provision for FEOGA could be turned to account, though German support would again be necessary.

14. Another element of obligatory expenditure in the 1984 PDB which could be cut is the interest subsidies granted as part of the measures associated with the establishment of the EMS. The Commission have just put forward a new Council Regulation extending these and have proposed entering 200 million ecus in the 1984 budget. Only Italy and Ireland benefit from this expenditure and it would be open to the UK (with other member states) to oppose the regulation, which requires unanimity. We may in fact be able to let the Germans, French and Dutch take the lead in resisting the further extension of EMS interest subsidies.

15. Other areas of obligatory expenditure include some food aid, financial protocols with third countries, some FEOGA guidance and own resource collection costs. It may be possible to secure small savings in the first three categories - for example, we would argue (on financial protocols) that the Commission has overestimated the speed of payment, justifying some cut in payment appropriations. But overall cuts in these are unlikely to provide savings of more than 100 mecu. The 10 per cent own resource collection costs are provided for in the Treaty, and it would probably not be legal to reduce provision for them in the absence of Treaty amendment. Member states would most probably strongly resist this. In any case, our share of this expenditure is disproportionately high, so reducing it would not be attractive. It might, nevertheless, be open to member states to forego their refunds voluntarily during a year - a one-off operation to which we should only agree as a last resort if it is the only way to protect our refunds.

(b) Non-obligatory expenditure

16. On non-obligatory expenditure, the scope for reductions is influenced by the fact that the European Parliament has the last word subject to the maximum rate of increase. It would be possible for the Council to insist on reductions which would limit the increase adopted by the EP to no more than the maximum rate (thereby providing savings of some 700 mecu), although an increase in the maximum rate has always been granted in the past. This has been partly due to the EP's power to reject the budget. There is no reason to

suppose that the Parliament will not insist on one again in respect of 1984 (particularly in view of their bargaining position explained in paragraph 8(i) above). But we will still have to try to keep non-obligatory expenditure to a minimum particularly given the difficulties in holding down obligatory spending. In order to do this, it is important at the first Budget Council to restrict it to half the maximum rate (thereby providing savings of around 1 billion ecu) -the provisions of Article 203 would then ensure that Parliament's margin was not more than the maximum rate. If the Council fails to cut to half the maximum rate, then the EP can increase non-obligatory spending by a further half of the maximum rate.

17. Until we have a political agreement on the size of our refunds, we should therefore seek in Budget Committee and COREPER to cut the increase in non-obligatory expenditure to half the maximum rate. The French and Germans are likely to be in the lead in advocating this. To get their agreement to cuts in obligatory expenditure we should seek to take credit for reducing non-obligatory spending. Administrative expenditure accounts for some 15 per cent of non-obligatory expenditure in the 1984 PDB. So far, in discussion of the small institutions' budgets, the UK has been in the lead in seeking to ensure that increases in expenditure do not exceed 7 per cent (the Commission's forecast of the average Community inflation rate) in 1984. This has meant opposing all new staff and regradings etc. But an even tougher approach may be needed, so that some posts are actually cut. This could be done without redundancies and there is some evidence that the French will take a similar line.

18. On other non-obligatory spending, we should seek to identify those lines from which we benefit most (such as the European Social Fund (ESF))and from which we might benefit (spending on coal) and try to protect them as much as we can in the inevitable bargaining process which will be needed to cut the non-obligatory increase to under 5.8 per cent, that is half the maximum rate. We will consult Departments to identify our priority areas and with colleagues in other member states to see whether some co-ordination of approach can be achieved before the Budget Council. But it must be recognised that member states have different interests in non-obligatory expenditure and it may not always be possible to safeguard our priority areas.

19. Subject to that general point, our initial ideas for the main areas of cuts include aid, energy, research and administration. On aid, the Commission is proposing an increase of some 18 per cent. It should be possible to cut this quite sharply, producing savings of some 150 million ecus in payments. On administration, we might look for payment savings of some 100 million ecus. On energy, we may wish to support provision for solid fuels; but we could still cut some 65 million ecus from the programmes. On research, the Commission is

proposing large increases - savings here might total up to 200 million ecus in payments. Transport could be cut by about 20 million ecus.

20. This will still not be enough, however, and we may have to look for savings in the regional and social funds as well. It might be best to concentrate on the regional fund which gives us less net benefit and which is less of a priority for the Parliament. Some 200 mecus of payments might be cut here.

(c) Revenue

21. Although the own resources revenue estimate may well turn out to be too high, it is probably not in our interests to take the lead in seeking to reduce it. To do so would aggravate the headroom problem; and, in principle, we should receive our basic 1983 refunds by 31 March 1984 so that any cash difficulties which may arise should bite on expenditure other than refunds. Nevertheless we can hardly oppose reductions in the own resource estimates if other member states seek them.

Summary

22. The UK's objectives with regard to the 1983 Supplementary Budget No 2 and the 1984 PDB should in our view be as follows;-

(i) overall we must to ensure that sufficient headroom remains for payment of UK refunds for 1983 on the scale implied in the note tabled by the Foreign Secretary at Schloss Gymnich. The gross provision would need to be of the order of 2 billion ecus less any concession we make for overpayment. Most of this would come from the 1984 Budget but as much headroom as possible should be left in 1983 to allow for the possibility of a 3rd Supplementary Budget to provide refunds.

1983 Supplementary No 2

(ii) provision for risk sharing in respect of our 1982 refunds must be made in the 1983 Supplementary No 2. Gross budgetary provision required totals some 0.5 billion ecus;

(iii) provision for CAP guarantee should be reduced by 1 billion ecus below what the Commission is likely to put forward;

(iv) in principle, the Supplementary No 2 should limit its payment provision to risk-sharing and agricultural spending (ie make no provision for extra non-obligatory expenditure);

1984 PDB

(v) we must ensure that the draft budget contains specific and identifiable provision for our 1983 refunds, as well as a token entry for supplementary measures.

(vi) in order to make room for this, other expenditure must be reduced to allow the necessary headroom of some 2 billion ecu. Given the present PDB headroom of only 0.7 billion ecu, this will mean cuts of around 1.3 billion ecu.

(vii) we should therefore aim to hold down non-obligatory expenditure not specifically related to refunds to the maximum rate (11.6 per cent). This would provide savings of some 700 mecu. For procedural reasons, it will mean cutting non-obligatory spending to half the maximum rate at the July Budget Council.

(viii) we should also seek cuts in FEOGA guarantee spending. Our target should be to reduce it by at least 1 billion ecu and to fix a ceiling on FEOGA guarantee spending at 15½ or at most 16 billion ecu. Non-CAP obligatory expenditure should also be kept to a minimum.

Annex A

1984 PRELIMINARY DRAFT: SUMMARY (MECUS)

Payments			% increase on 1983
Total available revenue		26196	+ 7.8
FEOGA Guarantee		16500	+ 17.4
Other obligatory:			
Own resource refunds	1074		
EMS interest rate subsidies	200		
Fish	115		
FEOGA guidance	525		
Food aid (cereals)	156		
Other	263		
Sub total		2333	-
Total obligatory expenditure		18833	
Non-obligatory expenditure:			
Regional Fund	1500		
Social Fund	1550		
Energy	386		
Research	595		
Aid	832		
Administration	1230		
Other	602		
Sub total		6695	+ 27.0
Total expenditure		25528	+ 11.5
Margin		668	

A. BUDGET APPROACH AND PROPOSALS FOR 1984

COMMUNITY EXPENDITURE BY SECTOR

Including supplementary and amending budget No 1/1983
Appropriations for commitments

Sector	1983 budget		Preliminary draft 1984		Change (3:1)	
	Amount	%	Amount	%	Amount	%
	(1)	(2)	(3)	(4)	(5)	(6)
I. SECTION III B — COMMISSION (Operating appropriations)						
A — Agricultural market guarantees						
— EAGGF Guarantee (Ch. 10 to 29)						
Total A	*14 050 000 000*	*57,76*	*16 500 000 000*	*57,65*	*+ 2 450 000 000*	*+ 17,44*
B — Agricultural structures						
— EAGGF Guidance (Ch. 30 to 33)	759 400 000	3,12	733 500 000	2,56	— 25 900 000	— 3,41
— Specific measures (Ch. 38)	55 129 950	0,23	56 258 000	0,20	+ 1 128 050	+ 2,05
Total B	*814 529 950*	*3,35*	*789 758 000*	*2,76*	*— 24 771 950*	*— 3,04*
C — Fisheries (Ch. 40 to 46) *Total C*	*91 792 000*	*0,38*	*171 494 000*	*0,60*	*+ 79 702 000*	*+ 86,83*
D — Regional policy						
— Regional Fund (Ch. 50 and 51)	2 010 000 000	8,26	2 500 000 000	8,74	+ 490 000 000	+ 24,38
— EMS (Ch. 52)	200 000 000	0,82	200 000 000	0,70	—	—
— Supplementary measures (UK) (Ch. 53)	692 000 000	2,84	—	—	— 692 000 000	—
— Miscellaneous (Ch. 54 and 55)	26 800 000	0,11	45 850 000	0,16	+ 19 050 000	+ 71,08
Total D	*2 928 800 000*	*12,04*	*2 745 850 000*	*9,59*	*— 182 950 000*	*— 6,25*
E — Social policy						
— Social Fund (Ch. 60 and 61)	1 696 500 000	6,97	2 400 000 000	8,39	+ 703 500 000	+ 41,47
— Miscellaneous (Ch. 64, 65, 68 and 69)	95 605 000	0,39	171 772 000	0,60	+ 76 167 000	+ 79,67
— Education and culture (Ch. 63 and 67)	16 341 000	0,07	19 022 000	0,07	+ 2 681 000	+ 16,41
— Environment and consumers (Ch. 66)	12 690 000	0,05	21 064 000	0,07	+ 8 374 000	+ 65,99
Total E	*1 821 136 000*	*7,49*	*2 611 858 000*	*9,13*	*+ 790 722 700*	*+ 43,42*
F — Research, energy, industry, transport						
— Energy policy (Ch. 70 and 71)	723 835 000	2,98	772 585 000	2,70	+ 48 750 000	+ 6,73
— Research and investment (Ch. 72 and 73)	436 053 000	1,79	1 056 582 000	3,69	+ 620 529 000	+ 142,31
— Information and innovation (Ch. 75)	12 510 000	0,05	38 760 000	0,14	+ 26 250 000	+ 209,83

Continued

Sector	1983 budget		Preliminary draft 1984		Change (3:1)	
	Amount	%	Amount	%	Amount	%
	(1)	(2)	(3)	(4)	(5)	(6)
— Industrial and internal market (Ch. 77)	39 406 000	0,16	69 223 000	0,24	+ 29 817 000	+ 75,67
— Transport (Ch. 78)	16 450 000	0,07	106 950 000	0,37	+ 90 500 000	+ 550,15
Total F	*1 228 254 000*	*5,05*	*2 044 100 000*	*7,14*	+ *815 846 000*	+ *66,42*
G — Repayments and reserves						
— Repayments to the Member States (Ch. 80)	1 014 622 000	4,17	1 074 468 000	3,75	+ 59 846 000	+ 5,90
— Other repayments (Ch. 82 and 86)	108 681 757	0,45	69 105 794	0,24	— 39 575 963	— 36,41
— Financial mechanism (Ch. 81)	p.m.	—	p.m.	—	—	—
— Miscellaneous (Ch. 79, 83, 84 and 85)	p.m.	—	p.m.	—	—	—
— Reserves (Ch. 101 and 102)	5 000 000	0,02	5 000 000	0,02	—	—
Total G	*1 128 303 757*	*4,64*	*1 148 573 794*	*4,01*	+ *20 270 037*	+ *1,80*
H — Development cooperation and non-member countries						
— EDF (Ch. 90 and 91)	p.m.	—	p.m.	—	—	—
— Food aid (Ch. 92)	557 950 000	2,29	569 000 000	1,99	+ 11 050 000	+ 1,98
— Non-ass. dev. countries (Ch. 93)	248 935 000	1,01	323 532 000	1,13	+ 74 597 000	+ 29,97
— Specific and exceptional measures (Ch. 94 and 95)	92 045 000	0,39	167 470 000	0,59	+ 75 425 000	+ 81,94
— Cooperation with Mediterranean countries (Ch. 96)	160 512 000	0,66	192 000 000	0,67	+ 31 488 000	+ 19,62
— Miscellaneous (Ch. 97, 98 and 99)	50 125 900	0,21	59 060 000	0,21	+ 8 934 100	+ 17,82
Total H	*1 109 567 900*	*4,56*	*1 311 062 000*	*4,58*	+ *201 494 100*	+ *18,16*
Section III B total	*23 172 383 607*	*95,26*	*27 322 695 794*	*95,46*	*+4 150 312 187*	+ *17,91*
II. SECTION III A — COMMISSION (Staff and administrative appropriations)	748 404 800	3,08	860 097 570	3,01	+ 111 692 770	+ 14,92
Commission total	*23 920 788 407*	*98,34*	*28 182 793 364*	*98,47*	*+4 262 004 957*	+ *17,82*
III. SECTIONS I, II, IV and V — OTHER INSTITUTIONS	404 814 778	1,66	437 052 024	1,53	+ 32 237 246	+ 7,96
Grand total	**24 325 603 185**	**100,00**	**28 619 845 388**	**100,00**	**+4 294 242 203**	**+ 17,65**

COMMUNITY EXPENDITURE BY SECTOR

Including supplementary and amending budget No 1/1983

Appropriations for payments

Sector	1983 budget		Preliminary draft 1984		Change (3:1)	
	Amount	%	Amount	%	Amount	%
	(1)	(2)	(3)	(4)	(5)	(6)
I. SECTION III B — COMMISSION (Operating appropriations)						
A — Agricultural market guarantees						
— EAGGF Guarantee (Ch. 10 to 29)						
Total A	*14 050 000 000*	*61,36*	*16 500 000 000*	*64,63*	*+2 450 000 000*	*+ 17,44*
B — Agricultural structures						
— EAGGF Guidance (Ch. 30 to 33)	597 120 000	2,61	647 810 000	2,54	+ 50 690 000	+ 8,49
— Specific measures (Ch. 38)	54 062 000	0,24	49 812 370	0,19	— 4 250 580	— 7,86
Total B	*651 182 950*	*2,84*	*697 622 370*	*2,73*	*+ 46 439 420*	*+ 7,13*
C — Fisheries (Ch. 40 to 46) *Total C*	*84 392 000*	*0,37*	*116 994 000*	*0,46*	*+ 32 602 000*	*+ 38,63*
D — Regional policy						
— Regional Fund (Ch. 50 and 51)	1 259 000 000	5,50	1 500 000 000	5,88	+ 241 000 000	+ 19,14
— EMS (Ch. 52)	200 000 000	0,87	200 000 000	0,78	—	—
— Supplementary measures (UK) (Ch. 53)	692 000 000	3,02	—	—	— 692 000 000	—
— Miscellaneous (Ch. 54 and 55)	26 800 000	0,12	42 450 000	0,17	+ 15 650 000	+ 58,40
Total D	*2 177 800 000*	*9,51*	*1 742 450 000*	*6,83*	*— 435 350 000*	*— 19,99*
E — Social policy						
— Social Fund (Ch. 60 and 61)	1 350 000 000	5,90	1 550 000 000	6,07	+ 200 000 000	+ 14,81
— Miscellaneous (Ch. 64, 65, 68 and 69)	95 325 000	0,42	171 086 000	0,67	+ 75 761 000	+ 79,48
— Education and culture (Ch. 63 and 67)	16 341 000	0,07	19 022 000	0,07	+ 2 681 000	+ 16,41
— Environment and consumers (Ch. 66)	13 590 000	0,06	15 914 000	0,06	+ 2 324 000	+ 17,10
Total E	*1 475 256 000*	*6,44*	*1 756 022 000*	*6,88*	*+ 280 766 000*	*+ 19,03*
F — Research, energy, industry, transport						
— Energy policy (Ch. 70 and 71)	711 658 000	3,11	385 900 000	1,51	— 325 758 000	— 45,77
— Research and investment (Ch. 72 and 73)	415 631 000	1,82	594 695 000	2,33	+ 179 064 000	+ 43,08
— Information and innovation (Ch. 75)	11 360 000	0,05	34 175 000	0,13	+ 22 815 000	+200,84
— Industrial and internal market (Ch. 77)	45 156 000	0,20	66 953 000	0,26	+ 21 797 000	+ 48,27
— Transport (Ch. 78)	14 450 000	0,06	33 950 000	0,13	+ 19 500 000	+134,95
Total F	*1 198 255 000*	*5,23*	*1 115 673 000*	*4,37*	*— 82 582 000*	*— 6,89*

Continued

Sector	1983 budget		Preliminary draft 1984		Change (3:1)	
	Amount	%	Amount	%	Amount	%
	(1)	(2)	(3)	(4)	(5)	(6)
G — Repayments and reserves						
— Repayments to the Member States (Ch. 80)	1 014 622 000	4,43	1 074 468 000	4,21	+ 59 846 000	+ 5,90
— Other repayments (Ch. 82 and 86)	108 681 757	0,47	69 105 794	0,27	— 39 575 963	— 36,41
— Financial mechanism (Ch. 81)	p.m.	—	p.m.	—	—	—
— Miscellaneous (Ch. 79, 83, 84 and 85)	p.m.	—	p.m.	—	—	—
— Reserves (Ch. 101 and 102)	5 000 000	0,02	5 000 000	0,02	—	—
Total G	*1 128 303 757*	*4,93*	*1 148 573 794*	*4,50*	+ *20 270 037*	+ *1,80*
H — Development cooperation and non-member countries						
— EDF (Ch. 90 and 91)	p.m.	—	p.m.	—	—	—
— Food aid (Ch. 92)	557 950 000	2,44	569 000 000	2,23	+ 11 050 000	+ 1,98
— Non-ass. dev. countries (Ch. 93)	143 935 000	0,62	196 132 000	0,77	+ 52 197 000	+ 36,26
— Specific and exceptional measures (Ch. 94 and 95)	89 045 000	0,39	164 170 000	0,64	+ 75 125 000	+ 84,37
— Cooperation with Mediterranean countries (Ch. 96)	136 457 000	0,60	165 573 000	0,65	+ 29 116 000	+ 21,34
— Miscellaneous (Ch. 97, 98 and 99)	50 125 900	0,22	59 060 000	0,23	+ 8 934 100	+ 17,82
Total H	*977 512 900*	*4,27*	*1 153 935 000*	*4,52*	+ *176 422 100*	+ *18,05*
Section III B total	*21 742 702 607*	*94,96*	*24 231 270 164*	*94,92*	+ *2 488 567 557*	+ *11,45*
II. SECTION III A — COMMISSION (Staff and administrative appropriations)	748 404 800	3,27	860 097 570	3,37	+ 111 692 770	+ 14,92
Commission total	*22 491 107 407*	*98,23*	*25 091 367 734*	*98,29*	+ *2 600 260 327*	+ *11,56*
III. SECTIONS I, II, IV and V — OTHER INSTITUTIONS	404 814 778	1,77	437 052 024	1,71	+ 32 237 246	+ 7,96
Grand total	**22 895 922 185**	**100,00**	**25 528 419 758**	**100,00**	**+ 2 632 497 573**	**+ 11,50**

Annex B

PROVISIONAL BUDGET TIMETABLE

Friday 10 June	PDB documents available
Tuesday 14 June	First reading in Budget Committee of Commission Budget starts (Part A first)
Friday 17-19 June	European Council
Wednesday 22 June	Second reading in Budget Committee of Commission Budget starts
Wednesday 20-21 June	Budget Council

cc CST
Mr Middleton
Mr Bailey
Mr Wilding
Mr Pestell
Mr Judd
Mr Hopkinson
Mr Fitchew
Mr Edwards

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Patrick Jenkin MP
Secretary of State for the
Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

16 June 1983

Dear Secretary of State

I wrote to Tom King on 24 May about the PAC's Report on Dog Licensing, explaining that if I was in a position to do so I would be returning to the attack immediately after the election. I now do so.

The position in which we find ourselves on dog licensing is quite indefensible. The present fee of 37½p has not changed since 1878 and the revenue, a fairly constant £1M a year, is far outstripped by the payments which your department makes to the Post Office for issuing licences. The amount paid over in 1982-83 was about £3.6M.

The question of what to do about the present unsatisfactory arrangements has been raised several times in recent years. But so far no action has been taken. The PAC investigated matters last year and in their report concluded that the present arrangements served no useful purpose (indeed only about 50% of dog owners now bother with licences). They recommended that the present arrangements be temporarily suspended until a policy decision was reached.

We were not able to settle the form of the Treasury Minute responding to the PAC's report before the election. However we must aim to do so very quickly, since I hope to be able to lay the Treasury Minutes for all the reports so far received from the PAC by the end of the Session. That will require agreement by about the end of June.

The differences in the respective stances of Tom King and Peter Walker on the one hand and myself on the other hand are illustrated by the different versions of the draft texts of the Treasury Minutes ... referred to in my letter of 11 April to Tom (texts attached for reference). In brief, I proposed a more positive form of Minute -

accepting that the present arrangements should be modified or ended as soon as possible.

As I explained in my letter of 24 May it will be most regrettable if we cannot demonstrate to the PAC at least our resolve to get to grips with the problem. Indeed a positive Treasury Minute could be speedily followed by substantive decisions on ending the present nonsense which makes no financial sense, and leaves us very vulnerable to criticism. I hope that you will soon bring the substance of the problem - and some way of finally disposing of it - to H Committee. We shall have no better opportunity than early in the new Parliament with a substantial majority behind us.

I should therefore be grateful for agreement from you and Michael Jopling by 24 June to the more positive form of the Minute.

I am copying this letter to members of H Committee, Michael Jopling, Jim Prior and to Sir R Armstrong.

Yours sincerely

Martin Donnelly

PP NICHOLAS RIDLEY

(Affixed by the Financial Secretary; signed in his absence.)

NOT FOR E & AD EYES

ANNEX A

DRAFT TREASURY MINUTE ON THE FIRST REPORT FROM THE COMMITTEE OF PUBLIC ACCOUNTS SESSION 1982-83

Department of the Environment: Dog Licensing

1. The Treasury, the Department of the Environment and the Ministry of Agriculture, Fisheries and Food note the comments and recommendations of the Committee.

2. They share the Committee's concern about the widening gap between receipts from licence fees and the costs of collection. The Department of the Environment have introduced a minor change in the arrangements which will yield an annual saving of about £90,000 on the Department's expenditure. Further possibilities for effecting savings through more efficient working methods are also being examined in consultation with the Post Office.

4. The Committee specifically recommended the suspension of the present arrangements temporarily until a policy decision becomes possible. But, as pointed out in paragraph 10 of the Comptroller and Auditor General's Memorandum, such a suspension would require primary legislation.

[PREFERRED DRAFT]

ANNEX B

DRAFT TREASURY MINUTE ON THE FIRST REPORT FROM THE COMMITTEE OF PUBLIC ACCOUNTS SESSION 1982-83

Department of the Environment: Dog Licensing

The Treasury, the Department of the Environment and the Ministry of Agriculture, Fisheries and Food note the comments and recommendations of the Committee.

2. They share the Committee's concern about the widening gap between receipts from licence fees and the costs of collection; agree that the present arrangements serve no useful national purpose; and believe that they should be modified or ended as soon as possible.

3. Pending a policy decision, the Department of the Environment has introduced a minor change in the arrangements which will yield an annual saving of about £90,000 on the Department's expenditure. Further possibilities for effecting savings through more efficient working methods are also being examined in consultation with the Post Office.

4. The Committee specifically recommended the suspension of the present arrangements temporarily until a policy decision becomes possible. However, as pointed out in paragraph 10 of the Comptroller and Auditor General's Memorandum, such a suspension would require primary legislation. The Government will consider this option along with the others as soon as a legislative opportunity occurs.

CONFIDENTIAL

FROM: FINANCIAL SECRETARY
DATE: 20 June 1983

CHANCELLOR

cc Chief Secretary
Economic Secretary
Minister of State
Mr Middleton
Mr Cassell
Mr Battishill
Mr Robson
Mr Turnbull
Mr Graham - Parly Counsel
PS/IR

OUTSTANDING OIL LEGISLATION

The possibility of a joint royalties/'condoc' Bill has been discussed further with Lord Cockfield and the House authorities. Unfortunately this option does not seem to be a runner. A joint bill would be a bill of 'aid and supply' and, unless there were some special dispensation, this would prevent the Lords from amending any part of it, including the royalties part. The Lords would object to this as contrary to their Standing Order against 'tacking'. The Lords authorities have said that the Lords would not object to a joint Bill if the Commons were to indicate that they would waive their privilege in relation to any amendments the Lords might make on the royalties clauses. (There are precedents for this in the Severn and Erskine Toll Bridge Acts of 1965 and 1967 when the Commons agreed to waive privilege in relation to Lords amendments relating to traffic regulation as opposed to the tolls themselves.) But the Commons authorities have said that the Commons would not be prepared to waive privilege in relation to royalties clauses in a joint Bill. (The toll bridge Acts were a special case, partly because tolls are not fully analogous to taxes and partly because this legislation on toll bridges would have taken the form of private Bills, but for the fact that a motorway ran over the bridge). This, I think, rules out the joint Bill.

You have agreed that in these circumstances the fallback option is a separate oil taxation Bill to be taken in the autumn. (Draft clauses could be published before the recess.) You have already mentioned this to the Treasury Whip, and, if you agree, I will warn colleagues

of the need for this Bill at the meeting of Legislation Committee tomorrow morning, when the Secretary of State for Energy is seeking leave to publish and introduce the Royalties Bill into the House of Commons immediately.

Martin Donnelly
pp NICHOLAS RIDLEY

CONFIDENTIAL

FROM: E KWIECINSKI
DATE: 21 June 1983

PS/CST

cc PS/Chancellor
PS/EST
Mr Robson
Mr Prescott/IR
PS/IR

BUSINESS EXPANSION SCHEME: PROPOSED GOVERNMENT AMENDMENTS TO SCHEDULE 5, FINANCE ACT 1983

The Financial Secretary has seen Mr Prescott's submission of 17 June and Miss Simpson's minute of 20 June.

He has commented that all of the proposed Government amendments should be treated as essential and should be made in the forthcoming Bill. He does not think they will arouse much opposition or debate during the passage of the Bill.

E KWIECINSKI

FROM: M E DONNELLY
DATE: 21 June 1983

MR LENNON

cc PS/Chancellor
PS/Chief Secretary
Mr Middleton
Mr Littler
Mr Unwin
Mrs Hedley-Miller
Miss Court
Mr Edwards
Mr Peet

NET CONTRIBUTIONS TO EUROPEAN COMMUNITY BUDGET

The Financial Secretary has seen the table of net contributions to and receipts from the EC Budget attached to Mr Williamson's note to NO.10 of 15 June.

The Financial Secretary would be interested to see the figures for net contributions/receipts for all 10 member states on the following bases:

i) per head of population;

ii) per head of population divided by an index of comparative prosperity per head, to show the extent to which poorer member states were transferring resources to richer ones.

MED

M E DONNELLY

FROM: M E DONNELLY
DATE: 21 June 1983

PS/INLAND REVENUE

cc PS/Chancellor
PS/Chief Secretary
PS/Economic Secretary
PS/Minister of State
Mr Middleton
Mr Robson
Mr Prescott - IR

STOCK EXCHANGE SUBMISSION ON FINANCE BILL NO.2

The Financial Secretary has seen Sir Nicholas Goodison's letter of 14 June covering the Stock Exchange's comments on the Finance Bill.

The Financial Secretary considers that the Stock Exchange proposals for amendments to the Business Expansion Scheme provisions in the Finance Act should not be accepted in the summer Finance Bill.

MED
M E DONNELLY

CONFIDENTIAL

FROM: M E DONNELLY
DATE: 21 June 1983

MR ST CLAIR

cc PS/Chancellor
PS/Chief Secretary
PS/Economic Secretary
PS/Minister of State
Mr Middleton
Mr Kemp
Mr Battishill
Mr Kitcatt
Mr C Ward
Mr Salveson
Mr I Wilson
Mr Richardson

PENSIONS COMMUTATION BILL

The Financial Secretary has told me that at Legislation Committee this morning it was decided that Treasury and Ministry of Defence should agree on this Bill bilaterally before it was reconsidered by L Committee.

The Financial Secretary would be grateful if you - in conjunction with DM - would take this on.

MED
M E DONNELLY

FROM: M E DONNELLY
DATE: 21 June 1983

MR WILLETTS

cc PS/Chancellor
PS/Economic Secretary
Mr Middleton
Mr Cassell
Mr Monck
Mrs Lomax
Mr Gordon
Mr Robson
PS/IR

COMPANIES (BENEFICIAL INTERESTS) BILL: 1914 BANKRUPTCY ACT: DEEP DISCOUNT BONDS

At Legislation Committee this morning, the Financial Secretary raised the possibility of using the Companies (Beneficial Interests) Bill as a vehicle for the changes required to the Bankruptcy Act 1914 to prevent unintended discrimination against deep discount and zero coupon bonds. (Your submission of 12 May and Mr Turnbull's submissions of 19 and 26 April refer.)

L Committee agreed that the possibilities of using this Bill to amend the 1914 Act should be explored further at official level, though without commitment to amend the Companies Bill.

The Financial Secretary would be grateful if you would explore the possibilities with the Department of Trade and report back.

MED

M E DONNELLY

RESTRICTED

FROM: M E DONNELLY
DATE: 22 June 1983

PS/ECONOMIC SECRETARY

TAX POLICY: DIVISION OF RESPONSIBILITY

We spoke about this.

... I attach a note, which follows closely the earlier distribution of responsibilities which you sent me.

The only suggested change is that the Financial Secretary thinks it would be sensible for him to continue to deal with the items arising on Purchase of Own Shares, Employee Share Schemes etc until the Summer Recess. This is because these are likely to arise in a Finance Bill context, and involve issues which he was dealing with in the context of the first Finance Act.

Correspondence

The Financial Secretary has discussed with Mr Middleton the question of correspondence dealing with firms who have PAYE payment problems. They both feel strongly that these cases have wider industrial policy implications, and therefore fall within the Economic Secretary's ambit.

More generally Mr Middleton is context with this distribution of responsibilities.

If the Economic Secretary is content I will send the attached note to the Chancellor for his approval.

MED

M E DONNELLY

TAX POLICY: DIVISION OF RESPONSIBILITY

1. FINANCIAL SECRETARY

(a) Schedule D/Schedule E borderline

(b) Schedule D self-assessment

(c) Corporation Tax self-assessment.

2. ECONOMIC SECRETARY

(a) Payroll Taxes

(b) Corporate Bonds

3. UNTIL SUMMER RECESS: FINANCIAL SECRETARY

SUBSEQUENTLY: ECONOMIC SECRETARY

(a) Business Expansion Scheme, and other "enterprise" measures

(b) Capital allowances

(c) Purchase of Own Shares, Employee Share Schemes etc.

CONFIDENTIAL

FROM: FINANCIAL SECRETARY
DATE: 22 June 1983

CHANCELLOR

cc Chief Secretary
Economic Secretary
Minister of State
Mr Middleton
Sir T Burns
Mr Littler
Mr Cassell
Mr Monck
Mr Ridley

THE OPERATION OF MONETARY POLICY

I have seen the record of your discussion with the Governor on 15 June.

My own view on all this is that I trust the money supply figures as a policy indicator less and less. I do not deny the importance of the money supply, but the figures are always hard to interpret due to:

- changes in the velocity of circulation;

- time lags;

- statistical aberrations;

all of which we have seen frequently in recent months.

Experience tells us to interpret them in the light of what is happening and what people think is going to happen. What is happening is a very mild recovery in output with no recovery in employment. What people think is going to happen is for the recovery to level out and unemployment to stay high, or even to continue increasing. No one expects an increase in inflation apart from the hiccup this coming Autumn.

I think the fiscal stance is still fairly tough and would be against tightening it more. As between using taxation to limit the PSBR, or borrowing financed by debt sales to the non-bank private sector, both have broadly the same effect on money supply. Taxation makes people worse off: borrowing by raising interest rates above what they would otherwise be makes investment less profitable. So to avoid this unpleasant choice I would want to hold the public spending totals as low as we can.

NICHOLAS RIDLEY

Treasury Chambers, Parliament Street, SW1P 3AG

S C Laws Esq
Office of Parliamentary Counsel
36 Whitehall
LONDON
SW1

22 June 1983

Dear Mr Laws

PENSIONS COMMUTATION BILL

... I enclose a money resolution for the Bill duly initialled by the Financial Secretary.

E KWIECINSKI
Private Secretary

PENSIONS COMMUTATION [MONEY]: Queen's Recommendation signified

Mr Nicholas Ridley

That, for the purposes of any Act of the present Session to dissolve the Pensions Commutation Board and to amend the Pensions Commutation Act 1871, it is expedient to authorise the payment out of money provided by Parliament of -

(a) amounts awarded as commutations under the said Act of 1871; and

(b) amounts paid under the said Act of the present Session in respect of the discharge of any liability to pay an annuity under section 8 of the said Act of 1871.

20 6 83

CONFIDENTIAL

FROM: M E DONNELLY
DATE: 22 June 1983

MR ISAAC - IR

cc PS/Chancellor
PS/Chief Secretary
PS/Economic Secretary
PS/Minister of State
Mr Middleton
Mr Monger
Mr Robson
Ms Seammen
Mr St Clair
Mr Ridley
PS/IR

PERSONAL TAXATION

Following the Financial Secretary's meeting this morning, you agreed to co-ordinate a short position paper setting out current issues in the personal taxation field.

This paperwill cover, inter alia, the following areas:

Husband and Wife;

NICIT;

Child Benefit;

Fiscal position of the elderly;

Superannuation/LAPR;

The contributory principle; early retirement.

It will be helpful to have this as early as possible next week.

MED
M E DONNELLY

RESTRICTED

FROM: M E DONNELLY
DATE: 22 June 1983

MR PRESCOTT - IR

cc PS/Chancellor
PS/Chief Secretary
PS/Economic Secretary
PS/Minister of State
Mr Middleton
Mr Cassell
Mr Monger
Mr Robson
Mr Beighton - IR
PS/IR

BUSINESS EXPANSION SCHEME

You discussed outstanding issues arising from the BES legislation with the Financial Secretary.

Takeovers

Your submission of 20 June refers. The Financial Secretary took the view that prima facie it was legitimate for companies to use money raised with relief under the BES to finance takeovers of other companies. He would use the Finance Bill debates to make clear that if this freedom led to widespread abuse of the Scheme the Government would have to reconsider this aspect of the BES legislation. You agreed to provide a draft passage on these lines.

Foreign Subsidiaries

The Financial Secretary wishes to discuss this area further in the light of the amendments which are put down to the Finance Bill. He would be grateful for a further submission in due course.

Flotation of BES Companies

The Financial Secretary pointed out that this issue had been discussed before the first Finance Bill had been published. It had now been raised again by Sir Nicholas Goodison. While the decision on the USM position should be unchanged he was prepared to remain open-minded on either shortening the qualifying period after which a company could be floated, or perhaps considering some amendment in the claw back rules. The Financial Secretary has slightly amended the draft reply to Sir Nicholas Goodison to reflect his willingness

to keep this point under review.

MED
M E DONNELLY

RESTRICTED

FROM: M E DONNEL
DATE: 23 June 19

IMMEDIATE

MR UNWIN

VISIT BY FINANCIAL SECRETARY TO GREECE

This note is to bring you up to date on developments.

We have been exploring how the Finance Bill obligations which the Financial Secretary has can be reconciled with the Athens trip.

After considerable negotiations with the Whips, and informal talks with the Opposition, I am afraid it looks as though 12-13 July are likely to be Committee days of the Finance Bill. We will not know this for certain until a week or so before hand; but the chances of the Financial Secretary being free are really not high enough to continue planning on the basis of those two days. The Financial Secretary himself while wishing to go to Athens for talks, does not feel that he can set aside his finance bill responsibilities.

I have been informally exploring a further option with the Foreign Office. As you know Mr Rifkind to travelling out on the Monday, with his programme of talks on the Tuesday (July 12). He will be giving a dinner for Mr Varfis on the Monday evening. It might be possible for the Financial Secretary to travel out on the Sunday 10 July, hold talks with Mr Roumeliotis during the Monday and attend the dinner for Mr Varfis in the evening possibily talking informally to him then. He could then return first thing on Tuesday morning (£9.00 p/m, arrives London 10.45 AM).

The Financial Secretary is happy for this possibility to be explored. Mr Rifkind's private Secretary will float the idea with him.

All this is of course contingent on your views; and those of Foreign Office officials here and in Athens. But it seems worth pursuing.

MED
M E DONNELLY

– Mr Unwin

We spoke. Mr Rifkind's Office tell me that dinner with Varfis on the Monday evening is probably not on, because Varfis is taking Rifkind out informally. But Mr Rifkind has no objection to the FST meeting Varfis separately, say during Monday afternoon. And no FCO objection to the general idea of the FST going out earlier in the week.

So the way seems clear for you to approach the Athens Embassy about the revised dates.

MJ
23/6

Treasury Chambers, Parliament Street, SW1P 3AG

Evan Sutherland Esq
Office of Parliamentary Counsel
36 Whitehall
LONDON
SW1A 2AY

23 June 1983

Dear Sutherland,

INTERNATIONAL MONETARY ARRANGEMENTS

... I enclose a money resolution for this Bill duly initialled by the Financial Secretary.

Yours Sincerely
E Kwiecinski

E KWIECINSKI
Private Secretary

INTERNATIONAL MONETARY ARRANGEMENTS [MONEY]: Queen's Recommendation signified

Mr Nicholas Ridley

That, for the purposes of any Act of the present Session to substitute a new limit for the limit on lending to the International Monetary Fund imposed by section 2(1) of the International Monetary Fund Act 1979 and to provide for the Bank of England to be indemnified in respect of certain financial assistance, it is expedient to authorise any increase attributable to the Act of the present Session in the sums charged on the Consolidated Fund or payable into or out of that Fund or the National Loans Fund.

18.4.83

Treasury Chambers, Parliament Street, SW1P 3AG

D W Saunders Esq
Office of Parliamentary Counsel
36 Whitehall
LONDON
SW1A 2AY

23 June 1983

Dear Saunders,

HOUSING AND BUILDING CONTROL BILL

...I enclose a money resolution for this Bill duly initialled by the Financial Secretary.

Yours sincerely
Eric Kwiecinski

E KWIECINSKI
Private Secretary

HOUSING AND BUILDING CONTROL [MONEY]: Queen's Recommendation signified

Mr Nicholas Ridley

That, for the purposes of any Act of the present Session to make further provision with respect to the disposal of, and the rights of secure tenants of, dwelling-houses held by local authorities and other bodies in England and Wales and to amend the law of England and Wales relating to the supervision of building work, the building regulations and building control, it is expedient to authorise -

(1) the payment out of money provided by Parliament of -

(a) any expenses incurred by the Secretary of State in providing assistance in relation to any proceedings or prospective proceedings;

(b) the administrative expenses of the Secretary of State under that Act;

(c) any increase attributable to that Act in the sums so payable under any other enactment;

(2) the payment of any sums into the Consolidated Fund;

(3) the payment out of or into that Fund or the National Loans Fund of any increase attributable to that Act in the sums so payable under any other enactment.

21 6 83

cc PS/Chancellor
PS/CST
PS/EST
Mr Robson
Mr Green
Mr Beighton
Mr Lawrence
Mr Bryce
Mr Northend
Mr Prescott
Mr Ballarsby
PS/IR
} IR

Treasury Chambers, Parliament Street, SW1P 3AG

Sir Nicholas Goodison
Chairman
The Stock Exchange
LONDON
EC2N 1HP

23 June 1983

Dear Nicholas

Thank you for your letter of 14 June and your suggestions on what is now the Finance Act 1983. I very much appreciated your words of support for the Business Expansion Scheme, and the Employee Profit-sharing Schemes.

Business Expansion Scheme

I appreciate your concern that companies should not be discouraged from going to the market when the time is ripe by the existence of BES equity. This is especially true if the company is ready for further expansion and its purpose in going to the market is to raise additional equity to finance that expansion. But it strikes me as going too far to suggest that there should, therefore, be no period for which a company under the Business Expansion Scheme must remain unquoted. That would be tantamount to extending the Scheme to all prospective quoted companies and would moreover be but a short step from including all existing quoted companies as well.

As you know, the fundamental purpose of the Scheme, and the generous relief available to investors under it, is to encourage new equity in companies which do not otherwise have ready access to sources of new equity. Clearly, a company which has secured access to the Stock Exchange itself or to the Unlisted Securities Market does not face this difficulty. So we thought it right to exclude such companies from the Scheme. It follows, therefore, that as the Scheme is for unquoted companies only, a company must remain unquoted for some minimum period.

As an alternative to having no qualifying period, you suggest that the period could be reduced from 3 years to 1 year. I readily accept that the appropriate duration for the qualifying period is, ultimately, a matter of judgement. But a period of only 1 year seems a

bit short, bearing in mind that another of the reasons for the very generous scale of the relief under the Scheme is to help compensate for the extra risk attaching to equity investment on a reasonably long term basis (the shares must be held for at least 5 years) in unquoted companies whose shares, by definition, lack marketability. A qualifying period of only one year could also cause difficulties as regards other features of the Scheme, notably the requirement that (for good reasons) a company has to satisfy certain other qualifying conditions for at least 3 years and, in certain circumstances, for longer than this.

Thus, I recognise that there is a valid point of concern here to the Stock Exchange. I am not yet certain what the desirable time should be for which a company under the Scheme should remain unquoted. I accept that this is a point that should be kept under review, and we can return to it next year.

Capital Gains Tax

I have noted the comments in your covering letter about the continuation of the tax in its present form. Clearly as the indexation provisions increasingly remove purely nominal gains from the tax charge this is something which we will need to study carefully. But I would not want to underestimate the difficulties of securing an equitable and acceptable regime for the taxation of real capital gains.

On the specific point about pooling you will recall that in my letter to you of 17 March enclosing the draft provisions introducing a form of pooling of securities for capital gains tax indexation purposes, I said why I thought it right to limit their availability to companies. I fully recognise that the present indexation provisions can be highly complicated for individuals and I am always ready to consider any proposals for their simplification. But I remain unpersuaded that these pooling provisions - directed as they are towards the particular problems of large institutional investors - fall into that category.

Yours ever
Nicholas

NICHOLAS RIDLEY

FROM:
THE RT. HON. LORD HAILSHAM OF ST. MARYLEBONE, C.H., F.R.S., D.C.L.

LORD CHANCELLOR

HOUSE OF LORDS,
SW1A 0PW

23rd June, 1983

FINANCIAL SECRETARY	
REC.	24 JUN 1983
ACTION	MR. HOPKINSON
COPIES TO	CST MR. MIDDLETON MR. BAILEY MR. WALDING MR. PESTELL MR. JUDD MR. FITCHEW MR. MEADOWS.

The Right Honourable
Nicholas Ridley, MP
Financial Secretary to the Treasury,
Treasury Chambers,
Parliament Street,
London,
SW1P 3AG.

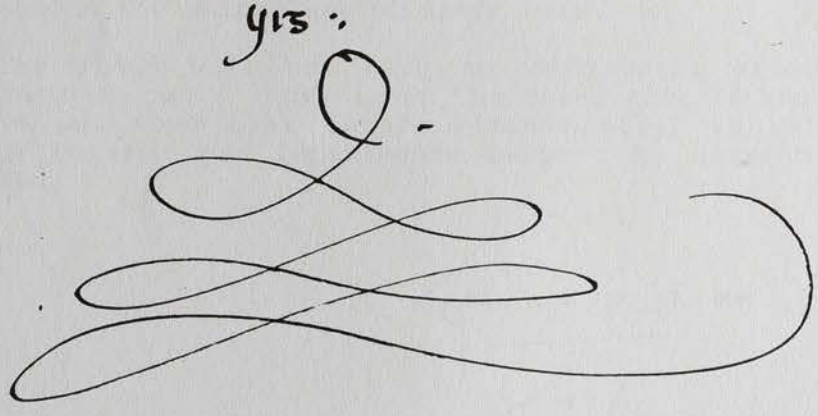
My dear Nicky.

You wrote to Patrick Jenkin on 16th June, that letter being copied to me, seeking agreement to the form of a Treasury Minute on dog licensing.

The simplest course is the best. Dog licences are unnecessary and their abolition would save £2 million. Collars with names and addresses are already obligatory independently of the licence. The Control of Dogs Order 1930 requires the wearing of a collar bearing the owner's name and address: the maximum fine is £400. There is therefore no need for a licence at all and the abolition of the nuisance would be a boon to dog owners, save the taxpayer money, and the Government the unpopularity of raising the charge.

I am copying this letter to the recipients of yours.

Yrs.



NG

DEPARTMENT OF THE ENVIRONMENT
2 MARSHAM STREET
LONDON SW1P 3EB
01-212 7601

MINISTER FOR HOUSING AND CONSTRUCTION

FINANCIAL SECRETARY	
REC.	-7 JUN1983
ACTION	Mr CORLETT IR
COPIES TO	PPS MST R CST
	Mr HOBSON
	Mr BATTISHILL IR
	RS/IR

My Ref: ST/PSO/42826/83

-6 JUN 1983

Dear Nicholas.

Thank you for your letter of 16 May in response to mine of 5 May about industrial building allowances.

The NEDO paper I enclosed had not been adequately thought through by its authors, and we had picked up several possible interpretations of its proposals at the detailed level. I accept that one could interpret it to mean virtually that a 25% initial allowance would be available on an essentially commercial building, and I understand your objections to that idea. However, I am fairly certain that that was not what NEDO had in mind. They still see the concession as relating to ancillary uses in primarily industrial buildings, and I still believe there is some substance in the main plank of their case.

As you say, the issue will now have to wait until after the election. Perhaps we could leave it on the basis that if and when an amendment is put down to a future Finance Bill, it will be discussed again between our Departments before the Government's view is finalised.

Yours ever

John

JOHN STANLEY

The Rt Hon Nicholas Ridley

01 211 6402

FINANCIAL SECRETARY	
MP/REC.	13 MAY 1983
ACTION	MR. EDWARDS
COPIES TO	MR. UNWIN
	MRS. HEDLEY-MILLER
	MISS COURT
	MR. PEET
	MISS WILKINSON

The Rt Hon Nicholas Ridley MP
Financial Secretary to
The Treasury
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

13 May 1983

EUROPEAN PARLIAMENT: POSSIBLE VISIT BY MEMBERS OF BUDGETS AND BUDGET CONTROL COMMITTEES

Thank you for copying to me your letter of 4 May to Douglas Hurd. I have no objections to a September visit by MEPs for a programme of the type you have outlined although I agree we should await events in June before issuing any invitation.

My only other comment is that we should try to forestall this invitation's triggering off numerous requests from other MEPs to visit energy projects; the Court of Auditors' and Commission's inspections already promise to create plenty of work for the industries. I suggest, therefore, that we should offer a proportion of the places in September to members of the Energy and Research Group, who, I know, maintain an enthusiastic interest in Budgetary matters.

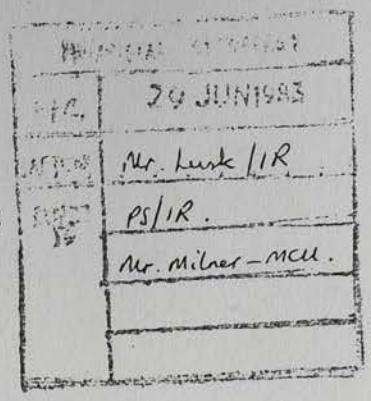
Copies of this letter go to recipients of yours.

Yours ever
Nigel

NIGEL LAWSON

HOUSE OF COMMONS
LONDON, SW1

24th June 1983



Dear Nick

Taxation of Holiday Lettings

I am not sure whether these matters are still part of your responsibilities. However, you will no doubt recall your reply to myself and Walter Clegg on this subject on 11th May. I enclose a photostat of the appropriate passage from Hansard.

The information which you gave on that occasion was most welcome in Blackpool and, I suspect, many other seaside resorts. However, those affected in Blackpool have been to see me and have presented me with copies of notes of a meeting at Somerset House and other opinions which raise doubt as to what our intentions are.

I would be most grateful if you could let me know what is the Government's intention with regard to holiday lettings and exactly what provisions will apply to this section of the self-catering holiday industry. From reading your helpful statement in the House, I thought there were no difficulties and have some problem in seeing the difficulties which are apparently being put up by Somerset House.

I would be most grateful for your reply before I discuss the matter again with my trades people in Blackpool.

Yours ever

Norman Miscampbell, M.P.

Nicholas Ridley Esq., MP,
Financial Secretary to
The Treasury

TAXATION OF HOLIDAY LETTINGS

NOTES OF MEETING HELD AT SOMERSET HOUSE ON 13 JUNE 1983

PRESENT AT MEETING

Inland Revenue - Mr R G Lusk, Policy Division
- Mr J Bryce, Policy Division
- Mr I Spence - Policy Division
- Mr P Tyrer, Technical Division
- Mr E Walker, Technical Division
- Miss A Rhodes, Policy Division

Binder Hamlyn - Mr J Norton
- Mr F Govan

English Tourist Board - Mr S Mills
- Mr H Norton

Cumbria and Lakeland Self Catering Association - Mr P Dean

PURPOSE

The purpose of the meeting held at the request of the English Tourist Board was to discuss proposals prepared by Messrs Binder Hamlyn on behalf of a working party representing the views of the English, Wales and Scottish Tourist Boards, the Highlands and Islands Development Board and self-catering holiday associations from principal tourist areas of the country.

INTRODUCTORY STATEMENTS

Mr Mills opened the meeting by describing the concern of the tourist boards and all those in the business of holiday lettings at the implications arising from the cases of Griffiths v Jackson and Gittos v Barclay. The judgements in these cases made it impossible for Inland Revenue to assess holiday lettings on any basis other than Schedule D Case VI, although Schedule D Case I treatment had prevailed previously in many parts of the country. He stressed the importance of the holiday lettings sector of the tourist industry, pointed to the increasing level of competition from overseas and stated that there was a strong economic argument for treating holiday lettings on the basis of a trade.

Mr Lusk, while referring to the carefully worded, but positive statement by Mr Nicholas Ridley in the debate on the Finance Act in the last Parliament, stated that:

- There could be no certainty that the new administration would wish to pursue Mr Ridley's proposals, although this would be given consideration.

- It should not be assumed that a fundamental change in the Law beyond Mr Ridley's statement was in prospect.

- At that day's meeting it was necessary to concentrate on agreeing definitions and to leave it to the Ministers concerne to decide how far they were to go in implementing change.

DETAILED CONSIDERATION OF BINDER HAMLYN'S PROPOSALS

Clarification was sought by Inland Revenue on a number of specific issues:-

- Further explanation was given of the figures shown in Appendix 1 to the Binder Hamlyn paper, clarifying that the "number of sites" did not necessarily relate directly to the number of owners although there was likely to be a close correlation particularly where the number of letting units on site was small.

- The question of personal supervision and involvement of the proprietor in the business was raised by Inland Revenue. Mr Norton repeated that the case presented was essentially an economic argument and that it would be wise to avoid too much attention to the definition of personal supervision which could give rise to difficulty.

- Inland Revenue questioned the extent to which economic damage arising from the current situation could be quantified. It was agreed that the present state of uncertainty was prejudicing future investment, although it was unlikely that there was any actual reduction in stock so far since most existing operators were hopeful that the Law would be changed in their favour. It was again stressed that European competit was intense and that a function of the tourist boards was to encourage improved standards and value for money and that this required favourable tax treatment.

- When asked to place in order of importance the various tax reliefs which might be made available, Mr Norton agreed that earned income relief, roll-over relief and retirement relief, which had been offered by Mr Ridley in his statement to the House of Commons, would go a considerable way towards alleviating the problem, but that capital allowances and the ability to offset these, together with losses, against other income were also most important particularly where the holiday lettings were only part of a total business activity. He made the point that depreciation allowances restricted to 10% of letting incomewere likely to be too low and that regular replacement and refurbishment was essential if standards were to be maintained. Mr Dean also considered the ability to off-set losses to be highly desirable.

- There was a brief discussion on the extent to which owners and operators of self-catering accommodation generally were disadvantaged by comparison with hotels and that problems of obsolesence caused by changes in fashion affected this sector of the tourist industry as much as any other business. Mr Mills mentioned the fact that the range of equipment required by one of the major holiday lettings agencies increase each year in line with market demand.

- Mr Lusk queried why standards continued to be too low as argued by the tourist boards if Case I treatment had been allowed for a great many owners of holiday lettings in past years. Mr Mills replied that standards were in fact improving, but that many small businesses were highly marginal and that a change in previous Inland Revenue practices would prejudice further improvement.

SPECIFIC CRITERIA

The meeting then went on to discuss the criteria proposed by Binder Hamlyn to establish a new trade of holiday lettings.

- Holiday Accommodation

  Binder Hamlyn had referred to the VAT legislation under the Finance Act 1972. It was made clear that the wording set out in this legislation provided a useful form of words, but it was not intended to link the present changes to VAT in any way.

- Short Lettings

  This was based on the wording of Section 38 FA 1978. Inland Revenue queried whether this would preclude the occasional letting to a repeat customer in the same season but it was agreed that the word "normally" should allow for this event.

  There was considerable discussion on the length of period during which the premises should be open for letting. The point was made that the words "open" or "available for letting" were preferable to insisting on a specified number of weeks during which the property would be let. Levels of usage during the holiday season varied in different parts of the country and were likely to be lowest during the first year.

  The question of student lettings was raised. It was agreed that apportionment of income was undesirable and in any case impracticable. Mr Norton suggested that it might be acceptable to limit Schedule D Case I assessment to those businesses earning at least 75% of total gross income from genuine holiday lettings.

Inland Revenue would prefer the "four month" qualifying pe
to be increased to six months. Mr Mills referred to the
split season in parts of Scotland, particularly Aviemore a
that it would be unwise to specify particular months in th
year. Mr Lusk's view was that the word "season" should be
retained.

- Furnishings

It was agreed that accommodation must be furnished to count
as holiday letting. Inland Revenue queried whether there
should be an established minimum standard. Mr Norton's
view was that this should be left to market forces and
Mr Mills stated that minimum standards could vary over time
There was discussion on the definition of a unit of accommc
It was suggested that qualifying units should be wholly sel
contained, including cooking, sleeping, washing and WC faci
It was recognised that not all holiday letting accommodatio
currently met this criterion.

- Use of Property by Proprietor

This and the following criterion were introduced as a means
of disallowing second home owners and those investing in
retirement homes. This was agreed to be desirable. The
point was made that the owner should be allowed to move
in for short periods to arrange for decoration. The case w
raised by Inland Revenue of the man buying a house, offerin
it for holiday lettings in the first year of ownership and
thereby claiming all available capital allowances, and then
adopting it as his permanent residence in the second or thi
year. It was agreed that if the self-catering unit became
a main or secondary residence within (say) six years, then
reliefs, including capital allowances should be clawed back.
It was agreed that this could present problems and that the
balancing charge was normally based on market value which
could be significantly less than cost. Inland Revenue would
consider how this could be overcome.

- Market Rent

It was agreed that this was a necessary criterion to
establish a bona fide trading activity at arm's length.
It was agreed also that the rules would apply to companies,
partnerships and sole traders.

CONCLUSION

The problem of personal supervision arose on a number of occasion
Mr Lusk stated that in his view a definition relating to personal
supervision would help the case for assessing holiday lettings
as a trade. He suggested that this was the major distinguishing
factor which separated holiday lettings from other forms of renta
income. The short term nature of the lettings increased the degr
of supervision required. The point was made that in Law there wa

no real difference betwe n carrying out an activity personally and carrying it out through an agent and that insistance on personal supervision could lead to considerable hardship. Mr Norton referred to the original recommendation of the tourist board's working party that personal supervision should be required where the number of units involved did not exceed three, but that over three units this could not sensibly apply. No real conclusion was reached on this point.

Mr Lusk was unable to commit the Inland Revenue to any particular course of action, but undertook to consider carefully the proposals which had been put forward. He thanked the tourist board's representatives for their advice. He would now be drafting a suitable statement for consideration by the Minister which would take account of the views expressed.

Clause 98

SHORT TITLE, INTERPRETATION, CONSTRUCTION AND REPEALS

Manuscript amendment made: In page 79, line 20, leave out "other than section 87".—*[Mr. Wakeham.]*

Clause 98, as amended, ordered to stand part of the Bill.

New Clause 4

TAXATION OF HOLIDAY FLATS (1)

'The use of land in the United Kingdom for the purposes of furnished holiday accommodation shall, if the land is managed on a commercial basis and with a view to the realisation of profits be treated as carrying on a trade or as the case may be part of a trade and the profits or gains thereof shall be charged to tax under class 1 of Schedule D.'.—*[Sir Walter Clegg.]*

Brought up, and read the First time.

The Chairman: 'With this we are to take new clause 5—*Taxation of holiday flats (2)*

'Profits and gains arising out of or from the use of land in the United Kingdom for the purposes of furnished holiday accommodation shall be charged to tax under class 1 of Schedule D.'.

Sir Walter Clegg (North Fylde): I beg to move, That the clause be read a Second time.

The purpose of the amendment is somewhat technical, and I have had some correspondence about it with the Financial Secretary. It is a matter that much concerns those who operate holiday flatlets in seaside resorts and, indeed, in all resort areas of the country.

Confusion seems to have arisen about how the income from these holidays lettings should be taxed. The intention of the new clause is to tax that income as a realisation of profit and for the operation to be treated as carrying on a trade or, as the case may be, part of a trade, and the profits gained therefrom taxed under class 1 of schedule D.

If the new clause were not accepted, these profits could be taxed as investment income, and that would have a drastic effect on the running of these holiday flatlets, which are now very much part of life in our resorts. I have tabled the new clause to obtain clarification and in the hope that my right hon. Friend will tell us that the profits should be taxed under class 1 of schedule D and not as investment income.

Mr. Ridley: I am grateful to my hon. Friend for giving me the opportunity to set out briefly the law as I think it is now, and then to say a word about the Government's intentions.

There is no doubt that the holiday lettings that my hon. Friend has in mind are probably taxable under case 6, and that the income would attract investment income surcharge, as long as the services provided to the tenants are not on such a scale as to turn the nature of the operation into a trade. There are probably many instances, on the strict interpretation of the law, that is true and the people concerned are not trading. My hon. Friend the Member for Bridlington (Mr. Townend), who has been assiduous in these matters, brought to our attention a recent case which suggested to him that somehow the law was changed by that case. A more likely interpretation is that the Revenue's view of the law was merely confirmed by that case. It is difficult to draw the line, both for taxpayers and tax inspectors.

My right hon. and learned Friend and I have been considering the matter with great care. We have decided, as a result of the strong and persuasive representations by my hon. Friends, to change the law in the way that they want. At a suitable opportunity we intend to bring forward proposals to change the law so that those carrying on a business of furnished holiday lettings will, in general, be able to claim capital gains tax retirement relief and relief on replacement of business assets, and to have their income from such a business treated as earned income, whether or not they are carrying on a trade.

I regret that it is not possible to bring the new clause into effect in the Bill, but the Committee will know the reason why that is so. The Bill's life is not likely to be as long as it should be before it becomes an Act, when the necessary complicated, technical drafting could be done. The Government are putting forward a complicated proposition. I regret to have to inform my hon. Friend that, perfect though his intentions are, his draftsmanship is not quite perfect. I am afraid that we shall have to return to this matter and put it right at a later opportunity. I am grateful to all my hon. Friends who brought the matter to the Government's attention. I hope that my announcement will be of comfort to them and to those whom they represent, who have been living in uncertainty about the law and the future.

Mr. Norman [illegible] (North): In putting my name to the new clause, I was responding to the considerable worry felt in my constituency and the contiguous constituency by those who are running the holiday business of self-catering flats, which is perhaps the business that is expanding most. In many cases a great deal of assistance is provided, but there is still a fear that the profits will be taxed as investment, with all the natural disadvantages of such a tax imposition.

We understand that it is not possible to make a change in the Bill. It may take a little while before there is a properly drafted clause. We knew as well as anybody else that the clause would not do. It was not our purpose to pass the new clause. Our purpose was to elicit a response from the Minister. What a generous response we have had.

When many hard-working people in charge of prosperous little businesses find out what has happened in Committee today, they will be pleased and will welcome the Minister's words. It is not often, when a new clause is moved, that the Minister says that the Government will change the law the way set out. I welcome that. If the law is changed the way we want, many people in Blackpool will be delighted. I extend my congratulations and thanks to the Government for what they have done. We fully understand why there must be a delay.

Sir Walter Clegg: I thank my right hon. Friend for the attitude that he has taken. In view of his reply and with the consent of the Committee, I beg to ask leave to withdraw the motion.

Motion and clause, by leave, withdrawn.

7.15 pm

Sir William Clark (Croydon, South): New clause 10, entitled "Rate of development land tax," is a most important new clause, but I fully realise, as I am sure my hon. Friends do, that at this late stage it is extremely difficult to pass all the proposals on the Finance Bill because Parliament must dissolve on Friday. However,

English Tourist Board

The Statutory Tourist Board for England

Mr D A Cummins
Donald A Cummins & Co
76 Buchanan Street
BLACKPOOL
FY1 3DG

16 June 1983

Dear Mr Cummins

HOLIDAY LETTINGS

As you know, we met with members of the Policy Division of Inland Revenue on Monday. I was accompanied by John Norton and Frank Govan of Binder Hamlyn, together with Mr Peter Dean of the Cumbria and Lakeland Self-Catering Association, who has taken a very close interest in this question since it first came to light.

In my view the meeting was useful, but by no means conclusive. It was quite apparent that neither Mr Lusk or his colleagues were prepared to commit their new Ministers in advance. It also became clear that they continue to dislike the idea of giving way to the very strong arguments presented for assessment under Schedule D Case 1. Mr Nicholas Ridley's statement referred specifically to the ability of owners to claim Capital Gains Tax retirement relief and relief for replacement of business assets and for income from such a business to be treated as earned, "whether or not they are carrying on a trade". I am therefore by no means certain that our arguments will prevail, although the mechanism for assessing holiday lettings, as a trade, subject to appropriate definition, seems relatively straightforward.

We were pressed hard on the question of personal supervision and involvement of the proprietor which appears to be central to current Inland Revenue thinking. We made the point that in Law there is no difference between the man who carries out an activity on his own behalf and an agent acting for him.

Attached are notes of the meeting, together with a copy of my subsequent letter to Mr Lusk which reiterates certain of the points made. I am proposing that our Chairman should write to the Chancellor of the Exchequer direct and I hope to let you have a copy of his letter in due course. We are also recommending that pressure should be brought to bear from the other Tourist Boards. No doubt you will wish to add weight to this.

Continued . . ./2

4 Grosvenor Gardens London SW1W 0DU Telephone 01 730 3400 Telex 266975 E T B G

I must finally apologise for the relatively short time allowed for consultation between us but I hope you will agree that we have represented your views reasonably fairly. I very much hope that our co-ordinated approach will bear fruit.

Kind regards.

Yours sincerely

Stephen Mills

Stephen Mills
Assistant Director (Development)

P.S. I believe Mr. Goren has now written to you on the points raised in your letter.

16 JUN 1983

Binder Hamlyn

Chartered Accountants

8 St Bride Street
London EC4A 4DA

Telephone: 01-353 3020
Telex: 24276 Binder G
LDE Box No 166

D.A. Cummins Esq FCCA, ATII
Donald A. Cummins & Co
Certified Accountants
76 Buchanan Street
BLACKPOOL FY1 3DG

Your ref

14th June 1983

Our ref FJG/ER

Dear Mr Cummins

FURNISHED HOLIDAY LETTINGS

Stephen Mills of English Tourist Board has asked me to reply to your letters of 27th May and 7th June. I have tried to summarise the contents of your two long and interesting letters under the following headings.

1. Present law and practice

Although I agree with you that the legal background on the taxation of lettings generally is somewhat confused and tortuous I do think that ultimately it has become clear that the exploitation of property by means of letting cannot be assessed under Case I Schedule D and is more properly attributable to Schedule A. There is of course specific authority within s.67(1)4 TA 1970 for assessing such income within Case VI Schedule D unless the landlord elects to the contrary. I do not see that it is possible to distinguish income from holiday lettings from letting income generally - there are certain features which are more akin to a trade but they are not in my view sufficient to overcome the trend established by the recent cases. To my mind the situation is clinched by the case of Griffiths v Jackson (STC 1983 page 184). Unfortunately there is a widespread impression that this case related only to student letting but in practice the lettings involved not only student accommodation but a purpose built block of holiday flats which were let on a normal short term basis. I gather from Mr Pearman (one of the defendants) that both Commissioners and the courts were fully aware of this type of letting during the course of the appeal but unfortunately these facts have not come out clearly in the case stated. At any rate I do not see any way in which I could disagree with Lord Justice Vinelott when he reaches the conclusion that the activity of letting furnished flats or rooms is not a trade although it is a demanding and time consuming business. In my view therefore the law on the matter is clear.

D.A. Cummins Esq FCCA, ATII
Donald A. Cummins & Co

14th June 1983

I think that the problem arises not so much from the legal background as from the long standing Inland Revenue practice which has been to treat certain types of holiday letting as being within Case I Schedule D. I must say that I think you have been favourably treated in Blackpool if you cannot recall a case where the provision of furnished holiday lettings has not been treated as a trade. I can assure you that the position in the country as a whole is very different. There is no clear pattern to the Inland Revenue and discretion has obviously been left to local Inspectors to do the best deal that they could. This has resulted in a very uneven treatment throughout the country as a whole giving rise to a great deal of unhappiness from taxpayers who can see that they are being treated badly as compared with their competitors.

2. Mr Ridley's statement

I think it is important not to be too optimistic about the statement made by Mr Ridley in the House on 11th May. A careful reading of the statement will make it clear to you that it is not a commitment to treat holiday lettings as a trade. In fact he is specifically committed only to:

Capital gains retirement relief
Capital gains relief for replacement of business assets
Earned income treatment for income tax purposes

This of course from our point of view is most unsatisfactory since it omits a number of important reliefs such as capital allowances on machinery and plant, interest relief and also restricts the use of losses. I can assure you however that this is the way in which the Inland Revenue interpret the statement (which in any case I believe was drafted by Inland Revenue Policy Division).

3. Your own clause

It may now be a little clearer to you why your own clause was not found acceptable by them. Not only did it commit them to trading status but for reasons which I fully understand it did not seek to restrict that trading basis to the tourist industry. It has been made very plain to us that if we are to succeed we will have to devise an acceptable definition of a trade which will in effect confine relief to the tourist industry and will act as a ring fence against the aspirations of others who are in the property business. I cannot tell you specifically what the Inland Revenue have to fear in this area but I would not be surprised if they had their eye on the large property groups who could easily adapt serviced lettings in London to meet the conditions imposed by your clause.

4. Recent developments

For this reason we have therefore spent a great deal of time and effort in trying to design a definition which would both be watertight

D.A. Cummins Esq FCCA, ATII
Donald A. Cummins & Co

14th June 1983

and would also stimulate the tourist industry as far as possible. Representatives of the working party did in fact have a long meeting with Inland Revenue Policy Division yesterday when our report was discussed in detail. You will receive a full report of the meeting in due course from English Tourist Board but I can tell you at the moment that we have still not yet definitely succeeded in establishing trading status - the Inland Revenue are most reluctant to move on this one (for reasons which they are unwilling to explain fully). They have however taken our points fully on board and have promised to give us their reaction in due course - if time permits before a clause is enacted. English Tourist Board will also wish to consider their position to see whether an alternative approach should be made via government ministers.

In conclusion may I say that both your letters were discussed in detail by members of the working party before the meeting and that they found the contents most helpful.

Yours sincerely,

F.J. Govan
Senior Tax Consultant

cc: S. Mills

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

From the Minister

The Rt Hon Nicholas Ridley MP
Financial Secretary to the Treasury
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

FINANCIAL SECRETARY	
REC.	23 JUN1983
~~ACTION~~	MR. HOPKINSON
COPIES TO	CST
	MR. MIDDLETON
	MR. BAILEY
	MR. WILDING
	MR. PESTELL
	MR. JUDD
	MR. FITCHEW
	MR. MEADOWS

23 June 1983

Thank you for sending me a copy of your letter to Patrick Jenkin of 16 June with which you enclosed alternative draft texts of a Treasury response to the PAC Report on dog licensing.

There is no doubt that the present position is indefensible and that the PAC Report means that something should now be done. I therefore entirely agree with you that H Committee should look at the problem as quickly as possible in the new Parliament.

Indeed I think that is the essential thing. I doubt very much whether it would help the Government to issue a Treasury minute for the moment in either of the forms suggested. I think that the right course would be to set up the H Committee discussion quickly and to decide how and when to reply to the PAC in the light of that discussion.

Incidentally when the time for the Treasury minute does arrive it should take account of the fact that my responsibilities are limited to England. The reference to MAFF in the first paragraph would be better as, "and the other Departments with responsibility for dog licensing".

I have copied this letter to members of H Committee, Jim Prior and Sir Robert Armstrong.

MICHAEL JOPLING

RESTRICTED

FROM: M E DONNELLY
DATE: 23 June 1983

PRINCIPAL PRIVATE SECRETARY

cc PS/Economic Secretary
PS/Mr Middleton

TAX POLICY: DIVISION OF RESPONSIBILITY

In the light of the division of responsibility agreed between Treasury Ministers, the Financial Secretary and the Economic Secretary have agreed how this should be put in practice in dealing with current taxation policy issues.

... The attached note sets out the detailed position. Item 3 lists those areas where for the sake of continuity through the Finance Bill period the Financial Secretary will remain in the lead until the Summer recess.

These arrangements have been discussed with Mr Middleton, who is content. If the Chancellor is also content, and subject to any comments he may have, I propose to circulate the attached note to officials concerned in these areas.

MED

M E DONNELLY

TAX POLICY: DIVISION OF RESPONSIBILITY

1. FINANCIAL SECRETARY

   (a) Schedule D/Schedule E borderline

   (b) Schedule D self-assessment

   (c) Corporation Tax self-assessment.

2. ECONOMIC SECRETARY

   (a) Payroll Taxes

   (b) Corporate Bonds

3. UNTIL SUMMER RECESS: FINANCIAL SECRETARY

   SUBSEQUENTLY: ECONOMIC SECRETARY

   (a) Business Expansion Scheme, and other "enterprise" measures

   (b) Capital allowances

   (c) Purchase of Own Shares, Employee Share Schemes etc.

CONFIDENTIAL

FROM: M E DONNELLY
DATE: 24 June 1983

PS/CHANCELLOR

cc PS/Chief Secretary
PS/Economic Secretary
PS/Minister of State
Mr Middleton
Mr Cassell
Mr Monck
Miss Kelley
Mr Pirie
Mr Jones
Mr Saunders
Mr Thomas
Mrs Jutsum

FRAUD

The Financial Secretary has seen Mr Middleton's minute of 16 June and the Economic Secretary's comments of 21 June.

The Financial Secretary agrees with the Economic Secretary that responsibility for the new investigation and prosecution unit should lie with the Secretary of State for Trade and Industry. But he is less certain about the overall advantages of preserving trial by jury in fraud cases.

MED
M E DONNELLY

CONFIDENTIAL

FROM: M E DONNELLY
DATE: 24 June 1983

CHIEF SECRETARY

cc Chancellor
Economic Secretary
Minister of State
Mr Middleton
Mr Bailey
Mr Battishill
Miss Kelly
Mr Mountfield
Mr Faulkner
Mr Stannard
Mr Willetts
Miss Everest-Phillips

STUDENT LOANS

The Financial Secretary has seen Mr Faulkner's submission of 22 June.

He agrees that the idea of a student loan scheme should be pursued. But given that even such modest proposals as those suggested by Mr Faulkner are likely to produce a public outcry, he wonders whether tactically it might not be as well to go for a more ambitious scheme raising considerably more revenue - so at least being hung for a sheep rather than this little lamb.

MED
M E DONNELLY

CONFIDENTIAL

FROM: E KWIECINSKI
DATE: 24 June 1983

PS/CHIEF SECRETARY

cc PPS
Economic Secretary
Minister of State
Mr Bailey
Mr Wilding
Mr Mountfield
Mr Middleton
Mr Cassell
Mr Battishill
Mr Monger
Ms Seammen
Mr Martin
Mr Robson
Mr Aaronson
Mr Hall
Mr Spence - IR

TCSC REPORT
THE STRUCTURE OF PERSONAL INCOME TAXATION AND INCOME SUPPORT

The Financial Secretary has seen Mr Robson's submission of 23 June.

He has commented that this shows how complex the question is. He thinks that it can be answered in three parts:

i) by not worrying about the traps so much - they are secondary problems;

ii) by increasing the personal allowances as much as possible; and

iii) by looking at the benefits to see why they are so high for some.

E KWIECINSKI

CONFIDENTIAL

FROM: E KWIECINSKI
DATE: 24 June 1983

PS/CHIEF SECRETARY

cc PPS
Economic Secretary
Minister of State
Mr Bailey
Mr Wilding
Mr Mountfield
Mr Middleton
Mr Cassell
Mr Battishill
Mr Monger
Ms Seammen
Mr Martin
Mr Robson
Mr Aaronson
Mr Hall
Mr Spence - IR

TCSC REPORT
THE STRUCTURE OF PERSONAL INCOME TAXATION AND INCOME SUPPORT

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ii) by increasing the personal allowances as much as possible; and

iii) by looking at the benefits to see why they are so high for some.

E KWIECINSKI

FROM: M E DONNELLY
DATE: 24 June 1983

PS/CHIEF SECRETARY

cc PS/Economic Secretary
PS/Minister of State
Mr Bailey
Mr Battishill
Mr Monger
Mr Mountfield
Mr Robson
Mr Norgrove
Mr Hall
Mr Salveson
PS/IR
PS/C&E

FINANCE BILL: TIMETABLE AND BRIEFING

The Financial Secretary has seen your note of 23 June to Mr Martin.

He thinks that in his opening speech next week the Chief Secretary might take as a central theme of his speech the fact that the Bill is simply needed to restore what the irresponsible Opposition knocked out before the election. So the whole affair is simply an exercise in putting right what should always have been.

MED
M E DONNELLY

FROM: M E DONNELLY
DATE: 24 June 1983

PS/CHIEF SECRETARY

cc PS/Chancellor
PS/Economic Secretary
PS/Minister of State
Mr Middleton
Mr Bailey
Mr Wilding
Mr Mountfield
Mr Monger
Ms Seammen
Mr Ridley

PENSIONERS EARNINGS RULE AND SOCIAL SECURITY UPRATING

The Financial Secretary has commented that over the longer term we will need to review our attitude to the earnings rule in relation to pensioners. He considers that if we are to go for job release schemes, early retirement, lowering of the pension age and other such provisions it will be essential for people to actually retire from employment before they are allowed to claim their pensions. The only test of genuine retirement is the earnings rule. Consequently further erosion of the earnings rule makes Government initiatives in the early retirement area more difficult and more expensive.

MED
M E DONNELLY

FROM: M E DONNELLY
DATE: 24 June 1983

MR JUDD

cc PPS
PS/Chief Secretary
PS/Economic Secretary
PS/Minister of State
Mr Middleton
Mr Bailey
Mr Wilding
Mr Battishill
Mr Lovell
Mr Pestell
Mr Hopkinson
Mr Fitchew
Mr Heaver

TREASURY MINUTE ON PAC REPORTS OF THE LAST PARLIAMENT

The Financial Secretary has seen your note of 23 June.

His initial reaction is that we may have to give a non-committal reply to the Dog Licencing Report before the PAC is reappointed. But he wishes to discuss the options with you.

This Office will be in touch to arrange an early meeting.

MED
M E DONNELLY

FROM: M E DONNELLY
DATE: 27 June 1983

PS/ECONOMIC SECRETARY

BUSINESS EXPANSION SCHEME PUBLICITY

The Financial Secretary has made a number of minor amendments to the attached draft leaflet on the Business Expansion Scheme, which I have incorporated into the revised version attached.

The Financial Secretary has commented that there remains a certain amount of repetition in the material. He would be interested in any comments that the Economic Secretary might have before sending it back to the Revenue.

MED
M E DONNELLY

BES LEAFLET: SECOND DRAFT

1. Summary

If you are the proprietor of a business, and are looking for outside investors to provide new capital, or if you are an investor looking for an unquoted company in which to invest, you may be able to take advantage of an important new tax incentive. This incentive is called the Business Expansion Scheme. Like its predecessor, the Business Start-up Scheme, it can substantially reduce the cost to an investor of his investment, and increase both his profit and the ability of the unquoted company to attract capital.

Who is it for?

It is open to most people who pay UK income tax, including those who have already benefited from the Business Start-up Scheme.

What is it worth?

The scheme gives the investor relief:

at his or her highest income tax rates (including investment income surcharge);

on the amount invested up to a maximum of £40,000 a year;

for each of four tax years - April 1983 to April 1987.

What do I have to do?

Invest in new ordinary shares issued by certain companies (normal minimum £500 in any one company).

What companies can I invest in?

Any company with which you are unconnected, which is starting up or continuing almost any trade, and which is not quoted on the Stock Exchange or dealt in on the Unlisted Securities Market.

When can I claim relief?

As soon as the company has completed four months trading, but not before 1 January 1984.

What conditions are there?

Full relief is kept if the shares are held, and certain conditions satisfied, for five years. Some conditions have to be kept for only three years.

2. Introduction

The main purpose of this leaflet is to give you a general idea of how the Business Expansion Scheme works, so that you can decide whether it can help you, either as an investor or as the proprietor of a company. The leaflet does not contain full details of the scheme, which can be found in the Finance Act 1983. If you decide you want to take advantage of it, you should make sure you understand the rules which would apply to you, by consulting your accountant, solicitor or professional adviser.

Investment in equity capital of unquoted companies brings with it risks but also the chance of considerable rewards. The Government does not, and no Government can, guarantee success for such investments. But the right kind of Government incentive can very substantially reduce the cost of the investment, and therefore increase the potential profit on it. Such a generous tax incentive is provided by the Business Expansion Scheme. It was introduced in 1983, and its purpose is to help outside

investors provide additional risk capital for unquoted companies to help with their trading activities.

3. The main features of the Scheme

The main features of the Scheme are as follows -

i. It is for equity investment in unquoted companies. This mean companies whose shares are not dealt in on the Stock Exchange or the Unlisted Securities Market.

ii. It covers most kinds of companies trading wholly or mainly in the UK - including manufacturing, service, construction, retail and wholesale distribution. But some companies are excluded, for example those involved in financial services and overseas companies.

iii. It is for outside investors, rather than for people putting money into their own business. Broadly, an investor may qualify if he (together with his close relatives or business partners see page) owns less than 30 per cent of the business and is not a paid director or an employee of the company. He may qualify if he is an unpaid director, or if he receives fees for professional and similar services to the company other than as a director or an employee.

iv. It is for new risk capital invested on a reasonably long term basis. The relief is therefore for investment in new ordinary shares which have no special rights, and which have to be held for at least five years.

v. The relief is for genuinely additional investment in unquoted companies. The relief may be withdrawn in whole or in part if the investor withdraws his money from the company, or sells his shares within a period of five years, or if some other condition of the Scheme is broken within a period of three years.

vi. The investor cannot have relief on more than £40,000 in total in any one year. He must invest at least £500 per company unless he invests through an approved investment fund (mentioned on page). Relief is given at the top rates of tax, and so can be as high as 75 per cent. The Scheme applies to shares issued from 6 April 1983 until 5 April 1987.

4. How can I qualify for the relief?

You can qualify if you -

live in the UK, (technically are resident and ordinarily resident here); and

subscribe for newly issued shares in a qualifying UK company with which you are not closely connected.

You are normally regarded as being closely connected with the company and therefore not qualifying for relief, if you or your associates -

own more than 30 per cent of the ordinary shares in it (or of the total share and loan capital combined, but excluding here bank overdrafts); or

are both a director of the company and receive directors fees during the first five years (you may be an unpaid director); or

are an employee or partner of the company.

For these purposes you count in with you own shares and interests those of your husband or wife, your grandparents, your parents, your children, your grandchildren, your business partners, and certain other "associates".

You can, however, claim relief if you invest in a company which is controlled by your sister or brother, or by your nephew or niece, or by more distant relatives. And, if you are a director of the company, you are not disqualified for the relief if all you receive is travelling and other expenses admitted for tax purposes. Nor are you disqualified if in a separate capacity you provide the company with, for example, accounting or legal services so long as you do not charge more than the market rate.

You do not qualify for relief if you come to a mutual agreement with someone else to invest in their company while they invest in yours.

5. What sort of company can I invest in?

The company must not be quoted - that is its shares must not be dealt in on the Stock Exchange or the Unlisted Securities Market.

The company must carry on a trade wholly or mainly in the UK. This does not prevent it from exporting some or even all of its output, provided that the bulk of its activities are in fact carried on in the UK.

Most types of trade are within the Scheme, but there are some exclusions. A company is excluded if it carries on a trade substantially similar to that of another company under the control of the same individual.

A company may have subsidiaries, as long as -

the subsidiaries are 100 per cent owned by the parent company; and

the subsidiaries are themselves qualifying companies.

6. Are there any restrictions on the kind of trade?

Yes, but they are few. The Scheme covers virtually the whole range of manufacturing, construction and service industries, including ordinary retail and wholesale trades.

The main exclusions are businesses which are concerned with such activities as banking and dealing in shares and land; leasing or hiring; dealing amounting to financial investment, for example in gold or whisky; and the provision of legal or accountancy services.

7. Do all types of share capital qualify for relief?

No. Relief is given for investment in new ordinary shares, which are at full risk. The shares may have different voting rights, but otherwise they must not have any advantage over other ordinary shares either in respect of dividends, right to a company's assets on its winding up, or present or future rights to be redeemed.

A company can qualify for relief whatever kind of share capital it has, provided only that all the shares are fully paid up. But the tax relief is only given for investment in the sorts of shares described above.

Investment in a company qualifies for relief even if the company has wholly owned subsidiaries, and the money may be raised for the purpose of the trade of a subsidiary, as well as that of a parent company.

8. How much relief can I claim?

You and your spouse can, between you, claim relief on up to £40,000 paid for shares issued in a year, for each year of the Scheme.

The relief is given at your highest rate of income tax, including the investment income surcharge. If you subscribe for the full £40,000 of shares for example, and pay at the top rate (75 per cent) on at least £40,000 of your income, the tax relief is worth £30,000. Thus an investment of £160,000 over the four years of the Scheme would (given the present rates of tax) attract a maximum tax relief of £120,000. This will be quite separate from the normal tax reliefs, for instance, capital allowances, available to the company when it in turn invests the money.

You can invest up to the whole amount in one company, or spread it between several companies. But there is a lower limit of £500 of investment in any one company in any one year, except for investments through an approved investment fund (see page).

Although the amount of investment qualifying for relief is restricted to £40,000 in any one year, you can of course invest more than this in a company if you wish, provided you (and your associates) do not end up with more than a 30 per cent interest in the company.

More than one taxpayer can invest in the same company and claim relief. There is no limit on the total amount of relief that may be given for investment in one company, or on the amount of a company's ordinary share capital which can qualify for relief. But relief is only available for new ordinary shares at full risk.

9. How long must I keep my investment in the company?

For at least five years, if you want to retain the full tax relief. There is nothing to stop you selling your shares within this period, but if you do so, you may lose some or all of the relief. After five years, you are free to dispose of the shares, or hold on to them if you wish, without losing the relief. If you die within the five year period, relief is not withdrawn on that account.

10. Can the relief be lost for any other reason?

The relief will no longer be due of course if the conditions are broken. This will happen, for example, if you receive some of your investment back from the company in a variety of ways. But these conditions apply only for the first five years after the shares are issued. Relief is also withdrawn if the company itself ceases to qualify within three years, for example because its trade no longer qualifies.

If the relief does have to be recovered from you, it will be done by reopening your tax liability for the year in which the relief was originally given. So you cannot lose more tax relief than you originally had. But you may be liable to pay interest to the Inland Revenue.

11. How do I claim relief?

Ask the company to seek authorisation from its Inspector of Taxes to issue you with a certificate showing that the conditions applying to the company and its trade are met. Send it with your claim to the Tax District to which you make your tax returns. Quote your tax reference number. You cannot claim relief until the company has been trading for four months, or until 1 January 1984, whichever is the later.

Slightly different arrangements apply where an investment has been made via an approved investment fund (see page).

12. Will I have to pay capital gains tax when I dispose of the shares

This will depend on the circumstances. Broadly, the normal capital gains tax rules apply. But where the disposal proceeds are less than the amount subscribed for the shares, there will be no gain or loss for capital gains tax purposes.

Even where the disposal of the shares does give rise to a gain, you may not have to pay any capital gains tax. If you have made losses on the disposal of other assets, these may be available to set against the gain. And, in any event, the first £5,300 of your total net gains in a year are exempt. The indexation allowance will also apply.

13. How do I find a company in which to invest?

This is largely up to you. Your accountant, solicitor, stock-broker or other financial adviser may be able to help. Or you may know of someone seeking outside equity capital through your own business contacts, or through the Press.

You may also be able to find an investment fund prepared to invest your money as nominee for you, by bringing together the funds of a substantial number of investors and spreading them over a number of unquoted companies. This might be of particular value to investors who want to spread their risk between a number of companies. Where such a fund has been approved for tax purposes by the Inland Revenue, the normal minimum of a £500 investment per company does not apply.

14. How do I find people to invest in my business?

You could go to the same sources of professional advice mentioned above, or look into the possibilities provided by approved investments funds and other venture capital institutions.

15. Further information

This leaflet is based on the law in force at the date of publication. It is for general guidance only. Full details of the Business Expansion Scheme are contained in the Finance Act 1983. If you want more information about the tax relief than is contained in this leaflet, your local Inspector of Taxes should be able to help. But you should consult a professional adviser on how you can make the best use of the Scheme.

FROM: M E DONNELLY
DATE: 27 June 1983

PS/IR

cc PS/Economic Secretary
Mr Monger
Mr Robson
Mr Salveson
Mr Milner

TAX POLICY: DIVISION OF RESPONSIBILITY

The attached note sets out the division of responsibility between the Financial Secretary and the Economic Secretary in detailed areas of tax policy.

In the event of uncertainty as to which Minister should take the lead, Private Offices will be happy to advise.

MED

M E DONNELLY

TAX POLICY: DIVISION OF RESPONSIBILITY

1. FINANCIAL SECRETARY

   (a) Schedule D/Schedule E borderline

   (b) Schedule D self-assessment

   (c) Corporation Tax self-assessment.

2. ECONOMIC SECRETARY

   (a) Payroll Taxes

   (b) Corporate Bonds

3. UNTIL SUMMER RECESS: FINANCIAL SECRETARY

   SUBSEQUENTLY: ECONOMIC SECRETARY

   (a) Business Expansion Scheme, and other "enterprise" measures

   (b) Capital allowances

   (c) Purchase of Own Shares, Employee Share Schemes etc.

RESTRICTED

FROM: M E DONNELLY
DATE: 27 June 1983

MR JUDD

cc PS/Chancellor
PS/Chief Secretary
PS/Economic Secretary
PS/Minister of State
Mr Middleton
Mr Bailey
Mr Wilding
Mr Pestell
Mr Hopkinson
Mr Perry
Mr Ridley

RESPONSE TO PAC REPORT ON DOG LICENCING

The Financial Secretary discussed this question today with yourself and Mr Hopkinson.

It was agreed that there was little prospect of a new PAC being appointed before the Autumn. Consequently the Government still had some time to work out its response to the PAC's Dog Licencing Report. However, a response on this Report was needed so that replies could be given to the other PAC reports produced before the Dissolution. Moreover the need to reply to the PAC could be used as a lever to encourage agreement on proposals to end the anomalies in the present dog licencing system.

On the substance of the issue the Financial Secretary stressed that a solution involving Dog Wardens was undesirable in that it would involve an increase in bureaucracy and consequently a further burden on the taxpayer. The most straightforward solution, which produced a net public expenditure saving, would be simple abolition of dog licences. The policy lead in this area lay with the Department of the Environment.

The Financial Secretary said that the best way forward both on PAC procedure and on substance would be for us to encourage Mr Jenkin to send an early reply to his 16 June letter, setting out how he proposed to take the issue forward. At the same time a non-committal form of words could be used as a preliminary response to the PAC's report explaining that a more substantive reply would be given in the autumn. This would encourage colleagues to discuss the policy problems in H Committee, and allow all the other replies to PAC reports that were now ready to be published. When dog licencing came before H Committee it would, in view of the expenditure questions involved, become primarily the responsibility of the Chief Secretary.

MED
M E DONNELLY

FROM: M E DONNELLY
DATE: 27 June 1983

MR PEET

cc Mr Unwin
Mrs Hedley-Miller

FINANCIAL SECRETARY'S VISIT TO STRASBOURG

I have spoken with Mr Marsden in UKREP.

It seems that we now have the (belated) agreement of all concerned that the Financial Secretary should take over Sir Michael Butler's programme for Tuesday 5 July in Strasbourg.

However there are two particular problems.

The EDG have asked to discuss the Stuttgart Summit, Northern Ireland (Haagerup) and recruitment of British officials to EC institutions. The British Socialists wish to discuss steel; the Social Fund; and Hunger in the World.

As you know the Financial Secretary is not an expert in any of these areas, apart perhaps from the Stuttgart Summit. If he is to take on speaking on these subjects he will need thorough briefing. But it is for consideration whether in the event it might be better for Mr Marsden or some other official to deal with these subjects, leaving the Financial Secretary free for purely budgetary discussions.

Perhaps we might discuss this tomorrow.

MED

M E DONNELLY

Treasury Chambers, Parliament Street, SW1P 3AG

D W Saunders Esq
Office of Parliamentary Counsel
36 Whitehall
LONDON
SW1A 2AY

28 June 1983

Dear Saunders

TELECOMMUNICATIONS BILL

... I enclose a ways and means and money resolutions for this Bill duly initialled by the Financial Secretary.

Yours sincerely

E KWIECINSKI
Private Secretary

WAYS AND MEANS

Mr Nicholas Ridley

Telecommunications

That any Act of the present Session to provide for the appointment and functions of a Director General of Telecommunications, to abolish British Telecommunications' exclusive privilege with respect to telecommunications and to make new provision with respect to the provision of telecommunication services ("the Act" may -

(1) authorise the inclusion in licences for the running of telecommunication systems of conditions requiring the rendering of payments to the Secretary of State;

(2) require persons to whom licences for the provision of cable programme services are granted to pay to the Secretary of State such sums as may be prescribed by or determined under regulations;

and that, for the purposes of the Act, it is expedient to authorise the payment into the Consolidated Fund or the National Loans Fund of any sums falling to be paid into that Fund by virtue of the Act.

NR

24.6.83.

TELECOMMUNICATIONS [MONEY]: Queen's Recommendation signified

Mr Nicholas Ridley

That, for the purposes of any Act of the present Session to provide for the appointment and functions of a Director General of Telecommunications, to abolish British Telecommunications' exclusive privilege with respect to telecommunications and to make new provision with respect to the provision of telecommunication services ("the Act"), it is expedient to authorise -

(1) the extinguishment by order of all or any liabilities of the successor company to the Secretary of State in respect of the principal of transferred loans;

(2) the payment out of money provided by Parliament of -

(a) the remuneration of, and any travelling or other allowances payable under the Act to, the Director General of Telecommunications and any staff of the Director, any sums payable under the Act to or in respect of the Director and any expenses duly incurred by the Director or by any of his staff in consequence of the provisions of the Act;

(b) any sums required by the Secretary of State for making grants or other payments under the Act or for discharging any liability imposed on him by the Act;

(c) any expenses incurred by the Secretary of State in acquiring securities of the successor company or of any subsidiary of the successor company or rights to subscribe for any such securities;

(d) any administrative expenses incurred by the Secretary of State in consequence of the provisions of the Act;

(c) any increase attributable to the Act in the sums payable out of money so provided under any other Act;

(3) the payment out of the National Loans Fund of any sums required by the Secretary of State for making loans under the Act;

and for the purposes of this Resolution "successor company" has the meaning given by the Act and "transferred loan" means any money borrowed or treated as borrowed by British Telecommunications the liability to repay which vests in the successor company by virtue of the Act.

24 6 83

PSO 24467

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

Mr Hoss. with papers

The Rt Hon Viscount Whitelaw CH, MC
Lord President of the Council
Privy Council Office
68 Whitehall
LONDON SW1

FINANCIAL SECRETARY	
REC.	30 JUN1983
ACTION	MR·SALVESON
COPIES TO	MR·BURGNER

29 June 1983

cc PS/Mrs Chalker
PS/Mr Mitchell
PS/Lord Lucas
PS/Mr Lazarus
Mr Hannigan
Mr Holmes
Mr Palmer
Mr Knighton
Mr Alcock
Mr Bridgman
Mr A.P. Brown
Mr W.P. Jackson
Mr Yass
Mr Stevens Mr Dawe
Mr Beathem Mr Gold

LEGISLATIVE PROGRAMME 1983-84

Thank you for your letter of 27 June.

I was disappointed to see that QL have not felt able to recommend either the British Airways or National Bus Company privatisation measures. It is most important that we press ahead with both these. The powers to privatise BA were taken in 1980 and, now that BA's commercial fortunes are restored, delay in giving them effect could call our intention into question. The capital reconstruction clauses are needed to allow this. As for the NBC, there is now enthusiasm for privatisation at the top of the company; it would be most unfortunate if this faded because of delay on our part.

I fully appreciate, however, what you say about pressures on Parliamentary time and the need to avoid risks of overspill into the following session. I would therefore propose combining my Civil Aviation proposal needed for BA privatisation with the NBC measures into one Transport and Civil Aviation Bill. This would be a short to medium length Bill, ready for introduction after the summer recess. I hope you will be able

CONFIDENTIAL

to include this revised bid in your memorandum to Cabinet, and I attach a summary of it.

You also send me a copy of your letter to Norman Tebbit, referring to timing of the Dock Work Regulation Bill, and I am responding to this separately.

TOM KING

BILL	DEPARTMENT	PURPOSE	LENGTH	TIMING ETC
Transport and Civil Aviation	Transport	a) To enable the capital reconstruction of British Airways to take place prior to privatisation. The legislation would enable the Government: (i) to pay sums to British Airways so that they can pay off outstanding debts; and (ii) to write off outstanding loans to British Airways from the National Loans Fund. b) To permit transfer of the National Bus Company to the private sector.	Medium	Manifesto commitments to privatise British Airways and introduce substantial private finance into NBC. Policy clearance for BA measures early July, for NBC policy approval to be sought soon after which consultation will be necessary with NBC. The Bill should be ready for introduction immediately after the Summer Adjournment. Royal Assent by March 1984 would be highly desirable enabling a capital reconstruction of BA to take place by the end of the financial year. Bill likely to be opposed by the Opposition. Some Conservative Members may be concerned about the effects of NBC privatisation on rural transport and may resist the BA measures, stimulated by the private airlines. Effect on PSBR of BA measures broadly neutral, and no manpower implications. Privatisation of NBC will produce £100-£150m in year of sale, offset by reduction in scheduled loan repayments in subsequent years. Local authority revenue support may increase by about £15m a year. 50,000 NBC employees will transfer to private sector.

FROM: M E DONNELLY
DATE: 29 June 1983

MR ASHCROFT - IR

cc Mr Robson
Mr Prescott - IR
PS/IR

BUSINESS EXPANSION SCHEME: PUBLICITY

The Financial Secretary has seen your submission of 24 June, and the draft leaflet on the Business Expansion Scheme.

The Financial Secretary agrees that it would be helpful to produce the leaflet on the BES. He has suggested some amendments to the layout and content of your draft. A revised draft is attached.

MED

M E DONNELLY

BES LEAFLET: SECOND DRAFT

1. Summary

If you are the proprietor of a business, and are looking for outside investors to provide new capital, or if you are an investor looking for an unquoted company in which to invest, you may be able to take advantage of an important new tax incentive. This incentive is called the Business Expansion Scheme. Like its predecessor, the Business Start-up Scheme, it can substantially reduce the cost to an investor of his investment, and increase both his profit and the ability of the unquoted company to attract capital.

Who is it for?

It is open to most people who pay UK income tax, including those who have already benefited from the Business Start-up Scheme.

What is it worth?

The scheme gives the investor relief:

at his or her highest income tax rates (including investment income surcharge);

on the amount invested up to a maximum of £40,000 a year;

for each of four tax years - April 1983 to April 1987.

What do I have to do?

Invest in new ordinary shares issued by certain companies (normal minimum £500 in any one company).

What companies can I invest in?

Any company with which you are unconnected, which is starting up or continuing almost any trade, and which is not quoted on the Stock Exchange or dealt in on the Unlisted Securities Market.

When can I claim relief?

As soon as the company has completed four months trading, but not before 1 January 1984.

What conditions are there?

Full relief is kept if the shares are held, and certain conditions satisfied, for five years. Some conditions have to be kept for only three years.

2. Introduction

The main purpose of this leaflet is to give you a general idea of how the Business Expansion Scheme works, so that you can decide whether it can help you, either as an investor or as the proprietor of a company. The leaflet does not contain full details of the scheme, which can be found in the Finance Act 1983. If you decide you want to take advantage of it, you should make sure you understand the rules which would apply to you, by consulting your accountant, solicitor or professional adviser.

Investment in equity capital of unquoted companies brings with it risks but also the chance of considerable rewards. The Government does not, and no Government can, guarantee success for such investments. But the right kind of Government incentive can very substantially reduce the cost of the investment, and therefore increase the potential profit on it. Such a generous tax incentive is provided by the Business Expansion Scheme. It was introduced in 1983, and its purpose is to help outside

investors provide additional risk capital for unquoted companies to help with their trading activities.

3. The main features of the Scheme

The main features of the Scheme are as follows -

i. It is for equity investment in unquoted companies. This mean companies whose shares are not dealt in on the Stock Exchange or the Unlisted Securities Market.

ii. It covers most kinds of companies trading wholly or mainly in the UK - including manufacturing, service, construction, retail and wholesale distribution. But some companies are excluded, for example those involved in financial services and overseas companies.

iii. It is for outside investors, rather than for people putting money into their own business. Broadly, an investor may qualify if he (together with his close relatives or business partners see page) owns less than 30 per cent of the business and is not a paid director or an employee of the company. He may qualify if he is an unpaid director, or if he receives fees for professional and similar services to the company other than as a director or an employee.

iv. It is for new risk capital invested on a reasonably long term basis. The relief is therefore for investment in new ordinary shares which have no special rights, and which have to be held for at least five years.

v. The relief is for genuinely additional investment in unquoted companies. The relief may be withdrawn in whole or in part if the investor withdraws his money from the company, or sells his shares within a period of five years, or if some other condition of the Scheme is broken within a period of three years.

vi. The investor cannot have relief on more than £40,000 in total in any one year. He must invest at least £500 per company unless he invests through an approved investment fund (mentioned on page ---). Relief is given at the top rates of tax, and so can be as high as 75 per cent. The Scheme applies to shares issued from 6 April 1983 until 5 April 1987.

4. How can I qualify for the relief?

You can qualify if you -

live in the UK, (technically are resident and ordinarily resident here); and

subscribe for newly issued shares in a qualifying UK company with which you are not closely connected.

You are normally regarded as being closely connected with the company and therefore not qualifying for relief, if you or your associates -

own more than 30 per cent of the ordinary shares in it (or of the total share and loan capital combined, but excluding here bank overdrafts); or

are both a director of the company and receive directors fees during the first five years (you may be an unpaid director); or

are an employee or partner of the company.

For these purposes you count in with you own shares and interests those of your husband or wife, your grandparents, your parents, your children, your grandchildren, your business partners, and certain other "associates".

You can, however, claim relief if you invest in a company which is controlled by your sister or brother, or by your nephew or niece, or by more distant relatives. And, if you are a director of the company, you are not disqualified for the relief if all you receive is travelling and other expenses admitted for tax purposes. Nor are you disqualified if in a separate capacity you provide the company with, for example, accounting or legal services so long as you do not charge more than the market rate.

You do not qualify for relief if you come to a mutual agreement with someone else to invest in their company while they invest in yours.

5. What sort of company can I invest in?

The company must not be quoted - that is its shares must not be dealt in on the Stock Exchange or the Unlisted Securities Market.

The company must carry on a trade wholly or mainly in the UK. This does not prevent it from exporting some or even all of its output, provided that the bulk of its activities are in fact carried on in the UK.

Most types of trade are within the Scheme, but there are some exclusions. A company is excluded if it carries on a trade substantially similar to that of another company under the control of the same individual.

A company may have subsidiaries, as long as -

the subsidiaries are 100 per cent owned by the parent company; and

the subsidiaries are themselves qualifying companies.

6. Are there any restrictions on the kind of trade?

Yes, but they are few. The Scheme covers virtually the whole range of manufacturing, construction and service industries, including ordinary retail and wholesale trades.

The main exclusions are businesses which are concerned with such activities as banking and dealing in shares and land; leasing or hiring; dealing amounting to financial investment, for example in gold or whisky; and the provision of legal or accountancy services.

7. Do all types of share capital qualify for relief?

No. Relief is given for investment in new ordinary shares, which are at full risk. The shares may have different voting rights, but otherwise they must not have any advantage over other ordinary shares either in respect of dividends, right to a company's assets on its winding up, or present or future rights to be redeemed.

A company can qualify for relief whatever kind of share capital it has, provided only that all the shares are fully paid up. But the tax relief is only given for investment in the sorts of shares described above.

Investment in a company qualifies for relief even if the company has wholly owned subsidiaries, and the money may be raised for the purpose of the trade of a subsidiary, as well as that of a parent company.

8. How much relief can I claim?

You and your spouse can, between you, claim relief on up to £40,000 paid for shares issued in a year, for each year of the Scheme.

The relief is given at your highest rate of income tax, including the investment income surcharge. If you subscribe for the full £40,000 of shares for example, and pay at the top rate (75 per cent) on at least £40,000 of your income, the tax relief is worth £30,000. Thus an investment of £160,000 over the four years of the Scheme would (given the present rates of tax) attract a maximum tax relief of £120,000. This will be quite separate from the normal tax reliefs, for instance, capital allowances, available to the company when it in turn invests the money.

You can invest up to the whole amount in one company, or spread it between several companies. But there is a lower limit of £500 of investment in any one company in any one year, except for investments through an approved investment fund (see page).

Although the amount of investment qualifying for relief is restricted to £40,000 in any one year, you can of course invest more than this in a company if you wish, provided you (and your associates) do not end up with more than a 30 per cent interest in the company.

More than one taxpayer can invest in the same company and claim relief. There is no limit on the total amount of relief that may be given for investment in one company, or on the amount of a company's ordinary share capital which can qualify for relief. But relief is only available for new ordinary shares at full risk.

9. How long must I keep my investment in the company?

For at least five years, if you want to retain the full tax relief. There is nothing to stop you selling your shares within this period, but if you do so, you may lose some or all of the relief. After five years, you are free to dispose of the shares, or hold on to them if you wish, without losing the relief. If you die within the five year period, relief is not withdrawn on that account.

10. Can the relief be lost for any other reason?

The relief will no longer be due of course if the conditions are broken. This will happen, for example, if you receive some of your investment back from the company. But these conditions apply only for the first five years after the shares are issued. Relief is also withdrawn if the company itself ceases to qualify within three years, for example because its trade no longer qualifies.

If the relief does have to be recovered from you, it will be done by reopening your tax liability for the year in which the relief was originally given. So you cannot lose more tax relief than you originally had. But you may be liable to pay interest to the Inland Revenue.

11. How do I claim relief?

Ask the company to seek authorisation from its Inspector of Taxes to issue you with a certificate showing that the conditions applying to the company and its trade are met. Send it with your claim to the Tax District to which you make your tax returns. Quote your tax reference number. You cannot claim relief until the company has been trading for four months, or until 1 January 1984, whichever is the later.

Slightly different arrangements apply where an investment has been made via an approved investment fund (see page).

12. Will I have to pay capital gains tax when I dispose of the shares

This will depend on the circumstances. Broadly, the normal capital gains tax rules apply. But where the disposal proceeds are less than the amount subscribed for the shares, there will be no loss for capital gains tax purposes.

Even where the disposal of the shares does give rise to a gain, you may not have to pay any capital gains tax. If you have made losses on the disposal of other assets, these may be available to set against the gain. And, in any event, the first £5,300 of your total net gains in a year are exempt. The indexation allowance will also apply.

13. How do I find a company in which to invest?

This is largely up to you. Your accountant, solicitor, stock-broker or other financial adviser may be able to help. Or you may know of someone seeking outside equity capital through your own business contacts, or through the Press.

You may also be able to find an investment fund prepared to invest your money as nominee for you, by bringing together the funds of a substantial number of investors and spreading them over a number of unquoted companies. This might be of particular value to investors who want to spread their risk between a number of companies. Where such a fund has been approved for tax purposes by the Inland Revenue, the normal minimum of a £500 investment per company does not apply.

14. How do I find people to invest in my business?

You could go to the same sources of professional advice mentioned above, or look into the possibilities provided by approved investments funds and other venture capital institutions.

15. Further information

This leaflet is based on the law in force at the date of publication. It is for general guidance only. Full details of the Business Expansion Scheme are contained in the Finance Act 1983. If you want more information about the tax relief than is contained in this leaflet, your local Inspector of Taxes should be able to help. But you should consult a professional adviser on how you can make the best use of the Scheme.

CONFIDENTIAL

FROM: M E DONNELLY
DATE: 29 June 1983

PS/CHANCELLOR

cc Chief Secretary
Economic Secretary
Mr Middleton
Mr Bailey
Mr Anson
Mr Byatt
Mr Battishill
Mr Burgner
Mr Christie
Mr Monck
Mr Mountfield
Mr Culpin
Mr Houston
Mr Lovell
Mr Halligan
Mr Morgan
Mr Richard
Mr Turnbull
Mr R H Wilson
Mr Grimstone

PRIVATISATION OF ROLLS ROYCE

The Financial Secretary has seen the Chancellor's comments on privatisation of Rolls Royce (Miss O'Mara's 23 June note) and Mr Halligan's submission of 28 June.

The Financial Secretary also feels that we should not be too gloomy about the prospects for a sale of some or all of Rolls Royce. It should be possible for potential buyers to make the same assessment as the Government of the company's future prospects, even though lack of a proven record of profits would of course affect the selling price. Sir William Duncan's September presentation should provide more information.

MED
M E DONNELLY

FROM: E KWIECINSKI
DATE: 30 June 1983

PS/ECONOMIC SECRETARY

cc PS/Chancellor
Chief Secretary
Mr Robson
Ms Rhodes)
Mr Lusk) IR
PS/IR

TAX TREATMENT OF NEWARK COUNCIL'S SMALL BUSINESS COMPETITION PRIZES

The Financial Secretary has seen Ms Rhodes' submission of 29 June. He is quite happy to complete the work on this case before handing this subject over to the EST, but he would welcome his views on it.

His own view is that the £5000 is a subscription of capital, just like new equity. As such he does not think it is taxable at all. He wonders whether the Revenue would accept this argument. Also he thinks that given the small amounts of money involved it would seem beyond all sense of reason to inist on taxing it, and is very bad for the Revenue's public image.

EK.
E KWIECINSKI

RESTRICTED

FROM: M E DONNELLY
DATE: 30 June 1983

MRS HEDLEY-MILLER

cc Mr Unwin
Miss Court
Mr Edwards
Mr Peet

FINANCIAL SECRETARY'S VISIT ATHENS: BRIEFING

We spoke.

I have arranged with Mr Rifkind's office that we will hold a joint briefing meeting at 5.30pm on Thursday 7 July, in Mr Rifkind's room in the FCO. We agreed to exchange briefing beforehand if possible. I understand that the FCO have the idea that the Financial Secretary's meeting with Mr Varfis should restrict itself to the short term refunds problem leaving Mr Rifkind to deal with the longer term, Stuttgart mandate etc. I suggested that this was a matter for discussion.

I will be in touch next week to arrange an internal Treasury briefing meeting for the Financial Secretary.

MED

M E DONNELLY

CONFIDENTIAL

FROM: E KWIECINSKI
DATE: 30 June 1983

MR R R MARTIN - IR

cc Dr Rouse
PS/IR
Mr Frost/IR

CASUAL WORKERS IN AGRICULTURE

The Financial Secretary discussed this subject with you today.

He is keen for your discussions with the National Farmers Union to reach a speedy conclusion, though he recognises that the initiative rests with them for the moment. He thinks that any agreement with NFU should be on a national basis, removing the ability of individual farmers to come to local arrangements with their Inspector of Taxes - as was allowed under the 1978 agreement. Otherwise he is broadly content for the 1978 agreement to form the basis of any future accord.

In the longer term he would be in favour of any new agreement being codified in the form of a new extra statutory concession. This would safeguard the Revenue from accusations that they were giving concessions without Parliament's authority.

As far as the recent correspondence is concerned the Financial Secretary wishes to send brief holding replies to all letters. These would be followed by careful and detailed letters explaining the position of casuals under the law and detailing any agreement reached with the NFU.

E KWIECINSKI

FROM: E KWIECINSKI
DATE: 30 June 1983

MR DRAPER/IR

cc PS/Chancellor
Mr Robson
Mrs Dunn
Mr O'Leary/IR.
PS/IR

STAMP DUTY: INSTITUTE FOR FISCAL STUDIES SEMINAL

I attach the provisional programme for the seminar on stamp duty that the Financial Secretary is attending on 27 July 1983.

The Financial Secretary would be grateful if you would supply him with a short speaking note for use at the seminar.

It would be most helpful if we could have this by Friday 15 July.

E KWIECINSKI

ifs

THE INSTITUTE FOR FISCAL STUDIES
1/2 CASTLE LANE, LONDON SW1E 6DR Tel. 01-828 7545

President:
THE LORD CROHAM, G.C.B.

Director:
JOHN KAY

Chairman:
DICK TAVERNE, Q.C.

June 29 1983

Mr Nicholas Ridley
Financial Secretary to the Treasury
H M Treasury
Parliament Street
London SW1

Dear Mr Ridley,

I enclose the provisional programme for the seminar on stamp duty which you have kindly agreed to address. We would suggest that you open the proceedings with an introduction to the Inland Revenue's Consultative Document. If you would prefer some other arrangement please let us know.

Yours sincerely,

J A Kay

PROVISIONAL PROGRAMME

THE FUTURE OF STAMP DUTIES

Wednesday 27th July 12.30 - 2.30 Royal Westminster Hotel
Buckingham Palace Road
London SW1

12.15	Registration	
12.30	Buffet lunch	
1.15	The Inland Revenue Consultative Document	
	- Mr Nicholas Ridley	(Financial Secretary to the Treasury)
1.30	Reactions to the document	
	- Mr Jack Harper	(of Malkin Cullis & Sumption)
	- Mr Reginald Nock	(Barrister)
	- Mr Stuart Valentine	(The Stock Exchange)
	- Mr John Hills	(Institute for Fiscal Studies)
2.20	Discussion	
2.30	Close	

CONFIDENTIAL

FROM: E KWIECINSKI
DATE: 30 June 1983

CHIEF SECRETARY

INCOME TAX AND CGT: LIABILITY OF TRUSTEES

The Financial Secretary had a word with you about this issue last night and said he would show you the papers (these are attached).

The Financial Secretary feels strongly that we should be wary of enacting retrospective legislation to compensate for what he sees as the incompetence of certain professional trustees.

He thinks that the best solution would be for the Revenue to try, if possible, to reach an out of court settlement with the trustees in the cases in question. These are rare cases, where a solution by discretion would, he feels, be better than legislation which could encourage trustees to be less prudent and could open scope for abuse.

He would be grateful for your comments.

M E Daulby
pp E KWIECINSKI

23 JUN 1983

FROM : S A ROBSON
DATE : 23 JUNE 1983

FINANCIAL SECRETARY

c.c. Mr O'Leary)
Mr Draper') IR

INCOME TAX AND CAPITAL GAINS TAX : LIABILITY OF TRUSTEES

Mr Draper's submission of 22 June.

2. You may wish to discuss this tricky issue. Yes, I think we should have a discussion of this. SR

3. Let us look at the two cases :

Case A — the essence of this case is that the trustees had a tax liability. Instead of setting money aside to meet that liability, they invested the money in shares and the shares crashed. In other words they took a risk and it did not pay off.

Case B — here the trustees realised a profit in October 1973. One of them resigned nine months later. The other resigned over a year later. The essence of their problem is that they left without either settling the tax liability or arranging some protection for their position.

In short the trustees can be seen as, at best, imprudent and, at worst, incompetent.

4. I would have more sympathy if the individuals concerned were ordinary people. They are not. They are professional trustees. They should not have been ignorant of their position in law.

5. For these reasons I see the merits of these two cases as small. As for the possible remedy of legislation to give limited liability to trustees :

(a) it is hard to see why trustees should be accorded more favourable treatment than other investors.

(b) it could open scope for abuse.

SAR

S A ROBSON

From: D G Draper
22 June 1983
INLAND REVENUE
POLICY DIVISION
SOMERSET HOUSE

1. MR O'LEARY PGL 22.6.83
2. FINANCIAL SECRETARY

INCOME TAX AND CAPITAL GAINS TAX: LIABILITY OF TRUSTEES

Introduction

1. We are sorry to have to bother you with a collection point so soon after the Election but a problem with trustees has arisen which if it is to be met will require legislation. It concerns cases in which trustees may be forced to settle trust tax bills out of their own pockets.

Background : Income tax/capital gains tax

2. There are no provisions in the Taxes Acts expressly charging trustees to income tax. Trustees are however liable under the general charging provisions as persons 'receiving or entitled to ..... income'. For capital gains tax there is a specific charging provision; a trust's chargeable gains can be assessed and charged in the name of one or more of the trustees acting at the time the assessment is made. In both instances the liability is personal in the sense that it can be enforced against the trustees and their property whether or not they have trust property out of which to reimburse themselves.

---

cc Chancellor
Chief Secretary
Economic Secretary
Minister of State
Mr Robson
Parliamentary Counsel

Mr Green
Mr Isaac
Mr O'Leary
Mr Houghton
Mr Hall
Mr Lawrance
Mr Draper
Mr M Elliott
Mr Fawcett
Ms Tyrrell
PS/IR

Instant cases

3. Two substantial cases have recently come to light where the trust funds are insufficient and as the law stands we had no alternative but to proceed against the trustees personally. In both instances professional trustees are involved who have no connection with the settlor or beneficiaries. The trustees concerned may be covered by insurance, but in one instance a trustee on whom liability may ultimately fall is known to have to bear the first £50,000. The facts relating to the two cases are summarised in the annex to this note.

CTT position

4. For capital transfer tax the position is different. Like income tax and capital gains tax a capital transfer tax liability which falls upon a trustee is a personal one. But as was the case for estate duty there is a provision in the CTT code which deals with insolvent trusts. Where the trustees have acted responsibly they are not normally required to pay any CTT liability on the trust fund out of their own pockets. The question is whether a similar rule should be introduced for income tax and capital gains tax.

Trustees of debts generally

5. It is not only in respect of tax debts that trustees are personally liable. The personal liability of a trustee extends to any obligation which falls on him in that capacity. The Courts have consistently upheld this rule. In a recent tax case Lord Roskill took the view that trustees should ensure that they are sufficiently protected whether by the beneficiaries or others for any liability which might fall on them. He said that if they fail to do so they have only themselves to blame. As however the CTT legislation shows

there are circumstances where it would not be right in a tax context to press this principle to an extreme. In Case A there is a case for limiting the liability to the funds in the settlement and in Case B to any money the trustees can recover from their successors following a successful outcome of any action against the Bank.

Board's care and management powers

6. We have considered whether the two cases could be disposed with under the Board's care and management powers. We do not think they can. First, the legal position we are advised is quite clear. Secondly, we have not hitherto granted extra-statutory concessions on the collection of assessed tax. Thirdly, the fact that there is a specific provision in the CTT code to deal with insolvent trusts makes it difficult to say that Parliament did not intend the liability of trustees to other taxes to be an unlimited liability. We do it is true remit other taxes in cases where the taxpayer is insolvent. This option however is not open to us here because the persons, ie the trustees, against whom proceedings would have to be taken are not themselves insolvent.

Legislation

7. Unless therefore we are to go ahead with collecting the tax in these and other similar cases it will be necessary to remove the liabilities by legislation. The details of any legislation would have to be worked out with Parliamentary Counsel, and it would be desirable to consult both the Law Society and the CCAB, but broadly we have in mind legislation which would have much the same effect as the CTT rule, ie the object would be to limit liability where the trustees had acted responsibly but not otherwise. We think this would involve limiting the tax liability of trustees to -

(i) trust assets;

(ii) property which has gone out of the trust after the income/capital gains arose;

(iii) property which the trustees should have got into the settlement eg an interest under a deceased person's estate; and

(iv) property which the trustees could recover for the payment of tax eg moneys due under the terms of an indemnity.

The legislation would apply to current recovery action and would cover the two cases mentioned even though the liabilities were incurred some years ago.

8. The case however for legislation is not clear cut. There are a number of arguments against limiting the trustees' liability in this way. It is well known that the liability of trustees under general law is very wide and some will probably agree with Lord Roskill that trustees have only themselves to blame if they accept obligations without ensuring that they are protected for liabilities which may ultimately fall on them personally. Although the CTT rule is a precedent for matching income tax and capital gains tax rules, it does need to be borne in mind that the CTT limitation derives from the estate duty charge on death where the case for a limitation of this kind is much stronger. In its essentials the CTT provision applies only to a trustee's involuntary liabilities (eg a liability arising on the death of a life tenant). The case for a limitation in respect of a liability incurred as a result of an action taken by the trustees themselves (eg on a distribution of part of the trust fund or on the sale of settled property) is more questionable. If the Government did legislate on the lines proposed there could be criticism that the trustees were being treated more favourably than other taxpayers whose investment turned sour

after a capital gains tax or income tax liability has been incurred. One further factor that needs to be borne in mind is that if trustees' liability is limited we may be driven to reconsider the assessing rules and other machinery provisions. It might not be possible to continue to live with different assessing rules for income tax and capital gains tax. One of the points which would need to be watched is the danger that trustees who are assessable could shuffle off liability by resigning.

Conclusion

9. The choice is either to recover tax in the two cases or to legislate on the lines proposed. Providing a statutory limitation on trustees' liability would remove one of the disadvantages of a trust and the legislation would be examined closely by tax avoidance specialists. There is a risk that any limitation would be misused. On the other hand recovery action against professional trustees particularly in Case A is likely to sour relations with the professions and could be regarded as inequitable. On balance we would recommend legislation.

D G Draper

ANNEX A

TWO EXAMPLES OF INSOLVENT TRUSTS

CASE A

The principal assets of certain family trusts were holdings in two quoted companies. In 1970 and 1972 both companies made rights issues. The trustees borrowed from their bankers £m1 secured by deposit of the shares then valued at approximately £m20. Before taking up the rights issues the trustees took independent advice. Some 9 months after the rights issue both companies failed during the secondary banking/property company crash. The effect of this was that the trustees were no longer in a position to meet their obligations to the settlements' banker or to the Inland Revenue in respect of liabilities to both income tax and capital gains tax. The trustees owe the Inland Revenue £120,000.

The bankers accepted in full satisfaction of their debt of £534,905 a proportion (£76,627) of the sale proceeds of the shares in one of the companies which failed. This left the trust with assets of £28,000 which has now grown to £35,000. The liabilities, if pursued, would fall in the main initially on a trust company of a leading firm of accountants; ultimately the liability may rest with two individual partners, one in the firm of accountants and the other in a leading firm of solicitors.

CASE B

Under the terms of an agreement made in 1972 by R, AJL (R's solicitor) and JWL (R's accountant) were appointed trustees. The beneficiaries were members of R's family. The trust was set up with the knowledge of the trustees with the object of reducing the rate of tax on certain transactions.

The principal source of funds which became available to the trustees derived from options to buy land. The subsequent

purchase of the land and re-sale in October 1973 realised a gross profit of £m1. This has been assessed on AJL and JWL, the trustees who received the income.

On 5.7.74 JWL resigned as trustee following a disagreement with the settlor. At the time there were sufficient funds in the trust to meet the tax liability. AJL resigned in 1975.

Subsequently R appointed H (a teacher and a friend of R) and Mrs D (R's secretary) as trustees. By the time the tax liability came to light there was nothing left in the trust fund. It appears that the trust fund had been dissipated by:

i. the issue of forged cheques drawn on the trust account;

ii. the unauthorised transfer of moneys out of the trust account;

iii. the use of trust assets to guarantee other accounts; and

iv. because the trustees had been obliged to sell assets at reduced prices.

H and Mrs D are understood to be sueing the trust bankers in relation to the forged cheques.

CONFIDENTIAL

FROM: M E DONNELLY
DATE: 30 June 1983

PS/CHANCELLOR

cc PS/Chief Secretary
PS/Economic Secretary
PS/Minister of State
Mr Middleton
Mr Bailey
Mr Anson
Mr Byatt
Mr Lovell
Mr Traynor
Mr Andren
Mr Burr o/r
Mr Ridley

THE LABOUR MARKET

The Financial Secretary has seen Mr Anson's 27 June submission covering Mr Burr's notes on union legislation and Wages Councils.

The Financial Secretary considers that it is perhaps worth accepting explicitly that the abolition of minimum wages would adversely affect the poverty and unemployment traps. A fall in wages would lead to more people entering the poverty trap; and by also compressing the differential between being in and out of work would worsen the unemployment trap. But he accepts that the longer term improvements in the functioning of the economy gained by abolition of the Wages Councils outweigh these disadvantages.

MED

M E DONNELLY

CONFIDENTIAL

FROM: NICHOLAS RIDLEY
DATE: 30 June 1983

CHANCELLOR

cc Chief Secretary
Economic Secretary
Minister of State
Mr Monger
Mr Robson
Mr Ridley
Dr Rouse
Mr Martin/IR
PS/IR
(without attachment)

EMPLOYERS/EMPLOYEES: NET OF TAX PAY

John Wakeham and I held a series of meetings with Revenue and Treasury officials during the last Parliament to discuss ways in which the PAYE system could be made more flexibile - in particular to suit the needs of smaller businesses.

One possibility we looked at was encouraging the wider use among employers of a "net of tax" system of paying wages. In my speech during the Budget resolutions debate on 16 March (Hansard Col 317) I said:

> "We have not yet found a way of providing for annual accounting for PAYE. The cost of doing so would be large, but I think it is worth drawing to the attention of business men that they may engage and reward their employees on a net of tax basis ..... We are considering whether there is more that the Government could do to help businesses interested in arrangements of this type. Tax inspectors are ready to explain this method of payment and to assist those who wish to switch to it."

I asked the Revenue to pursue this further and I append their submission which reports the results.

I do not think it our business to either encourage or discourage the use of the "net of tax pay" method. But I do think that it is worth printing special Taxable Pay tables for distribution to local Inspector of Taxes offices. This would - at the relatively cheap cost of £10,000 - be a symbolic gesture to those currently operating such a system, and would confirm the legitimacy of this method within the PAYE system. There is evidence that the "net of tax" method is of benefit to industrial relations within certain industries, especially where piece work is involved. If it encouraged only half a dozen or so employees to increase their productivity, or was instrumental in taking a handful of people off the dole queue, it would be money well spent. The new tables would help Inspectors of Taxe to deal with queries and requests from employers wishing to introduce this method. I do not envisage a flood of participants to this sort of scheme in the future, so I think that any worries about increased Revenue staff costs can be largely discounted.

The introduction of the new tables would be minor but positive evidence that this Government are continuing to seek ways of improving incentives in industry.

I would be grateful for your views and those of colleagues.

NICHOLAS RIDLEY

29 JUN 1983

From: R R MARTIN
INLAND REVENUE
POLICY DIVISION
SOMERSET HOUSE

29 June 1983

1. MR BLYTHE 29/6

2. FINANCIAL SECRETARY

EMPLOYERS/EMPLOYEES

1. Following my note of 21 March, and Mr Kwiecinski's response of 25 March, we have been pursuing further the subject of "net of tax" pay. This submission reports the results.

2. For the benefit of Ministers who may not have seen the previous papers, there are some employers who pay their employees on a "net of tax" basis. The employers who have introduced this scheme have done so by converting their employees' existing gross pay into their new net pay (at the same figure). The employer pays the tax on top. For the purpose of calculating the tax, the new net pay is grossed up, so that the arithmetical answer is the same as it would be if the employer paid the employee a gross sum (pay and tax together) and actually deducted the tax. Presentationally, the employee can look on his or her pay as a net sum without deduction of tax (although the itemised pay statement which is required by employment law will always in fact show the employee his pay and tax together).

---

cc Chancellor of the Exchequer
Chief Secretary
Economic Secretary
Minister of State
Mr Robson
Mr A Ridley

Sir Lawrence Airey
Mr Isaac
Mr Gracey
Mr Blythe
Mr Roberts
Mr Marshall
Mr Frost
Mr Fraser
Mr Martin

3. You asked us to see whether there were any ways in which we could help in the processes of tax calculation for employers of this type.

Visits

4. I have visited four employers who run this type of scheme: I and N Rabin Ltd, a firm of pharmaceutical wholesalers, employing about 40 people, in Hoxton; Henri-Lloyd Ltd, a firm who manufacture yachting and other waterproof clothing and equipment, employing about 110 people, in Manchester; Stylewear Ltd (run by Mr Len Ferns) who manufacture casual clothing and leisurewear (eg track suits) in Liverpool, employing some 200; and Bradford Workwear, another clothing firm, employing around 30 people in the centre of Bradford. In addition we have had a meeting here with Mr Tom Heywood, who was until recently Finance Director of Clifford Williams; they are a clothing manufacturer in Telford, employing nearly 2,000, of whom some 350 are on net of tax pay.

5. Looking at these various visits together, I think I have three main impressions.

6. First, the firms involved are not a uniform picture of commercial success - Bradford Workwear went into liquidation and restarted again in the late 1970's, and Stylewear's order books are not as high at present as they would like to see them. However, the employers I visited were all in favour of net of tax pay. It is almost all operated on the basis of piece-work pay arrangements, and for single or married women machine operators: the only firm in the service (as opposed to manufacturing) sector - I and N Rabin - has now dropped net of tax pay for most of

its employees and operates it only for four order clerks, who are paid by results. Clifford Williams have introduced the scheme for two of their eight factories but will not be carrying it over into the other six - partly (but apparently not wholly) because of union difficulties. It came over quite clearly from Mr Heywood that trying to introduce net of tax pay in a larger company, with unions and a bureaucratised management, was very much an uphill struggle.

7. Second, all the employers concerned seem to have adapted their payroll systems successfully enough to cope with PAYE, on their own initiative and design, though in varying fashion. The most efficient system (a computerised one) was run by Henri-Lloyd.

8. Third, however, despite the experience of these employers, the idea of net of tax pay has not in practice yet spread widely. Mr Ferns of Stylewear and Mr Finley of Bradford Workwear are both very energetic publicists for their systems, and Mr Ferns in particular seems to have been visited by a steady stream of other employers. Mr Emile Woolf also (whom you saw in January) has spoken and written quite widely about the principle. Despite this, net of tax pay on Mr Ferns' lines is still operated by only a handful of employers. The danger (which Mr Heywood and others made clear to us) is that in moving from gross to net of tax pay the employer is taking a risk. Converting the employees' old gross pay into their new net gives them an effective pay rise of something like 20 per cent. Those who run these schemes regard this initial step as essential, but it may not pay off in terms of increased productivity. The accountant at Henri-Lloyd admitted frankly that in terms of straight

productivity their net of tax pay system was probably not justified. If the risk does not pay off, you would go to the wall or have to backtrack quickly and perhaps damagingly.

Mechanics

9. Whatever principle of calculation you follow, PAYE on a net of tax basis is a more complex operation than conventional PAYE, which is itself most easily and efficiently coped with on computer. The best way of coping with net of tax pay (mechanically) is therefore by computerised payroll.

10. However, we could certainly produce some assistance for an employer who wanted to operate net of tax pay manually. We think that the best approach to follow would be the one identified in my previous note (and summarised again at Annex A). This would involve our printing a revised Deductions Working Sheet (on the lines of the example at Annex B) and special Taxable Pay Tables to take the employer in one step from column 4 of the DWS to column 5. The tables could incorporate step by step instructions and advice on how to use them and the DWS together.

11. In terms of publicity, we could make it clear as part of our regular annual guidance to all employers that these tables and forms are available.

National Insurance Contributions

12. Stylewear and the other firms whom I visited pay their employees net of tax but not net of National Insurance Contributions. In other words, the employee receives a net of tax sum but has his or her NIC deducted from it. (As a matter of fact, the NIC is calculated on the true gross amount, as it should be).

13. I ought to make it clear that what we are proposing in paragraphs 10 and 11 is appropriate for a net of tax system but not for a system which is net of tax and NIC. We have discussed with DHSS whether it would be possible to do anything similar for the latter type of scheme. Unavoidably, it seems, the answer is "no". DHSS have a number of different rates of contribution for employees. This would mean that any table would need to be multiplied three times in any case - to accommodate, as a minimum, full-rate not-contracted-out contributions, full-rate contributions, and reduced rate contributions. This would complicate things for employers, quite considerably. More fundamentally, in relation to our Annex A example, nominal taxable pay could mean a number of different things in terms of gross pay, depending on what the individual's personal allowances were. DHSS must base their take on gross pay, which would not be a constant. If the amount in (a) of the example were £200 and in (b) - because of higher tax allowances - were £60, lines (c) and (d) would be unaffected, but the NIC due would be greater. DHSS's view is therefore that it would not be possible to build an NIC calculation into the tables we have in mind.

Financial and staff costs

14. We would need a print of 7,000 sets of tables and 70,000 Deductions Workings Sheets to give PAYE tax offices a reasonable initial supply. With appropriate overheads such as envelopes and postage this would cost about £10,000.

15. Staff costs are highly imponderable; they will depend on how many employers and employees participate in schemes of this sort in the future, and how the employer runs his scheme. We have looked at the extra tax office work which

arises in one of these net of tax schemes (Clifford Williams at Telford). There is frequent contact between employees and the tax office over the levels of PAYE codings and repayments of tax made outside the cumulative process (this is a type of extra work which tables and Deductions Working Sheets will not help with). If the extra staff cost of this scheme were repeated for us over five per cent of the employment field as a whole, this would mean an extra 300 staff units; if it covered ten per cent, 600 staff units, and so on. The likely spread of these schemes is an unknown factor, but these figures give an indication of the risk.

Conclusions

16. All the firms I visited have adapted the PAYE process successfully enough to net of tax pay (and, having done so, they would probably prefer to stay with their own familiar methods). Most employers contemplating introducing net of tax pay would probably conclude that they could best cope with the mechanics on a computer program or at least with a hand-held calculator.

17. Notwithstanding this, we could certainly go ahead with producing alternative tables and Working Sheets on the basis I have outlined above. Our own view remains, however, that the right course would be to leave matters as they are. Our reasons for this are essentially those set in my previous submissions. I realise that you are familiar with them, and have already given them careful thought, but perhaps I could outline them again briefly for the benefit of other Ministers. They are -

a. A net of tax pay scheme effectively neutralises the benefit of the personal allowances - a married man gets no more advantage from them than a single person ie their net pay is the same for the same job.

b. The introduction of a scheme raises wages - when one of the Government's major priorities is to maintain downward pressure on them - and (since the employer meets the tax bill) the aggregate effect of schemes will be to hamper any shift the Government may want to make in the balance between personal and business taxation.

c. On a strictly practical level, frictional difficulties occur on such points as the PAYE coding-out of minor sources of income, tax refunds after the end of the year, and changes in individuals' codes or the tax rates generally. Problems of this type can normally be sorted out with patience and goodwill, but it is impossible for the tax office to avoid getting involved in them. This means extra staff time and costs.

d. Even at its simplest, the procedures involved are different from (and more complicated than) conventional PAYE for our staff to grasp and explain, and for employees to understand. This goes very much against the grain of our struggle to cut staff costs and to restrain the tax system from throwing out more tentacles of complication.

e. We have found it very difficult to establish whether the "net of tax" label is a real incentive.

R R MARTIN

Alternative taxable pay tables It will be possible to produce tables which allow you to read a tax figure straight from a figure of nominal taxable pay, by multiplying the latter by a factor of $\frac{100}{70}$ x 0.3. The steps involved in the principle of the calculation would be -

a. Take "net of tax" pay figure (say) £170.

b. Subtract "free pay" (as reflected in coding) £30.

c. Therefore Nominal Taxable Pay £140.

d. Apply alternative tables: tax £60.

e. Add (a) and (d) to reach gross pay £230.

f. Calculate NIC on the gross figure at (e).

This of course involves constructing alternative tables, but is in principle a shorter method than the one set out in the present Employer's Guide.

Deductions working sheet P11 (New) (FoT)

AMNDA D

Employer's name

Employee's surname (in BLOCK letters)

First two forenames

Tax Code†

Amended code†

Year to April 19.....

Tax District and reference

National Insurance no.

Date of birth (in figures) Day Month Year

Works no. etc.

Date of leaving (in figures) Day Month Year

Week/Month no. in which applied

Pay in week or month	Total Net Pay to date	Total Free Pay as shown by Table A	Total nominal taxable pay to date	Total tax due to date as shown by Table 'G'	Tax deducted or refunded in the week or Month	Gross Pay in Month (Cols 1+6)	Total Gross Pay to date	MONTH number	WEEK number	National Insurance Contributions* Total of Employee's and Employer's Contributions payable 9a	Employee's Contributions payable 9b	Employee's contributions at Contracted out rate (included in column 1b) 9c
	2	3	4	5	6	7	8			£	£	£
								6 April to 5 May	1			
									2			
									3			
								1	4			
								6 May to 5 June	5			
									6			
									7			
								2	8			
								6 June to 5 July	9			
									10			
									11			
									12			
								3	13			
								6 July to 5 Aug.	14			
									15			
									16			
								4	17			
								6 Aug. to 5 Sept.	18			
									19			
									20			
								5	21			
								6 Sept. to 5 Oct.	22			
									23			
									24			
									25			
								6	26			
								6 Oct. to 5 Nov.	27			
									28			
									29			
								7	30			
										Total carried forward	Total carried forward	Total carried forwar

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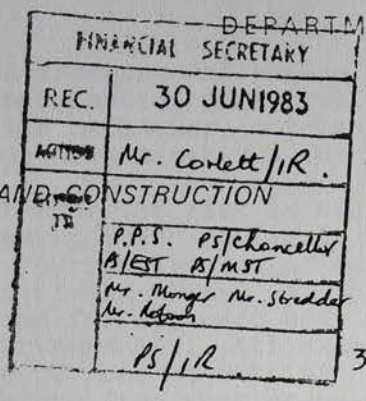
DEPARTMENT OF THE ENVIRONMENT
2 MARSHAM STREET
LONDON SW1P 3EB
01-212 7601

MINISTER FOR HOUSING AND CONSTRUCTION



Dear Neil,

30 June 1983

FINANCE BILL: CLAUSE TO RESTRICT CAPITAL ALLOWANCES FOR ASSURED TENANCIES TO APPROVED BODIES WHICH ARE LANDLORDS

You rang me last week about your proposal to include in the new Finance Bill a clause which will declare that capital allowances for construction expenditure on property let on assured tenancies are only available to approved bodies which are companies. The effect would be that any other type of approved body - and in particular partnerships of individuals - would then not be able to claim these allowances.

You will know that both Tom King and John Stanley were very concerned when this change was proposed before the Election, and on further consideration of the implications of this change, I am equally concerned. I am writing, therefore, to ask if you would please look again at the need for imposing this restriction.

Our policy continues to be to encourage the revival of investment in the private rented sector. There has been general agreement amongst Ministers that one useful way towards this revival is through the assured tenancy scheme, backed up by the capital allowances made available on an experimental basis last year.

The Family Policy Group was quite clear on this point at its meeting on 15 February. The successful development of assured tenancies will also contribute both to the welcome reduction in our reliance on municipal housing, which we are so concerned should proceed, and also to an increase in the proportion of the private rented sector letting at market rents - an objective which I know you share. It would be a pity, and will not be understood among the smaller landlords who are looking to us for encouragement in this direction, if because of their particular circumstances some good landlords, who are otherwise well-suited to participate in the scheme, are effectively excluded by a requirement that they have to trade as registered companies in order to qualify for the capital allowances.

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I know that you and Treasury colleagues have argued for the exclusion of non-incorporated partnerships on the grounds of potential cost to the Exchequer, not least because you fear the scheme could become a tax-haven for private individuals.

However, I doubt whether the risk is at all significant. Only one of the 71 bodies approved so far is a partnership, and that partnership is currently engaged on only one assured tenancy development of six flats. Of the 25 currently outstanding applications for approved body status, five are from non-incorporated partnerships. All except one of these have been formed for the purpose of letting residential property for some time. I therefore find your arguments of costs and tax avoidance unconvincing.

The long-term commitment involved in letting on assured tenancies, which is reinforced by the balancing charge provision in cases of early disposal under the capital allowance arrangements, means that only bona fide organisations with a genuine interest in providing new property for letting at market rents will find the scheme attractive. To restrict the ability of the smaller bodies to involve themselves in the scheme on the same basis as the larger bodies who are companies is not only damaging presentationally. It is also inconsistent with taxation policy towards partnerships of individuals involved in industrial buildings and hotels.

I would like to stress again our willingness to tackle any risks which may still concern you. For example, I would be pleased to examine ways of restricting capital allowances to active partners rather than sleeping partners, and also to consider tying the maximum relief to the corporation tax rate.

IAN GOW

Rt Hon Nicholas Ridley MP

2F

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DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

EXCHEQUER	
REC.	30 JUN 1983
ACTION	FST to deal.
COPIES TO	
	30 June 1983

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

FINANCIAL SECRETARY	
REC.	-1 JUL 1983
ACTION	MR. F. K. JONES
COPIES TO	PPS EST CST MST MR. MIDDLETON MR. BAILEY MR. WILDING MR. KEMP MISS KELLEY MR. JUDD MR. N. J. KING MR. ST. CLAIR MR. FARRINGTON.

Dear Nigel

Enclosed is a long letter about a nasty problem that has just arisen, which could cause considerable problems for our plans for privatisation of civil service activities. The problem arises from an Opinion from the Law Officers about the EEC Acquired Rights Directive. This could involve substantial extra costs on transfer, and thus jeopardise our plans to transfer heavy goods vehicle testing from this Department to Lloyds Register. We seem to be the first to run into this but clearly it could have wider implications for other transfers.

I hope therefore you will accept my suggestion of an early meeting with Law Officers.

Yours

TOM KING

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DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

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

30 June 1983

Dear Nigel,

PROPOSED TRANSFER OF GOODS VEHICLE TESTING TO LLOYDS REGISTER

One of my first tasks has been to review the progress of the privatisation initiatives in this Department. One of these is the transfer of heavy goods vehicle testing to Lloyds Register Vehicle Testing Authority (LRVTA).

We took powers in 1982 to transfer lorry and bus testing to the private sector. The industry itself was hostile, and we had some opposition from our own people, which we assuaged by agreeing that the function should go as a whole to Lloyds Register of Shipping, who have set up a separate body (LRVTA) for the purpose. This means, of course, that there is no effective competition, and that a statutory monopoly will be created with a licence fee income set by Government. Nevertheless, the transfer had, and still retains, distinct advantages. There is no doubt of Lloyds determination to maintain high technical standards. It will afford their management an opportunity to bring a single minded and purposive approach to the functions, and to introduce new technology. Not least it will remove some 1,000 people from the civil service, and help tilt the balance of power from the public sector unions.

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However, the transfer has not gone smoothly. It has already slipped massively: it was originally planned to take effect on 1 April 1983. The delays have not improved staff morale, nor have they made Lloyds any more enamoured with the deal. We have always recognised that the transfer could not take place unless sufficient of the experienced staff were willing to transfer to Lloyds and thus ensure the continuity of the statutory testing function. The unions are now consulting the staff on a revised offer of severance terms within the sum agreed between Geoffrey Howe and David Howell. They are to report back on 6 July, but all the indications are that it will be rejected by an overwhelming majority of the technical staff who are most essential to the success of the venture, both because they consider it inadequate, and because they are worried about their future with Lloyds as an employer.

All this, and a great deal of hard negotiation with Lloyds, has been done on the basis of advice from the Treasury Solicitor that the Transfer of Undertakings Regulations did not apply to this transfer, and in the light of that it was agreed that it should proceed in advance of the proposed Technical Redundancy Bill. We now have the advice of the Law Officers, admittedly in relation to the Technical Redundancy Bill, which suggests that the European Community Acquired Rights Directive, which the Regulations purport to apply in this country, covers this transfer, and that the Regulations would do so if they were not defective in a number of respects. This is a most unhappy state of affairs. If it is indeed the case - and my own preliminary view is that we are effectively bound by the Directive, notwithstanding the defects in the Regulations - our offer to the staff will have to be fundamentally revised, and this will need to be done in a way which we can carry through with Lloyds. We need quickly an authoritative legal view on the application

of these two instruments to this transfer and, to the extent that they are in conflict, which is the best and most defensible course to follow. I trust the Attorney General and the Lord Advocate, to whom I am sending copies of this letter, will be able to give us that urgently.

The attached note by my officials describes the situation as we see it in more detail, and identifies three options if the transfer is to continue as planned. First, we could adjust our offer so as to ensure a clear voluntary acceptance by the staff in full knowledge of their legal rights: on the present offer I judge this would mean we would have to add about £2m. to the existing £1.5m, but it could be more expensive. Second, we could operate directly on the one area where there is clear detriment and substantive concern, i.e. the redundancy compensation arrangements, by guaranteeing all those ex-civil servants PCSPS level redundancy terms for the remainder of their careers. Lloyds would resist this strenuously, not least because of its repercussions for their other staff. If they could be brought to accept it at all they would insist on an indefinite and unlimited guarantee. They may well in any case refuse absolutely to accept another aspect of the Regulations, the continuation of existing arrangements for collective bargaining. If we took either of these courses we should be using the powers in the Appropriation Act for making the compensation payments, and that would require a Ministerial statement about the intention to legislate at an early date. The third alternative would be to revert to the original scenario, and provide a clean break by offering full redundancy payments to all those concerned. This would solve problems with Lloyds and the staff but would cost some £8m. and would sit ill with our recent pronouncements. Moreover it is not clear to me that this

is possible, even on a voluntary basis, within the strict terms of the Directive. I think that we need legal advice on this point also.

I have considered whether it would help to defer the transfer until the Treasury's new legislation bites: but that would only be a valid option if we could keep Lloyds warm, could be sure that it would solve the problems we face and make a clear statement now about both its content and its timing. I gather we are not in a position to do that.

When we have the legal advice for which I have asked we shall need together to consider and cost whatever options are feasible in the light of it. The transfer will not come off unless the staff and Lloyds agree, and we need to be careful too that it does not put on the industry in terms of immediately increased fees a burden out of line with the longer term benefits it should provide. Lloyds are already producing new figures for 1984 which suggest fees higher than we had previously proposed. I understand that your predecessors thought the costs and benefits of the exercise closely balanced. These latest developments can only worsen the position.

If after a hard look we eventually conclude that the transfer does not offer demonstrable value for money, there are other ways of improving the service which we can examine. But the immediate priority must be the present deal. As I say, the unions are due to report back to us on 6 July. We cannot delay long beyond then without arousing suspicions, and indeed Lloyds will be looking for a clear statement of our plans before then. I think that the best course would be for you and me to meet with the Attorney General and the Lord Advocate within the next few days to discuss the way forward. I hope you will be prepared to arrange that.

I am sending copies of this letter also to the Prime Minister, to the Secretary of State for Employment and to Sir Robert Armstrong.

TOM KING

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TRANSFER OF VEHICLE TESTING TO LRVTA
THE ACQUIRED RIGHTS DIRECTIVE: THE IMPLICATIONS OF THE ATTORNEY GENERAL'S OPINION

1. The Acquired Rights Directive

The Directive requires Member States to provide rights for employees of undertakings which are transferred to new ownership to continue to enjoy their existing terms and conditions of employment (other than pension rights) after the transfer. It also requires Member States to ensure that the new employer is bound by existing collective bargains. The Directive is not of direct application. It was implemented in the UK by the Transfer of Undertakings (Protection of Employment) Regulations 1981. Those Regulations apply only to transferred undertakings which are "in the nature of a commercial venture".

2. The position on privatisations

In the course of developing policies for the transfer of Civil Servants to the private sector, advice was sought on the possible application of the Regulations in those circumstances. Treasury Solicitor advised in the autumn of last year that the Regulations did not apply to any of the privatisations in prospect for DOE/DTp because the activities to be transferred were not "in the nature of a commercial venture". There was at that stage no question as to whether the Regulations had satisfactorily implemented the Directive.

3. In the autumn of last year the Government decided to legislate to prevent Civil Servants who were being transferred to the private sector on equivalent terms of employment and who refused to accept those terms from having access to full redundancy compensation. As part of the preparation for that Bill, the Treasury sought an Opinion from the Attorney General on the scope of the Directive and the Regulations to place matters beyond doubt. The Attorney General pronounced shortly before the Election. Contrary to expectation he took a clear view that the Directive did apply to Civil Servants and

that the Regulations had not properly given effect to the Directive which applies to activities "of an economic character", a much less restrictive description than "in the nature of a commercial venture". That being so, he also advised that the Regulations did not satisfactorily deal with the right of transferring Civil Servants to have preserved their entitlement to redundancy compensation under the PCSPS. He was also clear that entitlement to redundancy compensation was a crucial part of the terms of employment covered by the Directive. He did not take the view that it would be necessary or could be expected that a private sector employer would be able to offer redundancy compensation terms as generous as those now enjoyed by Civil Servants but in that case staff should be offered compensation by the Government to buy out their existing rights. That would require the agreement of the staff. But there is no existing means by which Civil Servants can agree to accept changes in the PCSPS arrangements; that would require primary legislation.

4. Application to the HGV privatisation

The Department sought an urgent view from the Law Officers' Department on the relevance of the Attorney General's Opinion to the transfer of vehicle testing to LRVTA. Their advice is that the Directive does apply in this case. There are grounds for maintaining that the Regulations as they stand do not apply, but they conclude that it is "undoubtedly legally safest" to operate on the basis that they do apply, but this poses the difficulty of a direct transfer of the existing "contracts of service".

5. This suggests that the only sensible course to take is to accept that the Directive does apply and that we should follow the Attorney General's advice on how it should be implemented in UK law, despite the wording of the existing Regulations. There can now be no question of sweeping this under the carpet. There is the possibility of a challenge in the European Court. We could not properly hide what we now know from Lloyd's Register whose position is also affected. Neither the Department as employer nor the Government as a Member State can avoid the advice we have received on the application of the law.

6. This opens up a number of difficulties with the arrangements we have been making for transfer of testing staff:-

(i) <u>it casts doubt on the legality of the offer of compensation put to the Unions</u>.

We have already proceeded in the spirit of the Directive by offering compensation for the loss of certain pension benefits and rights of compensation on redundancy. But these have been calculated as global sums, not as figures to set against each individual's right to preserve his existing terms. In addition changes in other terms of employment - eg hours of work, leave etc - have been brought out in the offer of higher salaries by Lloyds. We could not speak for the calculations there. The political stance the Unions now appear to be taking makes it very likely that they would seize on any grounds either for challenging the severance terms in the UK courts or for taking up with the Commission in Brussels the wider question of the UK implementation of the Directive.

(ii) <u>it places legal obligations on LRVTA</u>.

Lloyds have always been adamant that they would only take on Civil Servants on their own terms and conditions of employment. They do not want to offer terms which could open up difficulties for their relations with their existing Lloyd's Register staff. They have also been adamant that they would not wish to continue the existing arrangements for collective bargaining, though in the course of negotiation their line has softened slightly here. The application of the Directive poses two particular problems. The first is the requirement to take over existing collective bargains. That is a clear obligation which cannot be bought out. It could only be overcome by agreement by the Trade Unions to change existing arrangements. The second is that, even if transferring staff were to accept changes to their conditions of employment with appropriate compensation, LRVTA would be exposed

to the possibility of actions in the courts for failure to comply with the Regulations. We had always known that action might be taken against the Department on the severance terms, but not against LRVTA. Lloyds would no doubt wish to be indemnified against any successful claims if they were prepared to shoulder the burden at all.

(iii) it destroys the timetable for transfer and almost certainly inhibits the ability of the Department to pursue the negotiations on this transfer without creating precedents for future privatisations.

7. The courses now open seem to be:-

(i) To make everybody redundant, paying them full redundancy compensation and in effect placing the transfer outside the scope of the Regulations. Whilst there cannot be absolute certainty that this would avoid the problems the Directive poses, or be legally compatible with it, it is highly unlikely that with compensation at that level there would be any challenge in the courts. Full redundancy compensation is what the Unions have always sought. The staff would be willing to transfer. This is the only course which would solve the difficulties (see 6(ii)) which Lloyds are otherwise likely to see as insuperable. The difficulties are:-

a) the cost of the payments - about £6.5 m above the compensation now being offered;

b) the political implications. Ministers have previously rejected this course and believed it to be publicly indefensible to pay redundancy compensation to staff who are not redundant;

c) the precedent it would set for future privatisations in advance of any bill.

(ii) Re-work the severance terms for each individual to provide a package of compensation which could stand up to the scrutiny of the courts. It would, we believe, be possible to calculate on formulae acceptable to staff and Unions compensation for changes in terms, either in the form of a salary increase or lump sum payment, apart from the loss of entitlement to Civil Service redundancy compensation. The Government Actuary has already been asked to produce a calculation for that factor and came to the view that an actuarial formula could not be reached because it was impossible to judge the risk of redundancy. If we pursued the idea we should have to accept a rough-and-ready approach in negotiation. The outcome would have to be acceptable to the staff and their ability to accept it (see para 3) would have to be assured by legislation. The cost is unknown and could be high but from staff reactions to the existing offer there is reason to think that a deal could be secured for an additional £2 m or so. It would be possible within that figure to offer the more senior and highly paid staff - who are crucial to a successful transfer - very substantial increases on the present offer. The difficulty is that this would set a precedent for other privatisations and for the Treasury's Technical Redundancy Bill. This is bound to mean significant delay. Even if a formula were found acceptable to colleagues and to the Unions we could still not be certain that staff would willingly transfer. The problems of Lloyd's Register would remain.

(iii) Re-work existing severance offer as in (ii) but preserve existing entitlements to redundancy compensation rather than seeking to buy them out. This would avoid the need to calculate and defend payments but Lloyds would require an indefinite 100% indemnity from the Government against any costs incurred as a result. Although cheaper than either of the other options, it is difficult to see how the Government could properly enter into an unlimited contingent liability of this kind, with no direct control over the incidence or amount of payments made. We also believe it very unlikely that Lloyds would agree to offer contractual arrangements for redundancy payments even with a full

indemnity, because of the precedent it would set for their own and future LRVTA staff.

(iv) Delay the transfer until the Technical Redundancy Bill is enacted. Deferment would only be a conceivable option if we could make a clear statement now on the Bill's timing and content, and if the content would clearly solve our problems. In fact the Bill's place in the programme for this Session is doubtful, and its content will in any case not be clear until after the conclusion of the discussions which will now be needed with the European Commission on the relation between the Directive and the Regulations. The lengthy delay would be untenable. Staff morale would be further damaged. Lloyds would almost certainly back out, for we could offer them no certainty of the position after the legislation nor that the Bill would deal with their concerns about the application of the Directive. They would in any case demand immediate payment of their expenses - about £½ m.

8. Next steps

The Unions meet management to report the results of their consultation with members on the existing severance offer on 6 July. Both they and Lloyds have been told to expect that invitations would be issued to staff to apply for jobs with LRVTA shortly after that. We shall have to explain what is happening to Lloyds, but, if we are to keep them in play, can hardly do that until we are clear what our course is now to be, and how far that can alleviate the major problems which both the Directive and the Regulations seem certain to pose for them.

Department of Transport, SW1

28 June 1983