

PO-CH/NL/0004  
PART B



STARTS 20-02-84  
ENDS 02-03-84

**SECRET**

(Circulate under cover and  
notify REGISTRY of movement)



PO -CH /NL/0004



PART B

BUDGET SPEECH 1984

NDs 25years N.A. 25/08/94

/NL/0004

-CH

PO

PART B

**CLOSED**

CONTINUED ON:-

PART C.....



PO/CH/NL/0004

PT. ~~A~~ B.

Budget      Speed  
84.





FROM: M E Corcoran  
DATE: 20 February 1984

PRINCIPAL PRIVATE SECRETARY

- cc PS/Chief Secretary
- Mr Anson
- Mr Byatt
- Mr Cassell
- Mr Watson
- Mr Battishill
- Mr Monger
- Mr Folger
- Mr R I G Allen
- Mr G P Smith
- Miss Goodman
- Mr Lord
- Mr Portillo
- Mr Isaac } Inland
- Mr Blythe } Revenue
- Mr Wilmott - C&E

*Re ① hold  
under } have  
clear }  
with }  
No ②, I agree. m.*

*I think we can  
now agree.  
Subject to JIC  
Proposed priv  
PEIT - Boreham  
contact. ?*

*JIC*      *Yes m.*

PRESENTATION OF BUDGET MEASURES

The Minister of State would be grateful for the Chancellor's agreement on two points.

First, the information presently available from the Family Expenditure Survey is adequate for the Treasury to assess the distributional effects of changes in, for example, indirect tax rates and simple upratings. It is not adequate for the kinds of indirect tax changes now contemplated. The Minister would therefore be grateful for the Chancellor's authority for officials to approach CSO so as to get the detailed information needed to make the best estimate they can of the effect of indirect tax changes in the Budget.

*? Yes - but after*

*PEIT → J Boreham*

*Ministry houses on leads?*

In assessing the distributional effects and the effects on persons of the Budget, child benefit will need to be taken into account. The decision on the level operating from next November will be taken and announced at the appropriate time and in the meantime the Public Expenditure White Paper assumes a 5½ per cent uprating. The Minister would be grateful for the Chancellor's agreement that the same assumption be made for the purposes of the present exercise.

*Must be right?*

*EE*

M E CORCORAN  
Private Secretary



Copy No 23 of 25.CH/EX REF NO B(84)197

FROM: J O KERR

DATE: 20 February 1984

cc Chief Secretary  
Financial Secretary  
Minister of State  
Economic Secretary  
Sir P Middleton  
Sir T Burns  
Mr Littler  
Mr Bailey  
Mr Cassell  
Mr Monck  
Mr Lankester  
Mr Monger  
Mr Scholar  
Mr Odling-Smee  
Mr Ridley  
Mr Lord  
Mr Portillo  
  
Sir L Airey: IR  
Mr Painter: IR  
Mr Fraser: C&E  
Mr Wilmott: C&E

MR BATTISHILL

**BUDGET SPEECH: FIRST DRAFT**

The Chancellor has worked this weekend on the version of the speech which you submitted on 17 February. I am sending you - and selected copy addressees - notes of his reactions to particular sections: this minute sets out his reactions to the speech as a whole.

(a) First, he believes that, at around 12,000 words, the text is too long. So the emphasis must be on paring away unnecessary verbiage.

(b) Secondly, he believes that the length of the various sections, and of the treatment of different subjects within these sections, does not adequately reflect their relative importance. Thus, for example, the MTFS section is very short, and does not contain any clear re-statement of the purpose of the MTFS, while the major CT/Capital Allowances/Stock Relief reform is covered in only one-third of section J, though much of the rest of section J contains fairly trivial matters.





- (c) Thirdly, he is inclined to think that the two year theme has got lost, and needs to be re-inserted fairly frequently.
- (d) He agrees with you that the PSBR - in the sense of "the Budget judgement" should be tackled in section G, while section D explains the MTFs (but without numbers).
- (e) He is clear that the LTPE section of section F needs to be considerably lengthened and strengthened.
- (f) He is sure that it would be a mistake for the first tax measure to be announced to be the exemption from CGT of new corporate fixed interest securities (section E, paras 13 and 14). He suggests that a home be found for this announcement in section K, between the LAPR and IIS announcements.
- (g) He considers that section J para 20 represents a totally inadequate presentation of PAS abolition. How best to present it needs careful thought, but he is convinced that the present marker paragraph won't do at all.
- (h) The share options section of section K can, he thinks, be considerably reduced, and should be transferred to section J, perhaps after the present para 14.
- (i) Foreign earnings and emoluments can he believes, similarly be shifted to section J from their present position in section L (paras 4 to 6).
- (j) Finally the public expenditure section should, in his view, contain a section on civil service manpower, the 1984 target achieved, and the 1988 target set.
2. Copy addressees will no doubt wish to let you have any further reflections on the overall structure of the draft.

A handwritten signature in dark ink, appearing to be 'J O Kerr'.





Copy No 1

FROM: A P HUDSON

DATE: 20 February 1984

PRINCIPAL PRIVATE SECRETARY

cc Chief Secretary  
 Minister of state  
 Economic Secretary  
 PCC Members  
 Mr Evans  
 Mr Lankester  
 Mr Monger Mr Battishill  
 Mr Odling-Smee  
 Mr Ridley  
 Mr Lord  
 Mr Portillo  
 Sir L Airey - IR  
 Mr Painter - IR  
 Mr Fraser - C&E  
 Mr Willmott - C&E

*A matter concerning  
 mis-type in section 1,  
 para - 17 ~~with~~ alterations  
 Schmidt.*

BUDGET SPEECH: FIRST DRAFT

1. The Financial Secretary has seen the speech attached to Mr Battishill's 17 February minute.

2. He has one general comment. The theme of the Speech is clear. But he would like to see another thread brought out clearly, along the following lines: the Government's first five years put in place the proper disciplined frame for the economy; that laid the basis for real jobs; now, the Government is concentrating on providing the conditions in which employment will grow.

3. He has the following specific comments.

Para A 3 - The word "hopefully" seems very tentative.

Para A 5 - In the second sentence, could we say "a simpler and more effective tax system for all"?

Para A 7 - In that, on present indications, the Chancellor will be announcing only part of next year's tax reductions, is this the best way to put an important point?

Para C 2 - In the middle sentence, should the Speech add that we were "saddled with heavy international debts"?



Para C 11-C 12 - The transition between these two is very abrupt.

Para D 5 - In the Final sentence, it may actually be easier to say "to eradicate inflation". There is no time frame attached to that, and "lower inflation" implies acceptance that there will be some inflation permanently.

Para E 4 - In all the comments on our monetary policy, we fail to explain the complications which were created by the removal of the "control" apparatus over the past four years. Thus not only do we lose out from not getting across the consequences of this for interpreting monetary data, but also take little credit from the remarkable achievements in these areas.

Para E12 - As oppose to a general warning, could this not be a little heavy-handed in the context of a Budget Speech, and thus create a little more concern than was intended.

Para E23 - The third sentence ("I have accordingly decided .....") risks recreating speculation which the second sentence would dampen down.

Block H - One additional point should be made: because of the complexity of the reliefs, there is a critical difference between the low yield of many taxes and the perceived high rates and disincentive of those taxes.

Para I12 - At the end of the first line, replace "power" with "office" (or a similar word).

Para J 3 - The point should be made that company liquidity was extremely low when stock relief was introduced, and is very different now.

Para L 6 - In the final sentence, it is sensible to say "For the present"?

AMH

A P HUDSON



00239

FROM : M D X PORTILLO  
DATE : 22 FEBRUARY 1984

CHIEF SECRETARY

cc Mr Ridley  
Mr LordPORTILLO  
22/2

## PRESENTATION OF BUDGET MEASURES

I wondered whether it might help to have some skeletal notes on some of the main arguments in your presentational area. It may be as well to start rehearsing them now, and you may even wish to attach an annex to your note to the Chancellor.

1. The Better-Off

This Budget is not a give-away to the rich. Virtually every spare penny in this Budget thrown into raising thresholds to help worst-off taxpayers. Inevitably that benefits all taxpayers right up the scale, but worth noting that:

- ✓ a) Higher thresholds raised only in line with inflation, despite the regrettable squeezing of the 40% band.  
Higher thresholds to rise 7% less than basic allowances.
- NO b) Car benefit scales to rise by almost twice indexation, despite large increases in recent years.
- NO c) Those spending more than 30 days abroad lose substantially from their present position on foreign earnings deduction change.
- ✓ d) Investment income surcharge abolition does greatly benefit a few - those who were paying a confiscatory 75% rate. But half of those benefiting are old, and many pay income tax only at standard rate. For the self-employed, IIS acted as a virtual tax on pensions ie on the income from investments made in order to provide for retirement.



NO

e) CGT threshold increased only by indexation.

✓

f) CTT : abolition of top rates sensible since 75% confiscatory.

No

g) Mortgages over £30,000 and second mortgages are caught by consumer credit duty.

2. Tax reforms

This Budget removes certain absurdities: confiscatory tax rates and over-generous allowances.

✓

a) Highest rate of tax will now be 60% compared with 98% in 1979. (IIS and CTT top rates scrapped). Healthy level that falls short of confiscation.

*abolish foreign*

b) We are ending the 30 day foreign earnings rule which was abused by many taxpayers and a nuisance to many employers. It is needed much less now than when the top rate was 75%. Inland Revenue will look at travel to and from foreign place of work.

c) We are phasing out the foreign emoluments deduction. Many foreigners regard Britain as a tax haven and pay much less here than they would at home or elsewhere in Europe. Certain anomalies like the second generation Pakistani working for Lufthansa. Also much less needed now top rates lower.

*MTG (summit):  
not for  
fair tax*

d) Removal of life assurance premium relief takes away an important distortion on investment behaviour.

3. Stamp Duty

✓

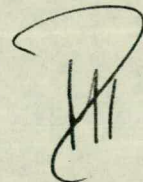
a) Reduction on housing very important for encouragement of home ownership and construction. Removed entirely from



homes £25,000 to £30,000. Absurd to overtax moving house when we need mobility.

- ✓ b) Reduction on equities emphasises our encouragement of capital owning as well as property owning democracy. Essential to help Stock Exchange to remain internationally competitive.

*7 - 1/2% for small units*



M D X PORTILLO





MR PORTILLO

FROM: A M ELLIS

DATE: 22 February 1984

cc PPS-  
PS/Chief Secretary  
PS/Financial Secretary  
PS/Minister of State  
Sir Peter Middleton  
Sir Lawrence Airey  
Mr Cassell  
Mr Monck  
Mr Battishill  
Mr Monger  
Mr Allen  
Mr Folger  
Mr Hall  
Mr Norgrave  
Mr Willetts  
Mr Ridley

## PRESENTATION OF BUDGET MEASURES

The Economic Secretary suggested that it would be a good idea for there to be drawn up a table of "winners and losers" amongst <sup>Conservative</sup> back benchers. The idea would be to have to hand a record of which back bench demands (and whose) would be met by Budget measures and which would not, so that the reaction to the Budget on the back benches could be predicted with some precision and, where necessary, pre-emptive action taken.

We spoke this morning and you agreed to pull together a preliminary assessment in time for next week's Budget overdue meeting.

A M ELLIS



BUDGET: SECRET

E 3

MR KERR ✓

(PWP)

FROM: ADAM RIDLEY  
22 February 1984

cc CST  
FST  
EST  
MST  
Mr Monck  
Mr Battishill  
Mr Folger  
PS/IR  
Mr Isaac/IR  
PS/C & E

PRESENTATION OF BUDGET MEASURES

Following your minute of February 14, and the allocation of Ministers to subject areas, I have discussed with Mr Lord and Mr Portillo how the advisers should divide their labours between the various pieces of work which have been launched. We would suggest that we should divide our labours as follows:

CHIEF SECRETARY: Mr Ridley and Mr Portillo

FINANCIAL SECRETARY: Mr Lord and Mr Portillo

MINISTER OF STATE: Mr Lord

ECONOMIC SECRETARY: Mr Ridley.

By and large we have established the necessary contacts with Private Offices and key officials. But where we have not, it would help greatly if those responsible could keep us posted as to relevant meetings, copy us papers and bear our interests in mind. As in past years, it falls to us to produce very extensive briefing for MPs and others, which has to be complete and ready for circulation on Budget day. Moreover, and in contrast to past years, we will have to set to work preparing it well before the weekend preceding the Budget.

*AR*

A N RIDLEY



22 FEB 1984

FROM: N MONCK  
DATE: 22 February 1984

000251

19

FINANCIAL SECRETARY

- cc Chancellor
- Chief Secretary
- Minister of State
- Economic Secretary
- Sir P Middleton
- Mr Cassell      Mr Byatt
- Mr Battishill
- Mr Monger
- Mr Lovell
- Mr G Smith
- Mr Hall
- Mr Folger
- Mr Portillo
- Mr Beighton    )
- Mr Crawley     ) IR

PRESENTATION OF BUDGET MEASURES

We are to discuss with you tomorrow the presentation of the major business tax changes. The list allocated to you in Mr Kerr's minute to you of 14 February also includes the North Sea and small companies. It would make sense to add unincorporated business and the self-employed to your list. But you will presumably be dealing with your responsibilities for share options and for the structure of personal taxation separately.

MONCK  
2/2

2. I attach notes produced by the Inland Revenue/<sup>Customs</sup>and FP on the main individual measures in your list, covering key themes, history and pitfalls (the first 3 of the subjects in Mr Kerr's commissioning note). These notes are, as you will see, no more than a first shot at the raw material which will later be transformed into the main instruments of presentation other than the speech itself: Press notices, budget briefs, notes for particular Groups such as backbenchers and the CBI, and possibly an EPR article. We envisage that on this occasion there should, be in addition to revenue department Press notices on individual measures, a Treasury Press notice on the business tax reforms.

Main Themes

3. The main theme will be the aim of improving economic performance through strengthening the supply side of the economy. The tax reforms will achieve this by:



- a. increasing aggregate post-tax company profits so increasing the rewards for success and initiative by reducing the tax bite on profits. <sup>This</sup> will stimulate companies to intensify their search for profitable activities and so lead to higher output and, other things being equal, more investment;
- b. reducing the extent to which the tax system distorts investment incentives, leading <sup>to</sup> a better quality and therefore more productive capital stock;
- c. reducing the tax subsidy to certain kinds of investment, discourage them. This will mainly take the form of reducing investment whose pre-tax yield is so low that it tends to reduce rather than increase living standards;
- d. reducing the cost of labour, increase employment in the medium term;
- e. widening the tax base and simplifying the system.

Budget Speech

4. The speech must be the main way of getting across the positive points in the previous paragraph and also of setting up the scaffolding for defensive lines. (In particular Press notices can be given a non-factual policy steer by means of references to the speech.)

5. I suggest the first item for your meeting tomorrow is to consider whether the present sequence of the speech hinders getting the positive points across. My own opinion is that it does. I appreciate the theatrical effect of leaving NIS to the end as a delightful surprise. But I think we need it in Block J for two main reasons:

- a. the abolition of NIS is the major element in lightening the tax burden. Without it we have to rely on the rather small benefit in 1985/86 of the Corporation Tax package. It is only about £450 million or £300 million if we knock off the new withdrawal of <sup>the</sup> ACT concession from the North Sea.



About half of the lower figure goes to the financial sector;

- b. we need NIS to complete the story about remedying the present bias in the tax system in favour of capital and against labour and as an offset to the overall increase in the cost of capital resulting from the CT reform.

6. There is also a problem about the placing of PAS. At the moment it comes at the end of Block J. I prefer Sir Peter Middleton's earlier suggestion that it should come in Block I on indirect taxes. It could follow the other VAT and "anti-EEC" items, and be justified in those terms and as a measure which, though having a mixed reception in industry, will give UK manufacturers of finished goods the same competitive advantages in their home market as similar businesses in most EEC countries enjoy. (A substitute surprise at the end would be on tax thresholds. Probably more of a surprise and qualifying the pro-business theme.)

Pitfalls and Defences

7. There are two general problems of presentation:

- a. there may be immediate hostile reactions not only from the potential losers we have foreseen (Nissan phase 2; ship owners; cable; tax-exhausted) but from others. Warnings or announcements about cancelling projects are a real possibility. So are big movements in share prices (which the Bank and the Revenue are seeking to predict). There may also be problems of a kind we have failed to foresee;
- b. the reactions from special cases will be amplified because parts of the budget could be represented as attacking motherhood - investment (regardless of quality) and manufacturing. There is a risk of the CBI and TUC uniting in opposition to these.

8. The first point suggests that Ministers will need to be very careful to distinguish bullish statements about the benefits to business in the aggregate from suggesting that there are prizes for all individual businesses. The general defence about losers will be that this is



BUDGET SECRET

- 4. -

inevitable in<sup>a</sup> bold and far-seeing reform which marks a changes of direction from persistent past failures of an interventionist kind.

9. The second point suggests a special effort to persuade the CBI that it cannot sensibly reject what is pre-eminently a pro-business budget, despite losers in manufacturing. You will wish to consider what can be done on this apart from preparing a special note for the CBI (as last year). . '

10. So far as the "anti-investment" criticism is concerned there are three big points which might appear in the budget speech:

- a. the rise in post-tax profits will work in the opposite direction from the rise in the cost of capital;
- b. in the next year or two some capital expenditure will be brought forward in order to catch the remaining first year allowances. The return on this investment will be enhanced by immediate and future cuts in the CT rate. (But this accelerated investment will include some low yielding projects);
- c. quality is what matters. The existing system gives bigger incentives to plant and machinery etc than in most other advanced countries. This has distorted the pattern of investment and may have contributed to the exceptionally low return on investment here. The argument about preparing for adjustment "when the oil runs out", far from pointing to retaining the present distortions, is an argument for getting rid of them and fostering investment which does not need subsidy (or needs less subsidy).

11. Two other pitfalls are:

- a. the failure to consult; and
- b. the reliability of a lasting low CT rate.



12. On a. the answers are presumably that we have stuck to the imputation system, the need to get reform started; the care with which the Government are phasing the reform and helping business to plan not only by pre-announcing but by legislating for the future changes.

13. On b. the answer must lie in the credibility of the MTF5 and of the LTPE, though a weakness of the latter is that it does not represent a policy decision only a statement of the problem and the case for flat public expenditure.

Sectors

14. At the end of this minute, for convenience, I attach a copy of slightly out of date tables: one showing the overall impact on business prepared by the Central Unit; and two produced by DEU showing the sectoral split of CT, NIS and PAS. Other Ministers are dealing with agriculture, construction, and the financial sector. We shall in particular need to consider whether to include the North Sea measures in the CT package.

15. There are two things we need to do here. One, not I suggest for your meeting, is to ensure that we do not have double counting ie that our sectors do not overlap. (The cake is of course cut differently for small companies, unincorporated business and the self-employed.) Officials will sort this out after your meeting.

16. The second subject could be usefully discussed at your meeting. This is how much detail to give in public about sectoral numbers. We shall clearly need to give overall totals for business as a whole, probably with the main component measures. But I suggest we should be very much broader in talking about different sectors of the economy. Many of the figures are based on heroic estimates and could not be seriously defended, even if they could not be conclusively refuted. In general it seems sensible to adopt a policy of confining statements on sectors to saying that they gain (or lose) overall with some broad indication of the measures which benefit (or hit) them and their relative importance. We do not want a whole series of PQs or questions from select committees about detailed figures for sectors or sub-sectors.



PAS

17. The problem here is that we count this as £1.2 billion in the claim that the budget as a whole is neutral, but need to score it as its interests costs and not its cash flow effect to claim that business gains in 1984/85. We cannot have it wholly both ways. The counterpart of the genuine difference between PAS and the other tax measures - that it does not affect costs or profits by anything like its cash flow effect - is that the monetary benefit of this once and for all switch will be reduced by the increase in bank lending. However this will be much less than pound for pound: for one thing foreigners will bear some of the cost and companies can meet the once and for all cost of PAS by means other than bank borrowing. This suggests that we should be ready to treat PAS publicly in two different ways. No doubt our first approach will be to score it in interest terms but we should be ready to acknowledge to obvious cash flow effect as well which turns 1984/85 into a loss for business. Hence the need for the two year approach which the Chancellor wishes to emphasise in his speech.

Conclusion

18. You and others will no doubt have points of your own or taken from the attached notes to raise. But I suggest that the agenda for your meeting tomorrow might include the following points, some of which, if you agree, might be reflected in a minute from you to the Chancellor:

- a. are the main themes on business tax reform the ones set out in paragraph 3 above;
- b. do you agree that the present sequence in the budget speech makes it difficult to get these points across;
- c. are the pitfalls and defences outlined in paragraphs 7-13 on the right lines and what <sup>major</sup>/alternatives/additions are there?
- d. is the approach to giving sectoral figures in public in paragraph 16 agreed?
- e. do you agree that, in addition to the revenue departments Press notices on individual measures, there should be a Treasury Press notice on business tax reforms in general?



BUDGET SECRET

- 7 -

- f. is it agreed that a special effort to win over the CBI should be made and, if so, how should it be done? Should there be a special note for the CBI as last year, as well as a Treasury Press notice?
- g. what other groups should be approached;
- h. is the approach to PAS in paragraph 17 agreed.

In the light of your meeting officials will go ahead with drafting Press notices, budget briefs and notes for special groups such as backbenchers and CBI.



N MONCK

Other relevant papers:

Paper on Economic Effects of CT Package etc (attached to minute to the Chancellor of 21 February);

Mr Norgrove's minute to Mr Battishill of 15 February on Presentation of Budget Measures.



BUSINESS	£m		Will <u>lose</u> directly from:	£m	
	1984-85	1985-86		1984-85	1985-86
Will <u>gain</u> directly from:					
Reductions in the corporation tax rate to 50% in 1984-85 and to 45% in 1985-86	200	1050	Reductions in the Capital Allowances and Stock Relief which may be set against CT		750
Reduction in the small companies rate to 30% in 1984-85	80	150	North Sea farm-ins		35
Stamp duty cut on share transfers: it is estimated that businesses will benefit from about three quarters of the value of this measure	120	145	Controlled foreign companies' profits brought into tax		25
Stamp duty cut on land & buildings: it is estimated that business will benefit from about a third of the value of this measure	90	110	Abolishing special low Building Societies CT rate		15
Abolition of NIS	465	925			-805
TSB's corporate status		10			
Carry back of ACT		30			
Deep discount stock		15			
Raising DLT threshold		2			
	<u>          </u>	<u>          </u>			
	+955	+2455			

Overall Business will gain in 1984-85 by £955 m  
and gain in 1985-86 by £1650m

But the effect of PAS also needs to be taken into account: two alternative treatments are possible:

- the cash flow reduction in 1984-85 of £1200 m, due to acceleration of VAT payments: the overall net cash flow loss in 1984-85 is then -£245 m
- the interest cost of permanently paying VAT 7 weeks early which will be between £120 m and £150 m p.a. But as abolition is scheduled for October 1984 and the first payments of VAT under the new arrangements will not be made till November, the first year cost will be about £50 m. This reduces the overall gain to business to about £900 m in 1984/85 and to about £1550 m in 1985-86

And can be said to gain indirectly from:  
Lower imports due to PAS.

And may be represented as losing from:

Widening of the VAT base - industries/trades concerned will lose some business.  
Change in treatment of VAT financial sector supplies.  
Life assurance premium relief - life offices will complain.



Composite rate for banks - which the banks see as a threat to business.

(Perhaps) loss of foreign earnings and foreign emoluments deduction - which they may have to compensate with higher salaries.

(Perhaps) higher car benefit scales - which companies and the motor industry always complain about.

More than indexation of any excise duties.

Credit Licence Duty - paid initially by the financial institutions. Even if the whole cost were passed to individuals through higher interest rates the financial sector might suffer a reduced volume of business.



TABLE 1

## BUDGET SECRET

EFFECT ON A. CASH FLOW & B. ON PROFIT OF PRIVATE INDUSTRY BY SECTOR: 1984/85 £m  
(Gain +, Loss -)

GAIN/LOSS ATTRIBUTED TO	ABOLISHING PAS (CASH FLOW)	2% REDUCTION IN CT RATE	ABOLISHING NIS	A TOTAL CASH FLOW	PAS INTEREST COST	B TOTAL PROFIT				
Manufacturing	-470 to -920*	+ 85	+ 175	-210 to -660	- 30	+ 230				
Distributive Trades	-150 to -600*	+ 50	+ 80	- 20 to -470	- 5	+ 125				
North Sea	- 5	+ 55	-	+ 50	-	+ 55				
Financial	- 40	+ 45	+ 55	+ 60	+ 5	+ 105				
Construction	- 5	}	+ 30	}	}					
Transport & Communication	- 10		+ 45							
Energy & Water Supply	-		+ 45				+ 25	+105	-	+ 195
Other Services	- 75		+ 45							
Agriculture, Forestry, Fishing	-		+ 5							
<b>TOTAL</b>	<b>-1200</b>	<b>+280**</b>	<b>+ 460</b>	<b>-460</b>	<b>- 30</b>	<b>+ 710</b>				

Footnote \* The split of losses between manufacturing and distribution will depend on how quickly distributors can pass on the squeeze on their liquidity to other sectors. The top end of the range for manufacturing (and the bottom end for distribution) assume all the imports by distributors that are for intermediate use by other sectors are for manufacturers and that distributors pass on the liquidity squeeze immediately. The PAS interest estimates are consistent with the top end of the range for manufacturing.

\*\* Includes effects of 8% reductions in small companies rate.

ANNEX  
To 2/12/84  
PAPER



**TABLE 2**

**GAIN (+) OR LOSS (-) TO PROFITS OF PRIVATE INDUSTRY BY SECTOR 1985/86**

£m

<b>GAIN/LOSS ATTRIBUTED TO</b>	<b>CA</b>	<b>SR</b>	<b>CT</b>	<b>TOTAL CORPORATE TAX</b>	<b>NIS ABOLISHED 1 AUG 84</b>	<b>PAS cost (interest)</b>	<b>TOTAL</b>
<b>MANUFACTURING</b>	- 70	- 230	+ 345	+ 45	+ 355	- 115	+ 285
<b>DISTRIBUTIVE TRADES</b>	- 40	- 160	+ 215	+ 15	+ 165	- 20	+ 160
<b>NORTH SEA</b>	- 45	-	+ 295	+250	-	-	+ 250
<b>FINANCIAL</b>	- 30	- 10	+ 165	+125	+ 100	+ 25	+ 250
<b>CONSTRUCTION</b>					+ 60	-	
<b>TRANSPORT &amp; COMMUNICATION</b>					+ 90	-	
<b>ENERGY &amp; WATER SUPPLY</b>	- 60	- 105	+ 180	+ 15	+ 55	-	+ 315
<b>OTHER SERVICES</b>					+ 90	- 10	
<b>AGRICULTURE, FORESTRY, FISHING</b>					+ 15		
<b>TOTAL</b>	- 245	- 505	+1200*	+450	+ 930	- 120	+1260

\* Includes effect of 8% reduction in small companies rate.

CA = Capital Allowances

SR = Abolition of Stock Relief

CT = Corporation Tax rate

CT = Revenue effects based on Annex A Table 2

BUDGET SECRET



National Insurance Surcharge

(1) Theme

(i) NIS is a tax on jobs. Introduced by last Labour Government and rate was  $3\frac{1}{2}$  per cent when they left office. If this had continued private sector would have paid about £3 billion [£3.025 billion] in 1984-85. Abolition, together with the rest of the corporate tax package, will reduce the bias in favour of capital and against labour.

Positive

(i) Rate was cut from  $3\frac{1}{2}$  per cent to  $2\frac{1}{2}$  per cent in Finance Act 1982, to  $1\frac{1}{2}$  per cent in National Insurance Surcharge Act 1982 and to 1 per cent in Finance Act 1983. Abolition from 6 August is worth further £465 million to private sector employers in 1984-85 and £850 million in a full year.

(ii) Even taking account of NIC increases since 1978-79, the overall effect of NIC and NIS changes is worth about £2.1 billion to private sector employers in a full year.

(iii) Overall NIC/NIS rate on contracted-in employers increased from  $8\frac{1}{2}$  per cent to  $13\frac{1}{2}$  per cent under previous Government. Now down to 10.45 per cent. Contracted-out rate down from 9 per cent to 6.35 per cent.

(iv) Beneficial economic effects from cost reductions. Reduces cost of employing labour.

(v) Abolition of NIS has widespread support, including CBI, ABCC, AIB, NFSE (and the Labour Party).

Defensive

(i) Change necessitates printing and implementation of complex new NI tables. Implementation on [6 August] allows employers time to make preparations. Furthermore NIS not covered by Provisional Collection of Taxes Act so cut cannot be implemented until legislation enacted.

(ii) Local authority direct labour organisations will pay NIS at 1 per cent for whole of 1984-85 while their private sector competitors will pay nothing from August. This competitive disadvantage is only temporary. Local authorities can take account of this disadvantage in judging the acceptability of tenders.



History

(ii) Took effect from April 1977 at rate of 2 per cent. Rate increased to  $3\frac{1}{2}$  per cent from October 1978. Finance Act 1982 reduced rate to 2 per cent from 2 August 1982 to 5 April 1983 (equivalent to average rate of  $2\frac{1}{2}$  per cent for 1982-83) and  $2\frac{1}{2}$  per cent subsequently. National Insurance Surcharge Act 1982 reduced rate to  $1\frac{1}{2}$  per cent from 6 April 1983. It also reduced the surcharge for 1982-83 by about  $\frac{1}{2}$  per cent (there was a reduction of 3 per cent in an employer's liability to NIC, including employee's NIC and NIS for 1982-83). Finance Act 1983 reduced rate to 1 per cent from 1 August 1983.

(iii) Presentational pitfalls

(a) May be criticised for not abolishing NIS earlier. Two points can be made in reply.

(i) Labour introduced NIS and, with the support of their Liberal allies, increased the rate in October 1978 to  $3\frac{1}{2}$  per cent.

(ii) Earlier cuts in rate were all that could be afforded within Government's responsible economic strategy.

(b) May be criticised for denying benefit of abolition to the public sector. Cash limits and EFLs will be reduced. Local authorities will continue paying NIS until end of 1984-85 because of difficulty of adjusting RSG to match NIC benefits in 1984-85. Public expenditure reduced by £170 million in 1984-85 and £485 million in a full year.

Benefit is being denied to the public sector because their needs were taken into account in fixing cash limits, EFLs and RSG. The treatment proposed will leave them in the same position as was originally intended.



VAT POSTPONED ACCOUNTING SYSTEM

PAS for VAT on imports withdrawn from 1 October 1984. Under the new arrangements importers will be required to pay VAT due at importation in the same way as customs duties.

Positive

- (i) By bringing forward the date when VAT due on imports by an average  $1\frac{1}{2}$  months, there is a once-for-all PSBR gain in 1984-85 of some £1,200 million (and financing gain of £180 million a year) to go towards financing reductions<sup>in</sup> in Company tax.
- (ii) Removes <sup>any</sup> the financial advantage which current VAT accounting arrangements give to imports over home-produced goods; and follows representations from sectors of British manufacturing industry about discriminatory effect of PAS.
- (iii) Brings us into line with our major EC competitors France, Germany and Italy.

Defensive

- (i) Financing burden on commerce and industry and increased compliance costs for importers, but needs to be seen in context of Budget which gives substantial boost to industry.
- (ii) Additional 120 Customs Staff needed but on-going financing gain of £180 million a year means cost of collection will be only 1.3p in the £.

Presentational Pitfalls

UK has previously supported Commission attempts to harmonise import procedures on basis of PAS, but these efforts were getting nowhere.



CORPORATION TAX

CT Rate

The Chancellor has announced the following corporation tax rates in his 1984 Budget:

for the financial year 1983	50%
" 1984	45%
" 1985	40%
" 1986	35%

i. MAIN THEMES

a. Investment, growth, etc

2. On its own reduction of CT rates will certainly stimulate investment and lead to growth. The immediate effect will be an increase in post-tax company profitability which could raise potential output in the longer term, even allowing for a considerable amount of the initial gain to be passed on. Supply side effects particularly in 1990s should offset declining yield from reductions in capital allowances, so allowing maintenance of low CT rate.

3. The effect on inward investment will be by and large favourable - a 35% CT rate is low internationally. By contrast, outward investment will look more unattractive, as multinational companies will be less able to claim full credit relief for foreign tax, and to offset the advance corporation tax they pay on dividends.

b. Inflation

4. Rate cuts reinforce favourable climate for corporate sector - profits and liquidity up, inflation and interest rates down/and reflect Government policy to continue through the MTFs to encourage these trends.

/ -



c. Distortions, including sectoral effects

5. Reduced CT rate will help to eliminate such distortions as exist eg the existing preference in the UK tax regime for debt finance rather than equity finance or through retained profits.

6. Reduction of the CT rates marks significant (and growing) switch in the balance of taxation in favour of companies. All sectors will gain from the reduction in CT rates, except the unincorporated. The tax-exhausted cannot gain because they do not pay tax. The financial sector will gain most; small companies (see separate brief) will gain proportionately less as their rate cannot fall by more than 8 percentage points. [Sectoral effects table: Mr Greenslade.]

d. Capital/labour

6.a. Due to the more even-handed pattern of tax incentives affecting different kinds of assets, there should be an improvement in the quality of investment and capital stock, raising both capital and labour productivity, though this effect should probably be more ascribed to the capital allowance changes rather than the CT rate changes. Investment in commercial buildings will benefit directly from the CT rate cut,

e. Simplification

(40%)  
7. Elimination of the special/corporation tax rate for building societies etc from Budget 1985 is a minor simplification. If they are small, they can still benefit from the preferential small companies rate of 30%.

f. Liquidity and cash flow

to both.

8. Effect of CT rate reductions is favourable/ [Table from Mr Greenslade]



g. Existing cases/transitional measures, etc

Transition favourable - as rate cuts precede clawback of allowances.

✓ Announcement of corporation tax rate for 3 years ahead as well as for the year just past will enable business to plan ahead with certainty.

ii. PAST HISTORY

9. 1965 corporation tax introduced by Labour Government at uniform rates on all profits, whether distributed or not ("classical" system). In addition shareholder liable to income tax on the dividends he received.

/since then. 10. 1972 Conservative Government introduced "imputation system with effect from April 1973 to avoid double taxation of distributed profits. Present system has remained unchanged/ Company pays corporation tax at 52% on all taxable profits whether distributed or undistributed. Company distributing profits in the form of dividends etc pays advance corporation tax (ACT) to Inland Revenue. This is set against company's corporation tax bill at a later date. Rate has remained unchanged at 52% since introduction of imputation system.

11. 1982 Conservative Government (Sir Geoffrey Howe) introduced corporation tax Green Paper responding to comments on present corporation tax and to suggestions for change. Overwhelming response to Green Paper was plea for stability of structure, which Chancellor accepted in 1983 Budget Speech.

(11a. History of special CT rate for building societies - see Annex.)

iii. PRESENTATIONAL PITFALLS

12. Points to be avoided or covered by defensive briefing, are as follows:



a. How soon does the corporation tax rate start to rise after financial year 1986 on revenue neutral assumption? On present figuring this is before 1990, making corporation tax reform transitory. If corporation tax rate to be held at 35%, increasing drain on Government's resources in 1990s, just at a time when revenue from North Sea is running out. What is the long term outlook for corporation tax rate?

b. Effect on outward investment. This is difficult to assess but there will be increasing pressure from powerful outward investment lobby to the effect that by reducing corporation tax rate in UK ability of multinationals to offset foreign tax/is reduced and investment overseas further disadvantaged. This will lead to pressure for further softening of the UK double tax regime, possibly leading to demands for 1965 style "overspill" relief.

c. Similar pressure may come from UK tax treaty partners tempted to follow us downwards who may put pressure on us in international tax treaty negotiations. These effects will take time to work through but defensive briefing certainly required.

d. No help to unincorporated businesses which do not pay CT.

e. Overwhelming sectoral advantages to financial sector generally and North Sea. For North Sea see separate brief. Possible criticism of reductions as bonus to financial and services sector, already doing rather well. Need to present countervailing arguments of package eliminating distortions and allowing resources to be allocated more efficiently - if that means financial and services sector, so be it.

f. Government bashing building societies by eliminating their special preference.

by means of credit relief



**CAPITAL ALLOWANCES**

1. The Chancellor has announced in his Budget Speech that first year capital allowances are to be reduced as follows in line with the CT changes:

Year	First year CAs for plant, machinery and vehicles	First year CAs for industrial buildings	Yield
84-85	75%	50%	
85-86	50%	25%	
86-87	25% wda	4% wda	(figures from Mr Pascoe)

2. The position as regards the secondary capital allowances is as follows: [Inland Revenue submission to Ministers by end of week, covering eg:

- Assured tenancy allowance
- Films
- Hotels
- Agricultural buildings
- Small workshops
- Enterprise zones
- Etc]

3. Special arrangements to be introduced for certain assets with very short lives.

3a. Entitlement to writing down allowances in case of machinery and plant to be altered so that start to run when expenditure incurred and not when asset brought into use.



1. MAIN THEMES

a. Investment, growth etc

4. Aim of capital allowance reductions is broadly to remove incentive element to allow more efficient allocation of resources in line with market. Changes have to be seen in association with corporation tax rate reductions (see main brief ). Wasteful investment will be reduced and quality of investment improved. On average higher pre-tax yield will be required to achieve given after-tax yield on new investment, and projects with low pre-tax yield will not go ahead. There will still be tax subsidy for most investment that gets it now. Projects not at present subsidised, like commercial buildings, will show better post-tax yield because of CT cuts.

5. Due to forestalling changes will accentuate forecast rise in investment in the next year or two, particularly in manufacturing where investment dominated by plant and machinery. In longer-term investment may be discouraged and leasing finance will become more expensive.

b. Inflation

6. 100% first year allowance has been seen as proxy for inflation accounting in this aspect of tax system on expenditure tax lines. Government has moved away from this to eliminate subsidy element. Changes do not precisely equate to economic depreciation (impossibly complicated in practice even with published asset lives), but 25% writing down allowance is a generous average figure based on historic costs.

c. Distortion, sectoral effects, etc

7. Prime aim of changes is to reduce distortions in corporate tax system due to over-generous capital allowances. Will undoubtedly hit those who have relied excessively on such allowances in past, eg manufacturing



with heavy investment in plant and machinery. They will lose, but stress [more than] compensating corporation tax rate reductions to improve resource allocation and increase efficiency.

8. Sectoral effects broadly as follows:

[Table from Mr Pascoe/Mr Greenslade]

9. Main losers from capital allowance changes are therefore manufacturing . . . . main gainers North Sea (see separate brief) . . . .

10. European Commission will approve reduction of subsidy element in capital allowances and move towards commercial depreciation.

d. Capital/labour

11. Changes should assist employment by reducing discrimination in favour of capital investment.

e. Simplification

12. Once stage 3 of package reached, there will be simpler system of capital allowances with - except for certain short-lived assets - only two main rates of writing down allowance:

- 25% for plant, machinery
- 4% for industrial and other buildings.

13. Commercial buildings will continue to get no allowance, largely on grounds of cost.



f. Liquidity, cash flow

14. There will be some adverse effect on liquidity and cash flow [Mr Greenslade/Mr Pascoe to insert table].

g. Special cases, transitional measures, etc

15. Main special cases are as follows:

Nissan - Example of adverse effects of package on inward investment in heavy capital project.

[Awaiting decision by Chancellor but NB that in early years Nissan gains by having some allowance at 75% but proceeds taxed at lower CT rates.]

Cabling - Announcement shortly after Budget Day that ducting and associated installation costs will qualify as plant and machinery, which should reassure industry. But will have to accept reduction of plant and machinery allowance in line with general arrangements.

? Films - [Expenditure on British films to be entitled to 100% capital allowances beyond 1987.]

Shipping - [No special treatment]

Scientific research allowance - currently 100%.

Any other cases?

ii. HISTORY OF CAPITAL ALLOWANCES [Mr Elmer to prepare history, concentrating on subsidy element and referring to investment grants experience from his recent history.]

iii. PRESENTATIONAL PITFALLS

16. No allowance for commercial buildings - undoubtedly distorting not to give allowance for commercial buildings, but main objection remains as before one of cost, not of principle.



17. Leasing Proposals will undoubtedly affect leasing, particularly when stage 3 (writing down allowances of 25% on plant and machinery only) is reached. Stress that initially leasing may be slightly advantaged (corporation tax reductions outweigh capital allowance reductions), but have to accept that as package begins to bite cost of finance leasing will go up, and leasing industry tend to contract.

18. Post-Budget 1984 contracts These will be subject to regime operating when expenditure incurred. Stress however that pre-Budget 1984 contracts will be protected - ie qualify for existing 100%/75% regime - so long as expenditure is incurred by 31 March 1987.

19. Nissan [Line to be settled]

20. "Stags heads" Possibly redefinition of machinery and plant under consideration, but not to be revealed. But reduction of capital allowances will reduce Exchequer subsidy for decor items.

21. [Any banana skins on secondary allowances?]

- scientific research allowance
- agricultural buildings

22. Mining capital allowances Previous Chancellor announced these would be reviewed. When is this going to happen and what is the result. Possible links with scientific research allowance. See North Sea brief.



## ABOLITION OF STOCK RELIEF

Factual

Stock relief to be abolished for periods of account commencing on or after Budget Day. Transitional relief applies for periods which end on or include Budget Day.

Key Points

- (a) (i) change should not be seen in isolation overall effect of CT rate reductions/ NIS abolition - which abolition of stock relief helps to finance - will be to industry's benefit.
  - (ii) but some losers from abolition of relief - mainly in manufacturing and distribution. Nevertheless industry will benefit from removal of distortion caused by stock relief - see (c).
  - (iii) abolition of stock relief may reduce attractions of UK to some inward investors (because many other countries have some form of stock relief).
- (b) although there are arguments of principle for a stock relief of some sort, the relief was introduced when levels of inflation were abnormally high - removing it now contributes to continuing fight against inflation.
- (c) abolishing stock relief helps cut back on major distortion of present over-generous treatment of debt-financed investment in stock



(exploited by some companies in distribution). Arguably some new distortions created but these are small while inflation is low.

(d) minimal effect on capital/labour balance

(e) abolition of stock relief a useful simplification of the tax system.

(f) (i) overall effect on liquidity of abolition of stock relief could be adverse initially - but companies likely to respond by reducing stocks; however

(ii) to the extent that stock relief has encouraged debt-financed stockholding, abolition could improve liquidity.

(g) transitional provisions for abolition are conceptually simple and legislation will not be complex.

#### History

(a) Relief for increase in stock values introduced in Autumn 1974 Budget in response to ~~severe~~ liquidity pressures on companies caused by high inflation. Scheme continued in much the same form as before until

(b) recession in 1979-80 led to heavy destocking which precipitated temporary reform of scheme (FA 1980)



to allow clawback changes to be deferred, followed by major changes (FA 1981) relating the relief directly to price changes and eliminating clawback for continuing businesses. As in 1974, inflation was high and liquidity poor when these reforms were announced.

#### Presentational Pitfalls

- (a) Steer clear of link between stock relief and current cost accounting (CCA). For accountancy profession to decide how profits should be adjusted to reflect inflation, for reporting purposes. Requirements of the tax system are not the same and Ministers have never said they would accept CCA for tax purposes.
  
- (b) Stock relief and indexation of CGT conceptually similar - both exclude inflationary gains from taxation. But CGT indexation introduced as "fiscal justice" measure - no injustice to remove stock relief now, in very different circumstances from those in which it was introduced, when yield from abolition is being recycled to the corporate sector. Care needed to ensure line of argument left open for the future, that abolition of CGT indexation would be consistent with abolition of stock relief.



## CORPORATION TAX : SMALL COMPANIES

Factual

Present CT rate for small companies' income is 38 per cent - applies where profits £100,000 or less, with marginal relief for profits between £100,000 and £500,000. Proposed to reduce rate to 30 per cent for Financial Years 1983, 1984, 1985 and 1986 - profits limits to be left unchanged.

Key Points

- (a) (i) substantial initial gain for small companies as large rate reduction bites before capital allowances/ stock relief changes. Changes boost growth for regular CT payers (about  $\frac{1}{5}$  of sector) and should help intermittent payers ( $\frac{1}{3}$  of sector). No adverse effect initially on non-taxpaying companies ( $\frac{1}{2}$  of sector)
- (ii) has to be conceded that some small companies may lose by 1987-88 because of curtailment of reliefs. But low rate will help director-controlled companies wishing to retain profits rather than pay out as remuneration.
- (b) effects of inflation on small company profits perhaps less significant than for large companies because of heavy reliance on bank borrowing. So lack of inflation adjustments in tax system might not be such a serious problem.



- (c) changes eliminate distortion in tax treatments of debt and equity finance.
- (d) overall package will generally help labour intensive businesses but may well have adverse effect on capital-intensive businesses.
- (e) changes do not affect structure of company taxation so little effect on simplification
- (f) liquidity generally helped in the short-term by rate cut; in longer term, position could worsen for heavy investors in stocks or capital assets.
- (g) transitional effects favourable - rate cut precedes clawback of allowances.

#### History

- (a) No special relief for small companies when CT introduced in 1965.
- (b) When imputation system introduced, lower rate fixed for small companies' income because they retain a high proportion of their profits and so "benefit less from the reduction in the rate of tax on distributed profits than they would lose on paying the higher rate of tax on their retentions." (1972 White Paper (Cmnd 4955) para 26). Rate first fixed at 42 per cent (compare with 40 per cent rule under previous "classical system").



- (c) More recently changes to the small companies' rate and profits limits have been made with the aim of giving a general boost to small firms.

#### Presentational Pitfalls

- (a) change should not be presented as incentive to incorporate - in view of recent pressure for disincorporation reliefs.
- (b) in view of previous "108 measures for small businesses" should not be conceded that changes damage small companies - changes can be good for small firms generally (in terms of removing distortions, etc) without necessarily giving a cash hand-out to each and every company.
- (c) should not be suggested that further reductions in small companies' CT will follow. 30 per cent is the lowest possible rate without structural change.



THE SELF EMPLOYED

£m			£m		
Will <u>gain</u> directly from:	1984-85	1985-86	Will <u>lose</u> directly from:	1984-85	1985-86
<u>NIS abolition</u> (if they have employees)	15-45	80-95	Abolition of <u>stock relief</u> and reduction in <u>capital allowances</u>		40
<u>Mortgage interest relief</u> for self employed in tied accommodation buying their own homes)	6	8	VAT extended to <u>alterations to buildings</u> (mostly affects builders, etc)	?	?
	-----	-----		-----	-----
	20-50	90-100		?	?

May also be said to gain from:

Cutting top rates of CTT

Cutting stamp duty rate on land and buildings

VAT increase in registration threshold

May also be said to lose from:

PAS (if an importer of materials or finished goods)

NIC increases in Class 4 contributions (although broadly equivalent to increases for employers and employees)

Generally, the self-employed may object that they do not benefit from the CT rate offset in the business package and, if higher-rate taxpayers, may contrast bare indexation for their accrued income, with the abolition of IIS.



PRESENTATION BRIEFING

VAT REGISTRATION THRESHOLD

Registration Threshold (below which small traders are not obliged to register) raised from £18,000 to £18,500 taxable turnover a year.

Positive

Increase helpful to small businesses. Provides about 28,000 traders with opportunity to deregister if they wish. By broadly maintaining the real value of the threshold at its 1973 level, keeps new businesses out of the VAT net for as long as possible, and helps those businesses which would otherwise be forced into the register simply because of price increases.

Defensive

Large increase in the threshold not possible because of EC Sixth VAT Directive. The most favourable interpretation of the Directive only allows for increases in line with inflation since introduction of the tax in 1973.

Past history

At the inception of the tax, traders with a taxable turnover of less than £5,000 were exempted from registration. Since then, the exemption limit has been raised in line with inflation as follows:

1 October 1977 to £ 7,500  
12 April 1978 to £10,000  
27 March 1980 to £13,500  
11 March 1981 to £15,000  
10 March 1982 to £17,000  
16 March 1983 to £18,000

This year will be the Conservative Government's fifth successive annual increase, during which the limit has moved from £10,000 to £18,000.



Presentation Pitfalls

Future commitment about maintaining real value of limit risky because Commission do not accept our interpretation of EC Sixth Directive and could take infraction proceedings.



## NORTH SEA

## KEY THEMES

1. Need to keep up momentum of developmentPositive

- a. Last year's measures (phasing out APRT, PRT appraisal relief and new reliefs for future fields - costing £m800 over 4 years) provided renewed momentum: 10. oil, gas and pipeline developments approved in 1983; record 128 exploratio: and appraisal wells.
- b. This year's Budget gives further small easement to oil companies' cash-flow (£m280 over 5 years). This will help ensure companies not constrained on cash for development despite uncertainties on oil price.
- c. Future developments not significantly affected by reduction of capital allowances: our figures on likely future projects suggest if they are not yet paying CT profitability increases slightly; there may be a small reduction if they are paying CT but in this case the start from a higher level of profit anyway.
- d. Government has promised to introduce new relief for incrementals backdated to this year's Budget. Form to be discussed with the industry.

Defensive

- a. Front end relief is reduced (so increasing companies' maximum cash exposure on new projects) - but fully preserved for PRT and the switch from a "brought into use" basis to an "incurred" basis for writing down allowances will mean that reduction of front end loading for CT is limited.
- b. Future fields on an immediate CT basis and incremental projec will suffer - but former effect is small and from a high basic; promise of PRT relief for latter.



- c. Southern Basin fields not to benefit from last year's reliefs for new fields - but detailed analysis of figures provided by companies showed there was no need.
  - d. Yet another change in North Sea regime - but this is a corollary of general changes to CT which has been unchanged since 1972.
2. Need to achieve fair share of revenues for nation

Positive

- a. Action to prevent unjustified losses of tax through farmouts  
Last year pace of farmouts increased (in particular BP Forties sale). Wrong for tax to encourage shifts of ownership where no national benefit follows. Raises £m35 - £m40 a year.
- b. Provision which erodes PRT by repaying corresponding ACT is being repealed.
- c. Provisions to ensure adequate supply of information to value crude oil for PRT (need to get information about all disposals and acquisitions by a group so that North Sea producer cannot pass crude to affiliate and prevent sale price being known).
- d. Defects in provisions relating to taxation of non-residents being remedied.

Defensive

- a. Large revenues given away to existing fields without guarantee of reinvestment in UK - but overall only a modest cash flow gain. And lower marginal rate for existing fields reduces incentives to wasteful expenditure and eases any risk there might be of premature abandonment of fields.
- b. Farmout package only stops small proportion of leakages - but important not to stop desirable re-organisations. Where reliefs for future exploration or development are accelerated by farmouts the tax cost is associated with desirable activity and has not been stopped.



- c. "Stranding" of ACT not itself a sufficient reason to repay it: and widening of tax base makes it easier to achieve set-off.

## PAST HISTORY

- 3.a. Ever since North Sea got underway in early 1970s, 100% FYA's have existed. Strong emphasis in 1975 on need for front end loaded reliefs because of heavy front end costs of North Sea development.
- b. PRT initially at 45% increased in stages to 75% as a result of 1979-80 oil price hike (which has fallen away significantly in dollars but [not much] in sterling). Acceleration of take introduced 1980 first through SPD, then replaced by APRT. APRT phased out in 1983 Budget (finishes 1986).
- c. 1982/83 full analysis of future oil fields with the industry showed new fields were less profitable extra reliefs - hence double PRT oil allowance and abolition of royalties for them. Sir Geoffrey Howe promised to look at Southern Basin gas fields and extend reliefs to them if needed; similar analysis done this year, but they look very profitable without changes (because of low costs in shallow water and ability to use extensive existing infrastructure. Similar analysis of the effect on this year's CT package showed future oil fields (and Southern Basin fields) still viable. Incremental projects hitherto have not shown up as justifying help and problems of defining a relief were identified; this year's work shows assistance will now be needed but further work is needed in consultation with the industry on the form.
- d. 1975. A ring fence was drawn around the North Sea to stop losses on non-North Sea activities reducing tax on North Sea profits. Recent farmouts have shown there are leakages in the ring fence.
- i. non North Sea losses can be set against capital gains (sometimes substantial) arising from farmouts; and
  - ii. ACT on distributions which have nothing to do with North Sea profits are set off against ring fence CT.



- e. Because PRT was made the principal, and earlier, tax charge and so deductible for CT, to the extent that the deduction made it impossible to set off ACT, ACT was made repayable in 1975. But there is no compelling reason why ACT should be repaid in these circumstances, and a number of reasons why in current circumstances the provision is no longer appropriate.

#### PRESENTATIONAL PITFALLS TO BE AVOIDED

- 4.a. Important to present package in terms of modest cash flow gain to the industry taking all measures together and to avoid drawing unnecessary attention to the larger gains to existing fields arising from the CT package in isolation.
- b. The general arguments for the CT package should not be used in the North Sea context -

- i. PRT means there is no distortion in favour of investment in machinery and plant.
- ii. The benefits from reduced marginal rates are double-edged.

It helps on wasteful expenditure and risks of premature abandonment but reduces the sensitivity of the system to changed oil prices, and arguably gives more than is required to mature existing fields paying tax at the marginal rate on their production.

- iii. Simplicity is not important for the North Sea fiscal regime.
- iv. There is little scope for shifting the balance between capital and labour.

Rather the package should be justified by non-North Sea considerations but Ministers have checked against North Sea objectives and the overall package (taking account of other North Sea measures) seems reasonable in these terms too.



- c. Not all farmout tax losses will be stopped. It will be desirable if possible to avoid giving the cost of farmouts before or after the change as this is large compared with the yield of the package.
- d. There will be some gainers and some losers within the North Sea from the package. We cannot be certain but Marathon and Texaco seem likely losers from the CT package in isolation, Chevron, ICI, Murphy and Burmah from the ACT change (even after net gains from CT package). Some small companies may feel their chances to grow by farmins are reduced (although there will still be many tax advantages for them).

#### KEY GROUPS TO BE APPROACHED

- 5.a. UKOOA is the key trade association. Last year the MST(R) wrote to UKOOA on Budget Day. We suggest that the FST should write to UKOOA to tell them about the North Sea package, in particular about the exercise on incrementals and the outcome of the exercise on Southern Basin fields (where there is no non-North Sea equivalent), and possibly to assure them more generally that the effect of the CT changes on development have been carefully considered and that (subject to the position of incrementals to be reviewed) they are not thought to be adverse, and to urge them to use cash flow easement to promote the development.
- b. The Inland Revenue has previously handled consultations with the other two associations - Brindex and UKOITC. It might be tactically desirable for us to send a brief letter covering the relevant Budget press releases to them, but again we need to keep in step with non-oil practice.
- c. Some individual oil companies are likely to ask to see Ministers or officials on particular issues. These can be handled ad hoc.



BRIEFING FOR MINISTERIAL COLLEAGUES, BACKBENCHERS AND THE PRESS

- 6.a. Ministerial colleagues. We normally send Department of Energy the relevant Budget briefs. This has proved an effective and economic method of briefing.
- b. Backbenchers. Tim Eggar, Trevor Skeet, David Crouch, Sir William Clark are the ones who have expressed most interest in oil matters, but we have not hitherto supplied them with material.
- c. Journalists. Last year the MST arranged a post Budget off the record press briefing with energy correspondents.. We would doubt whether a special energy briefing would justify Ministerial time at the Budget, but officials could if Ministers wished, provide briefing for a few key correspondents.



BUDGET: SECRET

*Paul*

E 3

\$ (84) 771

FROM: ADAM RIDLEY  
22 February 1984

MR BATTISHILL

cc Mr Kerr —  
Mr Lord  
Mr Portillo

BUDGET SPEECH: FIRST DRAFT OF 17 FEBRUARY: SECTIONS A TO E

...  
I attach some comments and suggested drafting changes for Sections A to E, in the form of a photocopy of the original with ms inscriptions which I trust are not too illegible.

2. May I also add a few general thoughts:

- (1) Section B 4, to some extent, can and should be much shorter and clearer. This is a "turn-off" bit of the speech for the ordinary man. It needs to be got over with as quickly as possible. I have suggested numerous deletions.
- (2) The text is very free of needless "I" "my" and other egotistical possessives of the kind which so marred Mr Healey's many statements and Budget speeches! But there are still one or two left which I would urge should be purged.
- (3) The treatment of the recovery in B fails to do justice to the early, strong and continuing upturn in total investment in 1981, and should surely do so. People will otherwise see the upturn as consumption-led alone. One might also get in somewhere the thought that public investment, properly defined as in T.1.13 of the PEWP, has been neutralised in real terms since '79.
- (4) I would be tempted to plant a bigger and more obvious seed of the tax reform idea in A 7. It both creates the right atmosphere and will stimulate curiosity.
- (5) It is, I know, unreasonable to hammer the wretched draftsmen too hard at this stage about wording when it is an act of heroism to produce any coherent draft at all at such speed! But the eye is struck by the high cliché/tautology/redundancy ratio in some sections; and by needless repetition of passages which have occurred again and again in such speeches in nearly identical form. A good example of the latter is the passage about fellow finance ministers in B 2.

*M*



# BUDGET SECRET

## BLOCK A: INTRODUCTION

This Budget will set the Government's economic course for this Parliament. It is founded on the policies which we have consistently followed since 1979.

2. ~~The~~ hallmark of this Government is consistency of purpose. To defeat inflation. To improve economic performance. To lay the only sound foundations for future prosperity, more jobs and lower taxation.

3. The <sup>fruits</sup> results of the medium term financial strategy introduced in 1980 by my Rt Hon and Learned Friend the Foreign Secretary, can be seen in three years of recovery ~~and~~ rising living standards and inflation at the lowest level for 16 years. Employment is rising and hopefully we have reached the turning point for unemployment.

ENGL 4/14

4. The success of our policies is not in question. The facts speak for themselves. They are a tribute to the wise stewardship and foresight of the five Budgets presented by my predecessor from this Despatch Box.

See gen'l  
Comments on Egalism in Budget Speeches!

This

5. My Budget ~~is~~ has two themes: first, to continue our policies ~~which will achieve~~ <sup>for</sup> growth through lower inflation ~~and~~ growth; secondly, to reform taxation. The aim is to achieve a simpler tax system for all.

Either drop last sentence, or last phrase of previous sentence.

Consistency needed - better to avoid - by

# BUDGET SECRET

This is perhaps better phrasing, i.e.

"... two themes: <sup>our</sup> policies for lower inflation & higher output; and tax reform."



# BUDGET-SECRET

Ensure  
new to  
Delete  
Include directly in  
Prop!

6. ~~As is~~ traditional I shall begin by reviewing the economic background to the Budget. I shall then deal with the medium term financial strategy; with monetary policy and the monetary targets for next year; and with public spending. This will bring me to the vital issue of public borrowing and to the appropriate PSBR for the coming year. Finally I shall deal with taxation, and the changes I propose this year. As I have indicated I shall devote some time to matters of tax reform.

7. I can tell the House now that there will be no overall tax increases this year. But I shall announce significant tax reductions for next year. This is a Budget for two years, not one.

only?

BUDGET



# BUDGET - SECRET

This can & should be trimmed harder

## BLOCK B: WORLD BACKGROUND

~~The outlook for the world recovery is more favourable now than~~  
~~for some time.~~ (Inflation in the major industrial countries) has <sup>is</sup>  
~~fallen to~~ <sup>or</sup> its lowest level for more than a decade ~~with consumer~~  
~~prices rising by about [4.1] per cent in the past year.~~ Output in  
~~the same countries~~ has risen by about [3.1] per cent in the past  
year after three years of ~~negligible~~ <sup>negligible</sup> growth. Our overseas  
markets are growing at an annual rate of about [5] per cent.  
And the world background is altogether more promising than it  
was three years ago when the UK economy first began to lead  
the industrialised world out of the depths of recession.

2. It is no accident that <sup>this</sup> recovery has followed ~~the~~  
~~emergence~~ of widespread international <sup>agreement</sup> ~~consensus~~ on the critical  
need to defeat inflation. ~~This consensus is now firmly~~  
~~established among the members of the international~~  
~~community, and is the understanding of the policies required to~~  
achieve that. ~~I was particularly encouraged at the way Finance~~  
Ministers from both developed and developing countries readily  
agreed on the crucial importance of control over monetary and  
- ~~which they certainly would not have done a few years back~~  
fiscal policies when the world economy was discussed ~~at last~~  
year's annual meeting of the IMF.

3. (So, what are the prospects?) ~~It is no likely that~~ (output in  
<sup>or Japan</sup> the United States) should continue to grow strongly this year.  
~~And the recovery in the rest of the world is becoming more~~  
~~steadily based, with activity rising in Japan, and signs that the~~

?

Concerns in  
no word for a  
broadcast speech

This is  
(a) patronising in the  
(b) what G.H. needs to  
say every year  
but repeated abt!

Delete. We're  
already saying  
that they are  
favourable.

This might go  
better at the back  
of the document  
{}



# BUDGET-SECRET

And the long awaited upturn appears at last to be getting underway in Europe.

Ugla as opposed to in real?

4. Of course, there are real risks and uncertainties ~~in the present situation~~. The continuing high level of ~~international~~ interest rates ~~poses a potential~~ threat to ~~such needed~~ investment, ~~which~~ <sup>at</sup> makes the solution of debt problems more difficult. And there is wide acknowledgement of the concern generated by the <sup>high</sup> continuing, and growing ~~high~~ level of <sup>the</sup> US budget deficits. Large imbalances in current accounts may increase the risk of ~~unstable~~ <sup>vulnerable</sup> exchange rates, ~~and they also~~ bring risks of greater protection ~~is~~

5. ~~Uncertainties remain too~~ in uncertain in the oil markets, though perhaps ~~less~~ ~~than~~ at sometimes in the past. The possibility of a sharp fall in <sup>prices</sup> oil has been reduced by the prospect of ~~steady~~ recovery, ~~in the world economy~~. But it has not disappeared. ~~and a lower oil price~~ (though ~~almost certainly~~ <sup>it would</sup> help ~~the~~ world activity in the long term, <sup>in</sup> would ~~be~~ <sup>(if adjustment)</sup> pose short-term problems ~~with countries adjusting to it~~

6. In managing our own affairs <sup>we must always</sup> ~~it is~~ prudent to recognise ~~in such~~ ~~the~~ ~~risks~~ to world recovery and to give them due weight in ~~forming~~ domestic policies. ~~But the risks should not be~~ ~~suggested~~ ~~by~~ ~~the~~ world economy, <sup>is</sup> now ~~more~~ ~~likely~~ to achieve ~~continued~~ growth with lower inflation than for some years ~~past~~ and to that extent our own prospects are ~~strengthened~~.

Totally vacuum  
at this repetition

However such risks  
are less than for some time

However, then when ~~the~~ could ~~imply~~ ~~is~~ - in the future?



# BUDGET-SECRET

## BLOCK C: DOMESTIC ECONOMY

*What is the*

~~The world recovery has been more than matched by the~~  
progress of our own economy.

*Cliche*

~~At the end of the seventies, we were poorly equipped to withstand economic pressures - weakened by many years of high inflation, excessive ~~pay~~ increases, and poor productivity performance. We had to tackle inflation and grossly excessive~~

*This para could be made interesting by a cumulative*  
1981 - - -  
1982 - - -  
1983 - - -

*instead of in*  
**FALSE**

~~public borrowing during the deepening world recession. Since 1980, inflation has ~~fallen~~ <sup>fallen</sup> ~~fallen~~ from a peak of more than 20 per cent, interest rates have fallen ~~while~~ <sup>fallen</sup>~~

~~and domestic demand have recovered strongly~~ <sup>distorted by</sup> ~~since 1981~~  
*Total Investment turned up in 1982, has grown vigorously since then*  
*Employment started growing again in 1983, a year which*

3. ~~1983~~ saw a combination of low inflation and soundly-based growth. The increase in prices ~~was~~ <sup>at</sup>  $4\frac{1}{2}$  per cent was the lowest since 1967.

4. We have seen a welcome further improvement in productivity by the [third] quarter of 1983, for the whole economy, it was [about 10 per cent: - GDP(A)/ELF] above the level three years earlier. In manufacturing alone, output per man hour was up [16 per cent]. Of course, productivity improvements do in part reflect cyclical factors. But in manufacturing the underlying rate of growth of productivity now appears better than the 1 per cent a year recorded between 1973 and 1979.

*NOT THE LANGUAGE OF A BROADCAST SPEECH*

*This para sounds as if it will be a drawing to too long if it illustrates its present position*



5. Productivity gains, ~~combined with~~ a moderate level of pay settlements, <sup>together</sup> produced the smallest annual increase in unit wage costs in manufacturing since 1970 - around 4 per cent. But we cannot rest on our laurels. ~~Last year~~ <sup>Last year</sup> unit wage costs fell ~~last~~ year in the US and Germany.

(Japan?)

6. The slow growth of costs, ~~combined with~~ <sup>4</sup> lower inflation, has allowed a significant and welcome recovery in real levels of profitability. The CBI has put the net pre-tax real rate of return for non-North Sea companies at [6. <sup>1</sup>/<sub>2</sub> per cent] last year with a further estimated improvement to ~~7.2~~ <sup>7 1/2</sup> per cent] in 1984. ~~Profitability at these levels,~~ <sup>However,</sup> though the best since 1977 and 1978, <sup>such levels</sup> are still too low. ~~There needs to be still more improvement as the basis~~ for long run growth and employment.

There  
known  
Demand demands  
1/2 is normally  
what's needed  
here

~~As~~ <sup>better profits</sup> the background is one of lower inflation, lower costs and lower interest rates.

<sup>have been</sup> ~~This has produced~~ a better environment for industry and <sup>knowing</sup> ~~rising~~ business and consumer confidence. Not surprisingly, demand, output, profits and employment all rose during 1983. Lower inflation reduced consumers' needs to save and personal consumption rose by some [3 1/2 per cent] compared with 1982. ~~The rate of~~ investment increased again in the service industries and, although manufacturing investment fell back a little, fixed investment as a whole rose by [4 1/2] per cent last year, rather faster than consumption. Total domestic demand grew by an estimated [4 1/2] per cent.

Stem  
demand,  
+ total  
investment  
have both been  
rising here  
-81



# BUDGET-SECRET

9. These trends were reflected in our balance of payments. Last year UK exports rose by [1] per cent, in line with the slow growth of world trade. The most encouraging growth in export volumes occurred in the fourth quarter of 1983 and into 1984. Imports are estimated to have risen by about 5 per cent. This picture is consistent with our emerging from recession generally more quickly than our trading partners, with demand growing faster in the UK than ~~in~~ overseas ~~markets~~. For 1983 the balance of payments on current account is expected to have been in a surplus by about £[2] billion, a much better performance than was expected at the time of the November Industry Act Forecast.

10. Nominal GDP in 1983 grew by a bit over [9] per cent of which [3] per cent represented a (real) growth of output. This is a much healthier division between inflation and real growth than we saw in the 1970s. And it brought the average measure of GDP above its level in the cyclical peak year of 1979.

*Who?* ~~inflation continues to drop~~ there is still room for further improvement, ~~as~~ *of course*

*This is true at any time!*

11. ~~I am pleased to say that~~ *create more jobs* growth in output has started to ~~feed through into the labour market~~. The number of people in employment increased by 87,000 between May and September last year. The loss of jobs in manufacturing has slowed down sharply, while jobs in services ~~increased~~ *by much more - above* by nearly 200,000 in the first nine months of 1983. This is encouraging news for the unemployed and those who will be leaving school later this year.

BUDGET-SECRET



# BUDGET-SECRET

Our neighbours

12. ~~We~~ no longer regard ~~as~~ as the poor relation. Last year our growth was the fastest of the members of the European Community. ~~And~~ both the OECD and the European Commission have forecast ~~continued~~ <sup>we will continue</sup> ~~growth~~ <sup>do better than Europe</sup> ~~in~~ ~~Europe~~ this year, too.

13. Even the pessimists can no longer doubt the strength of our recovery. ~~Expect~~ <sup>should</sup> inflation to remain low, edging down to 4½ per cent by the end of the year. Although personal consumption, fuelled by rising incomes and low inflation ~~will~~ <sup>will</sup> continue to grow, the recovery is becoming more widely based. Investment encouraged by higher profitability is forecast to rise by [ ] in 1984. And as world trade grows, so there will be increasing opportunities for <sup>our</sup> exports, which could rise by about [5] per cent in real terms. Output is expected to rise again at a rate of 3 per cent in 1984 and only a little less rapidly in ~~the~~ the first half of 1985.

It's like...  
let them imply  
There will be no  
growth...  
Consequences of the...  
time horizon...  
higher will appreciate

Why oh why do we  
go on saying this? It  
has been traced than consumption  
for 40. If any demand  
component is to be added here, it  
is likely stocks or net exports  
which has to be summed to  
support this darkness for now.

BUDGET



# BUDGET-SECRET

## BLOCK D THE MTFS

This implies  
positive growth is  
instructive

Sustainable growth

Our ~~ultimate~~ objectives are ~~price stability~~, high <sup>ultimately, price stability</sup> employment and ~~sustainable~~ <sup>long-term & structural peak rate</sup> growth. Inflation has fallen, and is set to fall further. Output has been recovering steadily for two <sup>1/2</sup> years, and there are sound reasons for expecting this growth to continue. [It can no longer be doubted that] steady growth can be combined with falling inflation if the right policies are followed.

2. The MTFS remains the centrepiece of this Government's monetary and fiscal policy. In this first Budget of a new Parliament, therefore, it is appropriate to carry the MTFS forward to the end of the Parliament. That is what I have done in the MTFS published to-day in the FSBR - the Red Book. The policies described there cover the five years from 1984-85 to 1988-89. <sup>entirety of the MTFS is</sup> They indicate a continuing downward path for the monetary ranges over the next five years, <sup>and</sup> together with a <sup>consistent with</sup> ~~consistent~~ path for public borrowing. These take full account, as they must do, of important <sup>highlights</sup> ~~considerations~~ like ~~the pattern of~~ our North Sea oil revenues, and ~~the programme of~~ asset sales. But <sup>such</sup> ~~these~~ more technical <sup>issues</sup> ~~points~~ must not be allowed to obscure the key role played by the strategy itself in setting a ~~policy~~ framework for strengthening recovery, falling inflation and improving prospects for employment.

Reference unfused  
& printing.

Pages

There are  
a year many  
Redundant  
in this  
part. Shaker &  
Ciuro.

5. ~~There can be no disputing the importance of ensuring~~  
~~continuing growth in output with falling unemployment. The~~



MTFS is designed to create the conditions in which lasting improvements can be achieved. The precise figures set out in the MTFS are not ~~to be regarded~~ as a rigid framework, lacking flexibility. To regard it as such is to misunderstand its purpose, and to ignore ~~that~~ <sup>how it</sup> has been applied in practice. As in the past, ~~in the past~~ there may well need to be adjustments (to take account of changing economic circumstances.) But this is the strength of a medium term strategy that such changes can be made without jeopardising the consistent pursuit of the Government's objectives, in particular lower inflation.

Start

Some would question this? better omitted?

6. Of course, the Government alone cannot determine precisely what happens to inflation, or to the growth of output. But it can influence the growth of (total national income, or money GDP. How far <sup>it is</sup> growth in national income is then dissipated in rising prices and how far it comes in the form of rising output depends on the behaviour of employers and employees, on productivity, efficiency and attitudes to pay.

Government to suddenly start talking about ~~high~~ national income?

7. Within <sup>it</sup> the financial framework the MTFS provides the more (that) inflation comes down, the more room there will be for output and employment to grow. Interest rates play a role here: nominal rates fall with inflation and help cash flow, encouraging spending by both companies and households. Public spending programmes drawn up in cash terms go further with lower inflation. And, most important of all, with low inflation, slower growth in pay makes room more jobs.



# BUDGET-SECRET

8. The winning combination of falling inflation and rising output which we have seen in the last two years is no accident. It has come about as the result of responsible financial policies, consistently applied, and increasingly better understood throughout the country. At the heart of the MTFS is a recognition of the crucial importance of sound money, and proper monetary control. It is to monetary policy that I turn next.

BUDGET-SECRET



# BUDGET-SECRET

## BLOCK E: MONETARY POLICY

~~It will be clear to the House from what I have said about our medium term plans that monetary policy will continue to play a crucial role. I propose now to describe how I expect monetary policy to operate in the coming year.~~

W AFFRE '84  
it breaks the flow

2. A central theme of my predecessor - and of his predecessor too in his better years - was the need for monetary and financial discipline. ~~My Pt. Hon. and Learned Friend saw this as the indispensable condition for bringing down inflation and establishing the basis for economic recovery.~~

Now  
when

3. It remains no less important now that inflation has been substantially reduced and recovery is firmly under way. The Government's success to date would all too easily be thrown away if monetary conditions were to be relaxed. On the contrary, continuing downward pressure on the monetary aggregates will be required to achieve further reductions in inflation which in turn will help sustain the recovery.

4. ~~To judge the appropriate degree of monetary pressure is~~ <sup>clear to judge</sup> ~~more than to achieve~~ it. Monetary targets provide an important framework. But the assessment of monetary conditions remains an art rather than a science. It involves judgements on a variety of evidence, sometimes conflicting -including the monetary aggregates, the exchange rate and interest rates. And our ability to influence monetary

clear to judge  
than to achieve



# BUDGET - SECRET

conditions, particularly in the short run and with due regard for external factors, is ~~not~~ <sup>limited</sup> ~~unbalanced~~.

*policy could be negative*

*Why the (big) interest?*

5. Yet it is important to strike the right balance between excessive stringency which might halt the recovery, and undue laxity which would lead the economy to grow at an unsustainable pace and rekindle inflation.

*close as the way Ben deals with it*

6. Looking back over the period since the last Budget, I believe we have achieved ~~the right balance~~ <sup>the right balance (between stringency & laxity)</sup>. Monetary conditions in general have been consistent with our objectives. Inflation has turned out lower than even we - and certainly members opposite - anticipated, notwithstanding several unfavourable factors including the rebound of commodity prices. And we can look forward to making further progress. This has demonstrably not been achieved at the expense of the recovery; which has been faster than forecast at the time of last year's Budget.

*The concept of two words only "right balance"*

*fuller*

7. The House will find ~~the facts set out in greater~~ <sup>fuller</sup> detail in the Red Book. Monetary growth over the full year to mid-February, as reflected in the three target aggregates has been at or a little above the top of the target range. There was particularly rapid growth in the early months; but since the summer the growth of all three aggregates has come back within the target range. The growth of MO, about which I will have more to say in a moment, has been fairly steady.

8. So too has been the effective exchange rate. Interest rates have fallen; but in real terms, taking into account



# BUDGET-SECRET

expected inflation, they remain high by historical standards. Other evidence that monetary conditions have not been too lax includes some slowing down in recent months of the rate of increase in house prices.

9. ~~It is likely that~~ higher than expected PSBR this year has placed a heavier burden on funding. Nonetheless, net sales of debt to the public have broadly covered the PSBR. Consequently, the money supply has not been inflated by the demands of the public sector. Nor have the very substantial sales of gilts prevented long rates from moving down further. National Savings have again made a major contribution, and are likely to achieve this year's target of £3 billion.

interest

10. Lending to the private sector rose rapidly in 1983. This has given rise in some quarters to what I believe are exaggerated fears - either that the recovery is too dependent on borrowing or that it is causing an unwarranted loosening of monetary conditions.

11. There is nothing unusual about company borrowing rising at this stage in the cycle; and there seems little reason to think that <sup>only</sup> ~~the~~ lending to individuals - which has helped consumer spending <sup>resources without targets</sup> - cannot be sustained. Higher lending for house buying, reflecting the heavy inflows of funds to the building societies, has taken place without this causing an acceleration in house prices. And more generally, as I have said, the overall evidence is that monetary conditions have remained well under control.

Indeed NO!  
That's the problem, this!  
The real qn is whether bits together can be reconciled

with aggregate or no change?

BUDGET-SECRET into the mon. targets

continue para over



*we shall*

12. Nonetheless, it ~~would be imprudent not to watch the~~  
course of private sector borrowing carefully in the months  
ahead. If ~~there were to be an excessive build-up of liquidity~~  
and spending, that would obviously be cause for concern. But  
the ~~risks at present do not appear to be~~ great.

*Reserve are  
& largely  
idle*

*Bank of England in London*

*Finance moves in the markets*

13. One encouraging factor has been the ~~strength of~~  
~~issues~~ by UK companies. ~~These~~ *New ones* reached a record £2.8 billion in  
1983, more than ~~50~~ *higher much again as* percent higher than the previous record. If  
this continues - and the size of the Bank of England's new issue  
queue suggests that it may - it ~~should help mitigate the growth~~  
~~of~~ lending to companies, and help ~~companies by~~ strengthening  
their balance sheets.

14. I propose to introduce four measures in this year's Finance  
Bill to ~~assist~~ *further* the issue of corporate bonds. ~~The~~ *Two -* attractive tax  
arrangements for deep discount stock, and the reliefs for  
companies issuing Eurobonds in this country, have already been  
announced. In addition I propose to exempt all new corporate  
fixed interest securities from Capital Gains Tax and to extend  
the stamp duty exemption for such stock to certain convertible  
instruments. I shall come later to another important change  
affecting equity finance.

15. Of course the most important contribution the  
Government can make to the revival of the capital market is to  
maintain sound financial conditions. I have decided to make  
two important changes in the way that monetary policy is  
framed. First, for the coming year, there will be separate



# BUDGET-SECRET

9 targets for broad and narrow money. The range for broad money will apply principally to £M3. Secondly, the range for narrow money will apply principally to M0. There will no longer be a target for M1.

16. The reason why I have discarded M1 is that it is no longer a satisfactory measure of narrow money, that is, money held for transactions purposes. Because of the rapid growth of its interest-bearing component, M1 has taken on some of the characteristics of broad money. Falling somewhere between the two, it is becoming a less reliable guide to monetary conditions.

17. *It would be wrong to*  
~~I am not, however, willing to go back to the earlier period when we only targeted broad money.~~  
*alone*  
Broad money, and in particular £M3, provides an important measure of liquidity in the economy. But it needs to be supplemented by a measure of money more closely geared to spending.

18. M0 consists mainly of the notes and coins in the hands of the public. For the time being at least, that is the best *can* measure of narrow money we have; and recent experience suggests that it is moderately responsive to interest rate changes. It will therefore be the main target aggregate alongside £M3.

19. Separate ranges are needed for broad and narrow money because narrow money, and in particular M0, has over the years tended to grow considerably more slowly. This reflects the

# BUDGET-SECRET



impact of institutional changes, such as the growth of bank accounts, on the public's demand for cash.

20. For later years, the Red Book includes illustrative ranges showing a downward path for both money measures. While precise targets will be decided for those years nearer the time, it should be clear that the Government are determined to achieve a substantial reduction in monetary growth.

21. For the coming year, the target for broad money will be set at 6-10 per cent - the same as in last year's MTFS. The target for narrow money is 4-8 per cent. Both ranges should be consistent with our objective of a continuing reduction in inflation.

JACKSON

22. In assessing monetary conditions, we will also take into account the growth of the other aggregates besides MO and EM3. However, experience has shown that it is not enough simply to look at the money ~~numbers~~<sup>also</sup>. We will continue to have regard to ~~other evidence as well~~ including the exchange rate, and changes in behaviour which might affect the demand for money. And whereas in the past, broad money - and in particular EM3 - has perhaps been the prime focus of attention, in future I would expect both broad and narrow money to have equal status. Broad money may be particularly relevant for decisions on fiscal policy and funding, while narrow money may be more relevant for interest rates.



# BUDGET-SECRET

23. I have considered whether the move to a target for MO should be accompanied by any changes in the methods of monetary control. While in principle it would be possible for the authorities to control MO directly, this would involve some unattractive features -including greater interest rate volatility -and some major institutional changes. I have accordingly decided that the time is not ripe for such a move. Control of the money supply will continue to rely on a combination of an appropriate fiscal policy, interest rates and funding.

24. In setting the PSBR for 1984-85, which I shall come to in a moment, I have of course taken into account the funding implications. The broad aim will be to continue fully to fund the PSBR, though over or under funding from time to time cannot be ruled out. With the PSBR I am planning, there should be a considerably lower requirement for net debt sales, leaving room for planned privatisation issues and for a further pick-up in new capital issues as well as some further reduction in interest rates.

*This is surely simply not true at least on the pre-BIT forecast*

25. I am sure it is right to rely on a continued substantial contribution to funding from personal savings. Within what is likely to be a reduced overall funding requirement, I have decided that the National Savings target for 1984-85 should be [£3½ billion - slightly higher than this year].

# BUDGET-SECRET



**INTRODUCTION**

This Budget will set the Government's course for this Parliament. It is founded on the policies which we have consistently followed since 1979.

2. Consistency of purpose is the hallmark of this Government. It is the only way to improve economic performance and lay the foundations for future prosperity, more jobs and lower taxation. Above all, it is the only way to defeat inflation and achieve our ultimate objective of stable prices.

3. The results of the Medium Term Financial Strategy introduced in 1980 can be seen in four years of falling inflation, down now to the lowest levels since the sixties. And that in turn has brought a steady recovery of output, rising living standards and, more recently, rising employment.

4. The facts speak for themselves. They are a tribute to the courage and foresight of the five Budgets presented from this Despatch Box by my distinguished predecessor, the present Foreign Secretary, whose duties sadly keep him in Brussels today.

5. Today's Budget has two themes: first, the further reduction of inflation, which will further improve the prospects



for jobs; and second, the reform and simplification of the tax system, ~~which will make it fairer for all.~~

6. I shall begin by reviewing the economic background to the Budget. I shall then deal with the medium term financial strategy; with monetary policy and the monetary targets for next year; and with public borrowing and the appropriate PSBR for the coming year. I shall then turn to public expenditure, including the prospects for the longer term. Finally I shall deal with taxation, and the changes in the structure of taxation which will pave the way for cuts in taxes in subsequent years. Some of these cuts I shall announce today, for this is in a sense a Budget for two years. In a wider sense it is a tax reform Budget, setting out a tax strategy for this Parliament.

7. As usual, a number of press releases will be issued today, filling out the details of my tax proposals.



**THE ECONOMIC BACKGROUND**

8. But I start with the economic background, and the convincing evidence of recovery: a recovery that springs from the monetary and fiscal policies to which we shall hold.

9. Since 1980, inflation has fallen steadily from a peak of over 20 per cent. Last year it was down to about 4½ per cent, the lowest figure since the sixties. And with lower inflation have come lower interest rates.

10. The underlying strength of the recovery is clear. Whereas in some previous cycles recovery has come from a self-defeating stimulus to monetary demand, this time its roots are in our commitment to sound finance and honest money. Lower inflation and lower interest rates benefit industry, business, and consumer confidence. Falling inflation has made room for real growth, as we always said it would.

11. Across the economy, total money incomes grew in 1983 by about 8 per cent, of which 3 per cent represented real growth in output. Although there is still room for improvement, this ~~clearly~~ is a very much healthier division between inflation and real growth than the nation experienced in the 1970s. Output in the second half of 1983 is now reckoned to have exceeded the previous peak, before the world recession set in, and is still rising strongly.



12. Productivity too has continued to improve rapidly. Just as over the past year many have wrongly predicted an end to the recovery, so some have tried to dismiss the sharp rise in productivity as a flash in the pan. Yet during 1983 manufacturing productivity grew by 6 per cent with no sign of slowing down. Unit labour costs across the whole economy are likely to show the smallest annual increase since the 1960s. This has allowed a welcome and necessary recovery in real levels of profitability.

13. Higher profits lead to more jobs. The number of people in employment increased by about 85,000 between March and September last year. The loss of jobs in manufacturing has slowed down sharply, while jobs in services increased by getting on for 200,000 in the first nine months of last year. This is encouraging news for the unemployed and those who will be leaving school this summer.

14. But further progress ~~on productivity~~ is needed: although our unit wage costs in manufacturing rose by under 3 per cent last year, such costs actually fell in the US, Japan and Germany, our three biggest competitors. The employment prospect would be significantly improved if a bigger contribution to improved <sup>competitiveness</sup> ~~productivity~~ were to come from lower pay rises. Good sense about pay remains vital.

15. Demand, output, profits and employment all rose last year. Home demand has played the major part in the recovery so far. Lower inflation reduced people's need to save and real



incomes rose. Personal consumption increased by over 3½ per cent compared with 1982. Fixed investment rose rather faster than consumption, with investment in housing and services particularly strong.

16. Imports rose a little faster than home demand last year, as the UK emerged from recession ahead of our main trading partners - our rate of economic growth last year was the highest in the European Community. For much of 1983 our export performance reflected the weakness in many of our overseas markets. But by the end of last year world trade was clearly moving ahead again, and in the three months to January manufacturing exports increased very substantially. The balance of payments on current account last year is estimated to have been in surplus by about £2 billion.

17. Our critics have been confounded by the combination of recovery and low inflation. Even the pessimists have been forced to acknowledge the strength of the recovery. It is set to continue throughout this year at an annual rate of 3 per cent. Inflation is expected to remain low, edging back down to 4½ per cent by the end of this year. With rising incomes and low inflation, personal consumption will continue to grow. And the recovery is already becoming more broadly based. Encouraged by improved profitability and better long-term growth prospects, investment is expected to rise by 6 per cent this year.



18. Looking abroad, economic prospects are also more favourable than for some time. Output in the United States should continue to grow strongly this year. And recovery is spreading to the rest of the world.

19. Of course, there are inevitable risks and uncertainties. The size and continued growth of the United States budget deficit causes widespread concern, not least among Americans, and keeps American, and hence international, interest rates high. This acts as a brake on world recovery and worsens the problems of the debtor countries. Another consequence is a massive and still growing deficit in the US current balance of payments, financed by inflows of foreign capital, and leading to mounting pressures for protectionism within the United States, and sharp exchange rate movements. It is an unstable situation, creating worrying uncertainties.

20. A second potential risk is disruption in the oil market. The immediate prospects are less obviously volatile than they were a year ago. But uncertainties remain, and the United Kingdom, and indeed the world economy, inevitably remains vulnerable to any major disturbances.

21. But despite these risks there is a growing sense throughout the industrialised world that the recovery this time is not merely cyclical, but one which can be sustained. The essential requirement is the continued pursuit of prudent monetary and fiscal policies.



**THE MTFS**

22. For the United Kingdom, the Medium Term Financial Strategy has been the cornerstone of such policies. It will continue to play that role; to provide a framework and discipline for Government and to set out clearly, to industry and the financial markets, the guidelines of policy. Too often in the past Governments have abandoned financial discipline whenever the going got rough, and been driven to stagger from one short-term policy expedient to another. The temptation to accommodate inflationary pressures proved irresistible, and the nation's longer-term economic performance was progressively undermined.

X 23. The discipline of the MTFS was designed to ensure consistency between monetary and fiscal policies, and a proper balance in the economy. It is so designed to ensure that the more inflation and inflationary expectations come down, the more room is available for output and employment to grow.

24. People now know that the Government intends to stick to its medium term objectives. They understand that the faster inflation comes down, the faster output and employment recover. Increasing realism, and flexibility in the economy, owes much to the pursuit of firm and consistent policies within the MTFS framework.



25. Originally the MTFS covered four years. In this first Budget of a new Parliament we have thought it is appropriate to carry it forward for five years. So the MTFS published today in the Financial Statement and Budget Report -the Red Book - shows a continuing downward path for the monetary target ranges over the next five years, and a path for public borrowing consistent with that reduction. It takes full account of important influences such as the pattern of North Sea oil revenues, and the level of asset sales arising from the privatisation programme. For the last two years of the new MTFS, which lie beyond the period covered in last years Public Expenditure Survey and last month's White Paper, the Government has not yet made firm plans for public spending. But the MTFS assumption - and it is no more than an assumption - is that the level of public spending in 1987-88 and 1988-89 will be the same in real terms as that currently planned for 1986-87.

26. The precise figures set out in the MTFS are not of course a rigid framework, lacking all flexibility. As in the past, there may well need to be adjustments to take account of changing circumstances. But such changes will be made only when they will not jeopardise the consistent pursuit of the Government's objectives.



## MONETARY POLICY

27. Monetary policy will continue to play a central role. For further reductions in monetary growth are needed to achieve still lower inflation.

28. Over the twelve months to mid-February the growth of £M3 has been well within the 7-11 per cent target range, with M1 and PSL2 at or a little above the top of it. While in the early months of the target period most measures of money showed signs of accelerating, growth in all the target aggregates has since the summer been comfortably within the range.

29. Other evidence confirms that monetary conditions are satisfactory. The effective exchange rate has remained fairly stable, despite the international uncertainties and instability which I have described. And nominal interest rates have continued to decline in line with falling inflation.

30. To maintain sound monetary conditions in the years ahead the monetary targets must reflect changes in the financial system and in the significance of different measures of money. There is nothing new in this. Over the years we have altered the target ranges and aggregates to take account of such changes. But the thrust of the strategy has been maintained.



31. One important development has been the attempt to give a more explicit role to the narrow measures of money. Even when targets were set solely in terms of £M3, we recognised the significance of their behaviour. £M3 and the other broad aggregates give a good indication of the growth of liquidity. But a large proportion of this money is deposited in ways which earn interest. In defining policy it is therefore helpful also to make specific reference to measures of money which bear very little interest, and provide a good guide to the immediate potential for spending.

32. M1 was for this reason introduced as a target aggregate, but it has not proved entirely satisfactory for that purpose. Its behaviour has been dominated by changes in its large interest-bearing component, which has grown rapidly, and now accounts for 25 per cent of the total. With the introduction of new, interest bearing chequing accounts, the signs are that this will continue.

33. Other measures of narrow money have not been distorted to the same extent. In particular, MO, which consists mainly of currency, has not been subject to this development. It has been affected by other innovations that have reduced people's need for cash, but the pace of change has not diminished its value as an indicator of financial conditions. There is also the new aggregate M2, which was specifically devised to provide a comprehensive measure of transactions balances and which may in time prove a useful guide, but still needs to be interpreted with particular care.



34. In the past two years, it has been possible to set a single target range for both broad and narrow measures of money. But this will not normally be the case; for narrow monetary aggregates tend to grow more slowly than broader measures. And this year's Red Book sets out two separate ranges.

35. The target range for broad money will continue to apply to £M3, and for the coming year will be set at 6-10 per cent, as indicated in last year's MTFS. The target range for narrow money will apply to MO and for next year will be set at 4-8 per cent. To avoid any possible misunderstanding, I stress that the use of MO as a target aggregate will not involve any change in methods of monetary control.

36. Both target ranges will have equal importance in formulating policy. And we shall continue to take into account other measures of money, especially M2 and PSL2, as well as wider evidence of financial conditions, including the exchange rate. As in the past, we shall seek to influence monetary conditions by an appropriate combination of funding and operations in the money market.

37. So far as funding is concerned, the role of the National Savings movement will remain important. This year's target of £3 billion is likely to be achieved: the target for the coming year will again be £3 billion.

38. Precise monetary targets for the later years will be decided nearer the time. But to give a broad indication of the



objectives of monetary policy, the new MTFS, like previous versions, shows monetary ranges for a number of years ahead. These ranges are consistent with a continuing downward trend in inflation: they demonstrate the Government's intention to make further progress towards stable prices.



BUDGET SECRET

PUBLIC SECTOR BORROWING ETC

39. I turn now to public borrowing, for just as the classical formula for financial discipline - the gold standard and the balanced budget - had both a monetary and a fiscal component, so does the medium term financial strategy.

40. The MTF5 has always envisaged that the Public Sector Borrowing Requirement would fall as a percentage of Gross Domestic Product over the medium term. And it has, notably as a result of the courageous Budget introduced by my predecessor in 1981, which brought the PSBR down to 3½ per cent of GDP in 1981-82.

41. Since then there has been little further fall. The latest estimate of the PSBR for the current year, 1983-84, remains what it was in November: around £10 billion, equivalent to 3¼ per cent of GDP. This is significantly above what was intended at the time of last year's Budget, and would of course have been higher still had it not been for the measures taken last July.

42. We now need a further substantial reduction in borrowing, in order to help bring interest rates down further as monetary growth slows down. Sterling interest rates are, of course, also influenced by dollar interest rates and so by the US situation which I have already described: but that makes it all the more



BUDGET SECRET

important to curb domestic pressures. In contrast to virtually the whole of the post-war period, UK longer-term rates are now lower than American rates. As long as American rates remain near their current level, it is highly desirable that this advantage be maintained.

43. The higher level of asset sales planned as the privatisation programme gathers pace is a further reason for reducing the PSBR significantly in the coming year. Asset sales reduce the Government's need to borrow. But their effect on interest rates is less than the effect of direct ~~cuts~~<sup>reductions</sup> in Government spending programmes.

44. Last year's MTFs showed an illustrative PSBR for 1984-85 of 2½ per cent of GDP, equivalent to around £8 billion. But I believe that it is possible, and indeed prudent, to aim for a somewhat lower figure. I have therefore decided to provide for a PSBR next year of 2¼ per cent of GDP, or roughly £7 billion.

45. The House will recall that in November I warned that on conventional assumptions, including the 1983 Red Book's PSBR figure of £8 billion for next year, I might have to increase taxes slightly in the Budget. I am glad to report that the latest, and more buoyant, forecasts of tax revenue in the coming year, [coupled with the decisions taken in the Public Expenditure Survey and the continuing effects of the July measures,] have changed the picture. Bringing the PSBR down to £7 billion will not



BUDGET SECRET

require such an increase in taxation. In fact it will require no overall net increase at all. So the measures I shall shortly announce will, after indexation, be broadly neutral in their effects on revenue in 1984-85.

46. Better still, they will reduce taxation in 1985-86 by some £1½ billion. And the MTFs published today shows that there should be room <sup>for</sup> further tax cuts not only in 1985-86, but throughout the remainder of this Parliament, provided ~~of~~ ~~that~~ that we stick firmly to our published plans for public expenditure to 1986-87, and maintain an equally firm control of public spending thereafter.



BUDGET SECRET

PUBLIC EXPENDITURE

47. The Public Expenditure White Paper setting out our spending plans for the next three years was approved by the House last week. Today I want to consider the critically important issue of government spending in a rather wider perspective.

48. For far too long, spending has grown faster than has the economy as a whole. The trend has seemed inexorable, and the result has been that the great mass of the population have had to pay more and more in tax. To take just one example: as recently as 1963-64 no married man had to pay a penny of income tax unless his taxable income was at least 45 per cent of the average earnings level. Today the tax threshold is down to ~~little more than~~ under a third of average earnings. Over the years more and more people on lower and lower incomes have been brought into income tax.

49. We have seen a steady enlargement in the role of the State, at the expense of the individual, and a steady increase in the dead weight of taxation dragging down our economic performance as a nation.

50. Clearly this ~~dangerous~~ process has to stop. Of course, much public spending is directed to eminently desirable ends. But there is an important choice to be made; and it is not



BUDGET SECRET

enough simply to make marginal changes in spending programmes from year to year. The choice needs more fundamental national consideration and debate; and it needs to be set within a longer time horizon.

51. I am therefore publishing today, in addition to the customary Budget documents, a Green Paper on the prospects for public spending and taxation in the next ten years. It examines past trends; discusses pressures for still higher spending; and examines the rewards for the individual if these pressures can be contained.

52. The Green Paper concludes that, without firm control over public spending, there can be no prospect of bringing the burden of tax back to more reasonable levels. On the assumptions made in the Green Paper, the burden of taxation will be reduced to the levels of the early 1970s only if public spending does not rise in real terms over the next ten years. If, on the other hand, spending grows by 1 per cent a year in real terms after 1988-89, the tax burden would by 1993 be only just below the 1978-79 level, and still well above its level in the 1960s, even if the economy grows by about 2 per cent a year over the ten years. And of course excessive taxation slows the whole economy.

53. The Government believes that the issues discussed in the Green Paper merit the attention of the House and the country.



BUDGET SECRET

It is a discussion document - descriptive not prescriptive - and we shall welcome the fullest possible discussion.

54. I can at once inform the House of a further innovation. In contrast to previous years, I have no specific public expenditure measures to announce in this Budget. The White Paper plans stand.

55. But lest the innovation seems too sweeping, I can make one small announcement, which I think the House will welcome. Within the plans we have been able to provide the National Heritage Memorial Fund with additional resources which will enable them among other things to secure the future of Calke Abbey. My Rt Hon Friend the Secretary of State for the Environment is providing £6.3 million from his planned expenditure for this year and next, and I have accepted a claim on the Reserve of £2 million for next year.

56. The House will recall that the proposals for the new rates of social security benefit to come into force in November are not now made on Budget day. Following last year's legislation to return to the historic method of uprating, price protection is measured by reference to the Retail Price Index for May. Accordingly, my Rt Hon Friend the Secretary of State for Social Services will be announcing the new rates of social security benefits, including Child Benefit, in June.



BUDGET SECRET

57. Before turning from Government spending to Government revenue, I should add a word on public sector manpower. At the beginning of the last Parliament, the Government set itself the target of reducing the size of the Civil Service from 732,000 in April 1979 to 630,000 by April of this year. That target has been achieved. We have now set ourselves the further target of 593,000 by April 1988, and I am confident that it too will be achieved, and that a leaner Civil Service will continue to operate with increasing efficiency. Speaking for my own Departments, the tax changes I shall be announcing today will reduce manpower requirements by at least 1000 which will help towards meeting the 1988 target.



**TAX REFORM**

58. I mentioned at the outset that this will be a radical, tax-reforming, Budget. It will also significantly reduce the overall burden of tax over the next two years taken together [and indeed over the whole MTF period -] and I hope to have scope for further reductions in tax in subsequent Budgets.

59. My proposals for reform are guided by two basic principles. First, the need to make changes that will improve our economic performance over the longer term. Second, the desire to make life a little simpler for the taxpayer.

60. But I am well aware that the tax reformer's path is a stony one. Any change in the system is bound, at least in the short term, to bring benefits to some and disadvantages to others. And, if I may borrow a phrase from the Rt Hon member for Leeds East, the howls of anguish from the latter group tend to be rather more audible than the murmurings of satisfaction from the former.

61. ~~Reform must succeed, but need not be, in this sense, a howling success.~~ So I have rejected the extreme suggestion, popular in some quarters, that I should scrap our income-based tax system and replace it with a brand new expenditure-based system. A reform of this kind would produce, in the real world, an upheaval of mind-boggling dimensions.



62. But I don't believe we can afford to opt for the quiet life and do nothing. So I have chosen the middle way: to work for improvements, some I believe very substantial, but within the framework of our existing income-based system. I shall also be proposing transitional arrangements where I believe it fair and appropriate to do so.

63. The changes I shall be proposing today fall into three broad categories. These are the taxation of savings and investment, business taxation, and the taxation of personal income and spending.



## SAVINGS AND INVESTMENT

64. First, the taxation of savings and investment. The proposals I am about to make should improve both the direction and quality of both. And they will contribute further to the creation of a property-owning and share-owning democracy, in which more decisions are made by individuals rather than by intermediary institutions.

65. First, stamp duty. This was doubled from its long-standing 1 per cent by the post-war Labour Government in 1947, reduced by the Macmillan Government in 1963, and once again doubled to 2 per cent in the first Budget presented by the Rt Hon member for Leeds East in 1974. At its present level it is an impediment to mobility and incompatible with the welcome movement to greater competition in the City, following the withdrawal of the Stock Exchange case from the Restrictive Practices Court.

66. I therefore propose to halve the rate of stamp duty to 1 per cent. [Transactions from today will benefit from the new rate, unless documents have to be stamped before 20 March, which is the earliest date on which the change will have legal effect.]

67. For the home buyer, the new flat rate 1 per cent stamp duty will start at <sup>(an increased threshold of)</sup> £30,000. Below this level no duty will in future be payable, and 90 per cent of first time home buyers will therefore not be liable for stamp duty at all.



68. Reducing the rate of duty on share transfers will remove an important disincentive to [direct] investment in equities and increase the international competitiveness of our stock market. It should also help British companies to raise equity finance.

X  
69. In addition, I have three proposals to encourage the issue of corporate bonds. I shall go ahead with the new arrangements for deep discount stock and the reliefs for companies issuing Eurobonds and convertible loan stock which were announced but not enacted last year. And I propose to exempt from Capital Gains Tax certain corporate fixed interest securities provided they are held for more than a year. Since such securities are already exempt from stamp duty ~~an exemption I can confirm also extends to certain convertible loan stocks~~ this means that the tax concessions for Government borrowing in the gilt-edged market will now be virtually the same as for private sector borrowing in the corporate bond market.

X

70. The reductions in stamp duty will cost £450 million in 1984-85, of which £160 million is the cost of the relief on share transfers, and £290 million the cost of the relief on transfers of houses and other real estate.

71. Next, life assurance. I have concluded that there is no longer any justification for Premium Relief on Life Assurance,



which is now only one of a number of savings channels for ordinary people. The main effect of the relief today is to encourage institutional rather than direct investment, and to spawn a multiplicity of well-advertised tax management schemes. I propose to withdraw the relief on all new policies made after today. I stress that this change will apply only to new (or newly enhanced) policies, taken out or increased after today. Existing policies will not be affected at all. The change is estimated to yield £90 million in 1984-85.

72. We must also review unjustified penalties on direct personal investment. The Investment Income Surcharge is an unfair and anomalous tax on savings and on the rewards of successful enterprise. It hits the small businessman who reaches retirement without the cushion of a company pension scheme, and impedes the creation of farm tenancies. In the vast majority of cases it is a tax on savings made in the first place out of hard-earned and fully-taxed income. More than half of those who pay the investment income surcharge are over 65, and of these more than half would otherwise be liable to tax at only the basic rate.

73. I have therefore decided that the investment income surcharge should be abolished. The cost in 1984-85 will be some £25 million, and in a full year around £350 million.

74. Finally, I propose to draw more closely together the tax treatment of depositors in banks and building societies.



These institutions compete in the same market for personal deposits. I believe that they should be able to do so on more equal terms as far as tax is concerned.

75. One inequality has already been removed, with the recent change made on legal advice in the tax treatment of building societies' profits from gilt-edged securities. They are now treated in the same way as those of the banks have always been.

76. But the major inequality of treatment, against which the banks in particular have frequently complained, lies with the special arrangement for interest paid by building societies, under which the societies pay tax at a special rate - the "composite rate" - on the interest paid to the depositor who receives credit for income tax at the full basic rate.

77. This system, which has worked well for the past 90 years, has both an advantage and a disadvantage. The disadvantage is that a minority of depositors, who are below the income tax threshold, still suffer the deduction of tax at the composite rate. However, it is always open to such depositors to put their savings elsewhere, such as National Savings. The advantage of the scheme is its extreme simplicity, particularly for the taxpayer; most taxpayers are spared the bother of paying tax on interest through PAYE or individual assessment, while the Revenue are spared the need to recruit an additional 2000 staff to collect the tax due on interest paid without deduction.



78. In common with my predecessors of all Parties over the past 90 years, I am satisfied that the advantage of the composite rate arrangement outweighs the disadvantage. It follows that equal treatment of building societies and banks should be achieved, not by removing the composite rate from the societies, but by extending it to the banks and other licensed deposit takers.

79. Non-taxpayers would ~~of course~~ continue to be able to receive interest gross, should they wish to do so, by putting their money into appropriate National Savings facilities. But the purpose of the move is not, of course, to attract savings into Government hands: as I have already announced, next year's target for National Savings will be the same as this year's and last year's, and the total Government appetite for savings, which is measured by the size of the Public Sector Borrowing Requirement, is being significantly reduced. Moreover I have decided to reduce substantially the permitted maximum size of future holdings in the National Savings Investment Account and in Income Bonds.

80. The true purpose of the move is simple: simplicity itself. Unless they are higher rate taxpayers, individual bank customers will, when it comes to tax, be able to forget about bank interest altogether, for all the tax due on it will be deducted at source. The Inland Revenue will be able to make staff savings of up to an extra 1000 civil servants. Moreover, this figure takes no account of the extra numbers that would have



been required to operate the present system as the trend towards the payment of interest on current accounts develops.

81. Accordingly, I propose to extend the composite rate arrangements to interest received by UK resident individuals from banks and other licensed deposit takers with effect from 1985-86. The composite rate will not apply either to non-residents or to the corporate sector. Arrangements will also be made to exclude from the scheme Certificates of Deposit and Time Deposits of £50,000 or more.

82. Taken together, the major proposals I have just announced on stamp duty, life assurance relief, the investment income surcharge and the composite rate, coupled with other minor proposals, will provide a simpler and more straightforward tax system for savings and investment. They will remove biases which have discouraged the individual saver from investing directly in industry. And they will reinforce the Government's policy of encouraging competition in the financial sector, as in the economy as a whole.



## BUSINESS TAXATION

83. I now turn to company taxation.

84. In this area, Government has two responsibilities towards British business and industry. The first is to ensure that they do not have to bear an excessive burden of taxation. The second is to ensure that, given a particular burden, it is structured in the way that does least damage to the nation's economic performance.

85. The measures I am announcing today will, taking the next two years together, result in a ~~very~~ substantial reduction in the burden of taxation on British industry. And in addition I shall be proposing a far-reaching reform of the structure of company taxation.

86. The current rates of Corporation Tax are far too high, penalising profit and success, and blunting the cutting edge of enterprise. They are the product of too many special reliefs, indiscriminately applied and of diminishing relevance to the conditions of today. Some of these reliefs reflect economic priorities or circumstances which have long vanished, and now serve only to distort investment decisions and choices about finance. Others were introduced to meet short-term pressures, notably the upward surge of inflation. With inflation down to 5 per cent and set to go lower, this is clearly the time to take a fresh look. And with unemployment as high as it is today, it is particularly difficult to justify



a tax system which encourages low-yielding or even unprofitable investment at the expense of jobs.

87. My purpose therefore is to phase out some unnecessary reliefs, in order to bring about, over time, a markedly lower rate of tax on company profits.

88. First, capital allowances. Over virtually the whole of the post-war period there have been incentives for investment in both plant and machinery and industrial (though not commercial) buildings. But there is little evidence that these incentives have strengthened the economy or improved the quality of investment. Quite the contrary: the evidence suggests that businesses have invested substantially in assets yielding a lower rate of return than the investments made by our principal competitors. Too much of British investment has been made because the tax allowances make it look profitable, rather than because it would be truly productive.

89. The nation needs more investment, and the 6 per cent increase forecast for this year is encouraging. But the greatest benefits flow from investment decisions based on analysis of future market assessments, not future tax assessments.

90. I propose to restructure the capital allowances in three annual stages. In the case of plant and machinery, and assets whose allowances are linked with them, the first



year allowance will be reduced from 100 per cent to 75 per cent for all such expenditure incurred after today, and to 50 per cent for expenditure incurred after 31 March next year. After 31 March 1986 there will be no first year allowances, and all expenditure on plant and machinery will qualify for annual allowances on a 25 per cent reducing balance basis.

91. In addition, from next year annual allowances will be given as soon as the expenditure is incurred, and not, as they are today, when the asset comes into use. This will bring forward the entitlement to annual allowances for those assets, such as ships and oil rigs, for which some payment is normally made well in advance of their being brought into use.

92. For industrial buildings, I propose that the initial allowance should fall from 75 per cent to 50 per cent from tonight, and be further reduced to 25 per cent from 31 March next year. After 31 March 1986 the initial allowance will be abolished, and expenditure will be written off on an annual 4 per cent straight line basis. I should add that, when these changes have all taken place, in respect of both plant and machinery and industrial buildings, tax allowances will still on average be rather more generous than would be provided by a strict system of economic depreciation.

93. The changes in the rates of allowances will not apply to payments under binding contracts entered into on or before today, provided that the expenditure is incurred within the



next three years.

94. After consulting my Rt Hon Friend the Secretary of State for Trade and Industry, I have decided to make transitional tax arrangements for certain investment projects in the regions. Existing capital allowances will continue to apply to expenditure on projects in Development Areas and special Development Areas for which regional development grants are available and offers of selective assistance have already been made between 1 April 1980 and today. Similar arrangements were announced for regional development grants in my Rt Hon Friend's White Paper on Regional Industrial Development last December.

95. Over the same period to 31 March 1986 most other capital allowances will be brought into line with the main changes I have announced. The Inland Revenue will be issuing a press notice tonight giving full details of these proposals.

96. Next, stock relief. As the House will recall, this was introduced by the last Labour Government as a rough and ready form of emergency help to businesses facing the ravages of high inflation. These days are past; and relief is no longer necessary; for company liquidity has improved and, above all, inflation has fallen sharply, ~~and will be falling further during this Parliament.~~ Accordingly, I propose to abolish stock relief from this month.



97. The changes I have just announced, in capital allowances and stock relief, enable me to embark on a major programme of progressive reductions in the main rate of Corporation Tax. For profits earned in the year just ending, on which tax is generally payable in 1984-85, the rate will be cut from 52 per cent to 50 per cent. For profits earned in 1984-85 the rate will be further cut to 45 per cent. Looking further ahead, to profits earned in 1985-86, the rate will go down to 40 per cent; and for profits earned in 1986-87 the main rate of Corporation Tax will be 35 per cent.

98. All these rates for the years ahead will be included in this year's Finance Bill.

99. And they will bring a further benefit. Responses to the Corporation Tax Green Paper published in 1982 revealed a strong and general desire to retain our imputation system of Corporation Tax. This allows a company to offset in full all interest paid. But only a partial deduction for dividends is allowed. Companies thus have an unhealthy incentive to finance themselves through borrowing, in particular bank borrowing, rather than by raising equity capital. The closer the Corporation Tax rate comes to the basic rate of income tax, the smaller this undesirable distortion becomes.

100. Of course, the majority of companies are not liable to pay the main rate of Corporation Tax at all. For them it is the small companies' rate, at present 38 per cent, which applies.



I propose to reduce this rate forthwith to 30 per cent, for profits earned in 1983-84 and thereafter.

101. The Corporation Tax measures I have just announced will cost £280 million in 1984-85. In 1985-86 the cost will be £600 million - made up of £1,150 million by way of reductions in the rates, only partially offset by a £550 million reduction in the value of the reliefs. The estimated costs for later years, which have been provided for in the MTFs figures contained in the Budget Red Book, have been drawn up on a cautious basis. Thus business and industry can go ahead confidently on the basis of the Corporation Tax rates I have announced today, and which set the framework of company taxation for the rest of this Parliament.

102. I expect these changes to have both a somewhat different impact in the short and long term. In the short term, some investment should be <sup>budget</sup> forward over the next two years, to take advantage of high first year capital allowances while they last - a prospect made all the more alluring for business by virtue of the fact that profits earned will be taxed at the new lower, rates. But the more important and durable effect will be to encourage the search for investment projects with a genuinely worthwhile return, and to discourage uneconomic investment.

103. It is doubtful if it was ever really sensible to subsidise capital irrespective of the true rate of return. Certainly,



with over three million unemployed it cannot make sense to do so.

104. These changes hold out an exciting opportunity for British industry as a whole: an opportunity further to improve its profitability, and to expand, building on the recovery that is already well under way. Higher net profits should encourage and reward enterprise and stimulate [higher current expenditure and] innovation in all its forms - research and development and work on new products, processes and markets. They are the centre-piece, for business, of this Budget and the tax strategy for this Parliament.

105. But I have further measures to announce that are relevant to business.

106. First, the Business Expansion Scheme, introduced last year as a successor to the Business Start Up Scheme, has been widely welcomed as a highly imaginative scheme for encouraging individuals to invest in small companies. It is already proving a considerable success. It now needs time to settle down, and I have only one change to propose this year.

107. The scheme was designed to offer generous incentives for investment in high risk areas by new or expanding companies. Farming is clearly not an area which falls within this category, and I therefore propose that from today farming should cease to be treated as a qualifying trade under the scheme. I am



also ready to consider tightening the scheme further, if it becomes clear at any time in the future that it is being used for purposes for which it was clearly not designed.

108. Secondly, as a measure of help to small firms, I propose to raise the VAT registration threshold with effect from midnight tonight from £18,000 to £18,700.

109. Thirdly, in keeping with what I have said about removing distortions, I propose to abolish two reliefs in the personal tax field which were introduced at a time when this country suffered from excessively high rates of income tax. As we have reduced those rates, the reliefs are no longer justified.

110. The first distortion is the 50 per cent <sup>tax</sup> deduction (falling after 9 years to 25 per cent) <sup>applies to</sup> ~~given from~~ the emoluments of foreign employees working here for foreign employers. Foreign employees are often paying much less tax here than they would either at home or in most other European countries. At present income tax rates, the need for the relief has clearly disappeared. Moreover it is open to widespread abuse. It is, for example, possible for the son of an immigrant, working here for a foreign company, to pay tax on only 75 per cent of his salary, even if he himself has lived in this country all his life. I therefore propose to withdraw the relief entirely for all new cases from today, and to withdraw the 25 per cent deduction from existing beneficiaries from 6 April next. The 50 per cent deduction will be phased out over the



5 years to 5 April 1989.

111. I also propose to withdraw the so-called foreign earnings relief for United Kingdom residents who perform their duties both here and overseas and who spend at least 30 days abroad in a tax year. This relief too has lost its rationale, which harks back to the days of penalty high income tax rates. It too has been exploited, in particular by those who prolong their overseas visits purely in order to gain a tax advantage. For the same reason, I propose to withdraw the matching relief for the self-employed who spend 30 days abroad, and for resident employees and self-employed who have separate employments or separate trades carried on wholly abroad. The relief will be halved to 12½ per cent in 1984-85 and removed entirely from 6 April 1985. However, I have also authorised the Inland Revenue to consult interested parties about a possible relaxation in the rules governing the taxation of expenses reimbursed to employees for travel overseas. I am not making any change to the 100 per cent deduction given for absences abroad of 365 days or more.

112. The abolition of these reliefs will eventually yield revenue savings of over £150 million; and represents another useful step in the removal of complexity and distortions.

113. I need to set the car benefit scales for 1985-86 for those provided with the use of a car by their employer.



Despite the increases over recent years, the levels still fall short of any realistic measure of the true benefit. I am accordingly proposing an increase of 10 per cent in both the car and car fuel scales with effect from April 1985.

114. Unnecessarily high rates of tax discourage enterprise and risk taking. This is true of the capital taxes, just as it is of the corporation and income taxes. It is a matter of particular concern to those involved in running unquoted family businesses. The highest rates of capital transfer tax are way out of line with comparable rates abroad, and with the top rates of other taxes in this country. I propose therefore to reduce the highest rate of capital transfer tax from 75 per cent to 60 per cent and to raise the threshold to £64,000 in line with indexation. [For lifetime gifts I further propose to make the rate one-half of that on death over the whole scale.]

*Mistaking*

115. For capital gains tax I will, as promised, bring forward in the Finance Bill proposals to double the limit for retirement relief to a figure of £100,000, backdated to April 1983. A consultative document on other possible changes in this relief is being issued next week. I am proposing no other changes this year in capital gains tax beyond the statutory indexation of the exempt amount from £5,300 to £5,600. However, the tax continues to attract criticism - not least for its complexity - and that is a matter to which I hope to return in a later year.



116. We have done much to improve the Development Land Tax. Early in the last Parliament, my predecessor increased the threshold from £10,000 to £50,000. I now propose a further increase to £75,000, which will reduce the numbers affected by the tax by more than one-third.

117. Next share options. The measures introduced in the last Parliament to improve employee involvement through profit sharing and savings related share option schemes have been a notable success. The numbers of all these employee schemes have increased from about 30 in 1979 to over 670 now, benefiting some half a million employees. To maintain and build on this progress I propose to increase the monthly limit on contributions to savings related share option schemes from £50 to £100. I have also authorised the Inland Revenue to double the tax-free limits under the concession on long service awards and to include the gift of shares in the employee's company.

118. But beyond this, I am convinced that we need to do more to attract top calibre company management and to increase the incentives and motivation of existing executives and key personnel by linking their rewards to performance. I propose therefore that, subject to certain necessary limits and conditions, share options generally will be taken out of income tax, leaving any gain to be charged to capital gains tax on ultimate disposal of the shares. The new rules will



apply to options meeting the conditions which are granted from 6 April, ~~1988~~.

119. I am sure that all these changes will be welcomed as measures to encourage the commitment of employees to the success of their companies and to improve the performance, competitiveness and profitability of British industry.

120. Before turning to North Sea taxation, I should like to remind the House of the Government's concern at the threat which the spread of unitary taxation in certain US states has posed to the US subsidiaries of British firms. With our European partners we are monitoring the situation closely, and await with keen interest the imminent report of a Working Group under my US counterpart. It is very important that a satisfactory solution be speedily implemented.

121. This issue is not wholly irrelevant to the North Sea, for US firms operating there, or elsewhere in this country, are not of course taxed on a unitary basis, taking account of world-wide profits.

122. Last year's North Sea tax changes were well received, and there has been encouraging progress in the number of development projects coming forward, as well as in exploration and appraisal. The Government is already committed to a study of the economics of investment in incremental development in existing fields. This is of increasing importance and in consultation with <sup>my vt has filed</sup> the Secretary of State for Energy I



therefore propose to review this area with the industry, and to legislate as appropriate next year to improve the position. To prevent projects being deferred pending this review, any changes will apply to all projects which receive development consent after today.

123. Meanwhile, I am taking two measures to prevent an unjustified loss of tax in the North Sea. First, in addition to the PRT measures on farmouts which I announced last September, I am limiting the potential Corporation Tax cost of such deals. Second, I propose to repeal the provision which allows Advance Corporation Tax to be repaid where Corporation Tax is reduced by PRT. I have concluded that this can no longer be justified. I have also reviewed the case for extending last year's future field concessions to the Southern Basin, but have concluded that additional incentives here are not needed.

124. I have just two further changes affecting business to propose, both of which will come into force on 1 October.

125. Ever since VAT was introduced in this country, we have treated imports differently from the way in which they are treated by our main European Community competitors. In a nutshell, they require VAT on imported goods to be paid in the same way as customs duties. We do not. Under our system an importer does not have to account for VAT on his



imports until he makes his normal VAT return, on average some 11 weeks later. During this time the importer enjoys free credit at the taxpayer's expense. This is an advantage not enjoyed by the home-produced equivalent of the import, since businesses buying from UK suppliers have to pay VAT when they pay their suppliers.

126. The UK system does indeed have many advantages, which is why the European Commission has for some years now been seeking to get it adopted throughout the Community, with the full support of both my predecessor and myself. But the plain fact is that in all that time the Commission has made no progress whatever.

127. I must tell the House that I am not prepared to put British industry at a competitive disadvantage in the home market any longer. Should our European partners at any time undergo a Damascene conversion, and ~~all~~ agree that the Commission's proposal should be accepted after all, then of course we would gladly revert to the present system. But in the meantime I propose to move to the system used by our major competitors and charge VAT straight away on imports, providing the same facilities for deferring payment as apply to customs duties. That means that most importers will be able to defer payment of VAT by on average one month from the date of importation. But that is all.



128. As I have said, this change will apply from 1 October. By bringing forward VAT receipts, it will bring in an extra £1.2 billion in 1984-85, some of which will of course be *borne* ~~carried~~ by foreign producers and manufacturers. There will naturally be no increased revenue in subsequent years.

129. The second change I propose to make on 1 October concerns the National Insurance Surcharge. This, once again, was a brainchild of the Rt Hon member for Leeds East. Having introduced it in 1977 at the rate of 2 per cent, he then raised it in 1978 to 3½ per cent. During the last Parliament, my predecessor succeeded in reducing it to 1 per cent, and we are pledged to abolish it during the lifetime of this Parliament.

130. Given the impact that this tax has, not only on industrial costs but also - at a time of high unemployment - on jobs, I have decided to take the opportunity of this my first Budget to fulfil that pledge. Abolition of the National Insurance Surcharge from October will reduce private sector employers' costs by almost £350 million in 1984-85, and over £850 million in a full year.

131. Thus my proposals offer British business the abolition of the tax on jobs and the reduction of the rate of taxation on profits. They also sweep away a number of out-dated reliefs, reduce distortions, and assist enterprise.



BUDGET SECRET

INDIRECT TAXES

131. Having announced major reforms of both the taxation of savings and investment and the taxation of business, I turn now to the third and final area in which I propose to make progress on tax reform. This is the taxation of personal income and spending.

*check problem* |  
132. The broad principle was clearly set out in the Manifesto on which we were first elected in 1979 and which emphasised the need for a switch from taxes on earnings to taxes on spending. My predecessor made an important move in this direction in his first budget, and the time has come to make a further move today. To reduce direct taxation by this means is important in two ways. It improves incentives and makes it more worthwhile to work, and it increases the freedom of choice of the individual.

133. I do not however see the excise duties - with certain exceptions - as an area for major change. I shall of course need to raise most of the duties broadly in line with inflation, so as to maintain their real value: not to do so would run counter to the philosophy I outlined a moment ago. But with inflation now as low as it is, the necessary increases are on the whole mercifully modest. Only for a few particular duties do I envisage steeper rises.



BUDGET SECRET

134. One significant exception is tobacco, where I ~~am~~  
~~convinced of the need~~ <sup>believe it is right</sup> to raise the duty in real terms, <sup>given</sup> ~~to help~~  
~~cut smoking and thus reduce~~ the potential danger to health. I  
therefore propose an increase in the tobacco duty which,  
including VAT, will put 10p on the price of a packet of  
cigarettes, with corresponding increases for hand-rolling  
tobacco and cigars. This will do no more than restore the tax  
on tobacco to its 1965 level. I do not propose to increase the  
duty in pipe tobacco, which is important for a great many  
pensioners. These changes will take effect from midnight on  
Thursday.

135. For the duties on petrol and derv I propose simply broad  
revalorisation, which means increases which, again including  
VAT, will ~~increase~~ <sup>raise</sup> the price at the pumps by 4½p and 3½p a  
gallon respectively. I do not propose to increase the duty on  
heavy fuel oil, which is of particular importance to industrial  
costs. These changes will take effect for oil delivered from  
refineries and warehouses from six o'clock this evening.

136. There is one excise duty which I propose to do away with  
altogether. Many of those who find it hardest to make ends  
meet, including in particular many pensioners, use paraffin  
stoves to heat their homes, and it is with them in mind that I  
propose to abolish the duty on kerosene from six o'clock  
tonight. I am sure that this will be welcomed on all sides of  
the House.



137. The various rates of Vehicle Excise Duty will, once again, go up roughly in line with prices. Thus the duty for cars and light vans will be increased by £5, from £85 to £90 a year. However, given the further evidence my Rt Hon Friend the Secretary of State has now received on the wear and tear that various types of vehicle cause to the roads, there will be reductions in duty for the lightest lorries, offset by higher increases for some heavier lorries. All these changes in Vehicle Excise Duty will take effect from tomorrow.

138. However, I propose to exempt from Vehicle Excise Duty all recipients of the War Pensioners' Mobility Supplement.

139. And I have decided to widen the specific VAT reliefs for the disabled in the important area of transport. The existing VAT relief for motor vehicles designed or adapted for use by the handicapped will be extended, and matched by a new Car Tax relief. The effect will be that neither VAT nor car tax will apply to family cars designed for disabled people or substantially adapted for their use.

140. I now come to the most difficult decision I have to take in the excise duty field. As the House will be aware, the rules of the European Community, so far as alcoholic drinks are concerned, are designed to prevent a Member state from protecting its own domestic product by imposing a significantly higher duty on competing imports. In pursuit of this, the Commission has taken a number of countries to the European Court of Justice.



BUDGET SECRET

141. In our case, the Commission contended that we were protecting beer by under-taxing it in relation to wine. We fought the case, but lost; and I am now implementing the judgement handed down by the Court last year. Accordingly, I propose to increase the duty on beer, not by the 7p a pint which has been widely rumoured in the press, but by the minimum amount needed to comply with the judgement and maintain revenue: 2p on a typical pint of beer, including VAT. At the same time, the duty on table wine will be reduced by the equivalent of about 18p a bottle, again including VAT.

142. I cannot, however, ignore the fact that while we comply with the judgement of the European Court, one of our partners appears determined not to do so. I refer to Italy, which has been ordered by the Court to remove forthwith its discrimination against Scotch whisky, but as yet shows no sign whatever of complying. I have therefore decided to introduce a temporary duty surcharge on vermouth of some 20p a bottle on top of the basic increase, to which I shall come in a moment. This surcharge will come into operation on 1 September unless the Italian Government has - as I very much hope it will - implemented the Court's judgement by that date, and it will lapse as soon as I am satisfied that it has complied.

143. As for the rest of the alcoholic drinks, cider, which increasingly competes with beer but attracts a lower duty, will go up by 3p a pint. The duties on made-wine will be aligned with those on other wine. And I propose to increase the duty on sparkling wine, fortified wine and spirits by about 10p a



bottle, including VAT. All these changes, except the vermouth surcharge, will take effect from midnight tonight.

144. These changes in excise duties will, all told, bring in some £840 million in 1984-85, some £200m more than is required to keep pace with inflation. The addition is of course ~~largely~~ due to the increase in tobacco duty.

145. But much of the extra revenue I need to make a substantial switch this year from taxes on earnings to taxes on spending will come from VAT. I propose no change in the rate of VAT. Instead, I intend to broaden the base of the tax by extending the 15 per cent rate to two areas of expenditure that have hitherto been zero-rated.

146. First, alterations to buildings. At present repairs and maintenance are taxed, but alterations are not. The borderline between these two categories is the most confused in the whole field of VAT. I propose to end this confusion and illogicality by bringing all alterations into tax. However, to allow a reasonable time for existing commitments to be completed or adjusted, the change will be deferred until 1 June.

147. Secondly, food. Most food is zero-rated. But food served in restaurants is taxed, together with a miscellaneous range of items including ice-cream, confectionery, soft drinks and crisps, which were brought into tax by the Rt Hon Member for Leeds East. Take-away food clearly competes with other



forms of catering, and I therefore intend to bring into tax hot take-away food and drinks, with effect from 1 May.

148. The total effect of the extensions of the VAT coverage which I have proposed will be to increase the yield of the tax by £375 million in 1984-85 and by almost £650 million in 1985-86.

149. The total impact effect on the Retail Price Index of the VAT changes and excise duty changes taken together will be less than three-quarters of one per cent. This has already been taken into account in the forecast which I have given to the House of a decline in inflation to  $4\frac{1}{2}$  per cent by the end of the year.

150. The extra revenue raised in this way will enable me within the overall framework of a neutral Budget to lighten the burden of income tax.



**PERSONAL TAXATION**

151. Since we took office in 1979, we have cut the basic rate of income tax from 33 per cent to 30 per cent and sharply reduced the confiscatory higher rates inherited from the last Labour Government. We have increased the main tax allowances not simply in line with prices but by around 8 per cent in real terms. It is a good record. But it is not enough. The burden of income tax is still too heavy.

152. During the lifetime of this Parliament, I intend to carry much further the progress we have already made. For the most part, this will have to wait for future Budgets, particularly since I have thought it right this year to concentrate on setting a new regime of business taxation for the lifetime of a Parliament - and beyond. But as a result of the changes to taxes on spending which I have just announced, I can make a start now.

153. I propose to make no change this year in the rates of income tax. So far as the allowances and thresholds are concerned, I must clearly increase these by the amounts set out in the statutory indexation formula, based on the 5.3 per cent increase in the Retail Price Index to December. The question is how much more I can do, and how to direct it.



154. I have decided that, this year, the right course is to use every penny I have in hand, within the framework of a revenue neutral Budget, to lift the level of the basic tax thresholds, for the married and single alike. It is fundamentally wrong that we collect income tax from people whose incomes are so low that they are entitled to social security benefits on grounds of need. Moreover low tax thresholds make the poverty and unemployment traps much worse, so that the financial incentive to find a better job or even any job may decline almost to zero. There is, alas, no quick or cheap solution to these problems. But that is all the more reason to make a start on solving them now.

155. I propose to increase most thresholds in line with the statutory requirement, and by no more. The first higher rate of 40 per cent will apply when taxable income reaches £15,400 a year and the top rate of 60 per cent to taxable income of £38,100 or more. The single age allowance will rise from £2,360 to £2,490 and the married age allowance from £3,755 to £3,955.

156. For the basic thresholds, statutory indexation would mean putting the single and married allowances up by £100 and £150 respectively. I am glad to say that I can do considerably better than that. I propose to increase the basic thresholds by well over double what is required by indexation. The single person's threshold will be increased by £220, from £1,785 to £2,005; and the married threshold by £360, from £2,795 to £3,155. ~~The special allowances for widows, and for single parents, will as a consequence go up by some 14 per cent.~~



157. This is an increase of around  $12\frac{1}{2}$  per cent, or some 7 per cent in real terms. It brings the married man's tax threshold for 1984-85 to its highest level in real terms since the war. It means that every tax-paying married couple in the land will enjoy an income tax cut of at least £2 a week. And it means that a large number of people, those with the smallest incomes of all, are taken out of income tax altogether. ~~And~~ Some 850,000 people - over 100,000 of them widows - will not pay tax in 1984-85 who would have paid if thresholds had not been increased. And 400,000 fewer than if the allowances had merely been indexed.

158. All these changes will take effect under PAYE on the first pay day after 10 May. Their cost is considerable: some £1.8 billion in 1984-85, of which roughly half represents the cost of indexation.

159. This is as far as I can go on income tax this year, within a broadly revenue-neutral Budget for 1984-85. But as I have already said, so long as we hold to our published planned levels of public spending, there is an excellent prospect consistent with the necessary downward path of public borrowing of further tax cuts in next year's Budget. These would be on top of the measures I have announced in this Budget which, as I have already told the House, will reduce taxation in 1985-86 by some £1 $\frac{1}{4}$  billion, with business taking the lion's share. So for next year I would hope to be concentrating on further help to individuals, and principally on income tax.



## CONCLUSION

160. I have, Mr Deputy Speaker, completed the course I charted at the outset this afternoon. I have described the recovery, and how the Government plans to sustain it, by working for further reductions in inflation, by maintaining sound money and by curbing borrowing. I have described a three part reform strategy for a fairer, simpler tax system. And I have been able to propose substantial tax reductions over two years in a Budget that is revenue-neutral for 1984-85. It is a Budget for responsibility and reform; and I commend it to the House.

16-80



# BUDGET - SECRET

(prof)

## BLOCK M: CONCLUSION

This Budget has confirmed the broad strategy on which we embarked in 1979. It takes economic renewal another stage forward. And it is an important tax reform Budget, which marks a major step towards lower taxes and a simpler tax system. I commend it to the House.

*To be done by Mr.*

### Conclusion.

160. I have, Mr Deputy Speaker, completed the course I charted at the outset this afternoon. I have described the recovery, and how the Government plans to sustain it, ~~and~~ ~~have restated the strategy, which~~ ~~adding to it~~ <sup>working for</sup> by further reductions in inflation, by maintaining sound money and by <sup>curbing</sup> borrowing. I have described a three part <sup>reform</sup> strategy <sup>to which</sup> for a fairer, simpler tax <sup>system</sup> strategy. And I have been able to <sup>propose</sup> ~~offer~~ substantial tax reductions over two years in a Budget that is revenue-neutral for 1984-85. It is a Budget for responsibility and reform; and I <sup>commend</sup> it to the House.



EST's  
Comments:

MWOOD POWOTS AT

2, 26, 28  
 32, 42  
 80, 95  
 68, 96  
 103, 157

### INTRODUCTION

THIS BUDGET WILL SET THE GOVERNMENT'S COURSE FOR THIS PARLIAMENT. THERE WILL BE NO LETTING UP IN OUR DETERMINATION TO DEFEAT INFLATION. THIS BUDGET WILL CONTINUE THE POLICIES THAT WE HAVE FOLLOWED CONSISTENTLY SINCE 1979. THOSE POLICIES PROVIDE THE ONLY WAY TO ACHIEVE OUR ULTIMATE OBJECTIVE OF STABLE PRICES. TO LET THEM GO WOULD BE TO RISK RENEWED INFLATION, AND MUCH HIGHER UNEMPLOYMENT. AS A RESULT OF OUR DETERMINED EFFORTS, INFLATION IS AT ITS LOWEST LEVEL SINCE THE 'SIXTIES. GROWTH IN THE ECONOMY IS STRONG. EMPLOYMENT IS GROWING.

2. THOSE ACHIEVEMENTS ARE A TRIBUTE TO THE COURAGE AND FORESIGHT OF THE FIVE BUDGETS PRESENTED BY MY DISTINGUISHED PREDECESSOR, WHOSE DUTIES (SADLY) KEEP HIM IN BRUSSELS TODAY.

SO FORTUNATELY

/My BUDGET



BUDGET SECRET

3. I SHALL DO NOTHING TODAY TO COMPROMISE THOSE SUCCESSES. BUT THERE IS MUCH THAT I CAN DO TO BUILD UPON THEM.

4. MY BUDGET TODAY HAS TWO THEMES.

5. FIRST, THE FURTHER REDUCTION OF INFLATION. AND SECOND, A SERIES OF TAX REFORMS DESIGNED TO ENABLE THE ECONOMY TO WORK BETTER. REFORMS TO STIMULATE ENTERPRISE AND SET BRITISH BUSINESS ON THE ROAD TO PROFITABLE EXPANSION. REFORMS THAT WILL HELP TO BRING NEW JOBS.

6. I SHALL BEGIN BY REVIEWING THE ECONOMIC BACKGROUND TO THE BUDGET. I SHALL THEN DEAL WITH THE MEDIUM TERM FINANCIAL STRATEGY; WITH MONETARY POLICY AND THE MONETARY TARGETS FOR NEXT YEAR; AND WITH PUBLIC BORROWING AND THE APPROPRIATE PSBR FOR THE COMING YEAR. I SHALL THEN TURN TO PUBLIC EXPENDITURE, INCLUDING THE PROSPECTS FOR THE LONGER

/TERM.



BUDGET SECRET

TERM. FINALLY I SHALL DEAL WITH TAXATION, AND THE CHANGES IN THE STRUCTURE OF TAXATION WHICH WILL PAVE THE WAY FOR CUTS IN TAXES IN SUBSEQUENT YEARS.

7. AS USUAL, A NUMBER OF PRESS RELEASES, FILLING OUT THE DETAILS OF MY TAX PROPOSALS, WILL BE AVAILABLE FROM THE VOTE OFFICE AS SOON AS I HAVE SAT DOWN.



THE ECONOMIC BACKGROUND

8. I START WITH THE ECONOMIC BACKGROUND.

9. SINCE 1980, INFLATION HAS FALLEN STEADILY FROM A PEAK OF OVER 20 PER CENT. LAST YEAR IT WAS DOWN TO ABOUT 4½ PER CENT, THE LOWEST FIGURE SINCE THE SIXTIES. AND WITH LOWER INFLATION HAVE COME LOWER INTEREST RATES.

10. THIS IN TURN HAS LED TO AN ECONOMIC RECOVERY WHOSE UNDERLYING STRENGTH IS NOW BEYOND DISPUTE. WHEREAS IN SOME PREVIOUS CYCLES RECOVERY HAS COME FROM A SELF-DEFEATING STIMULUS TO MONETARY DEMAND, THIS TIME IT HAS SPRUNG FROM SOUND FINANCE AND HONEST MONEY. LOWER INFLATION AND LOWER INTEREST RATES BENEFIT INDUSTRY, BUSINESS, AND CONSUMER CONFIDENCE ALIKE.

/ACROSS THE



## BUDGET SECRET

11. ACROSS THE ECONOMY, TOTAL MONEY INCOMES GREW IN 1983 BY ABOUT 8 PER CENT, OF WHICH 3 PER CENT REPRESENTED REAL GROWTH IN OUTPUT. ALTHOUGH THERE IS STILL ROOM FOR IMPROVEMENT, THIS IS A VERY MUCH HEALTHIER DIVISION BETWEEN INFLATION AND REAL GROWTH THAN THE NATION EXPERIENCED IN THE 1970s. OUTPUT IN THE SECOND HALF OF 1983 IS NOW RECKONED TO HAVE EXCEEDED THE PREVIOUS PEAK, BEFORE THE WORLD RECESSION SET IN, AND IS STILL RISING STRONGLY.

12. PRODUCTIVITY TOO HAS CONTINUED TO IMPROVE RAPIDLY. JUST AS OVER THE PAST YEAR MANY HAVE WRONGLY PREDICTED AN END TO THE RECOVERY, SO SOME HAVE TRIED TO DISMISS THE SHARP RISE IN PRODUCTIVITY AS A FLASH IN THE PAN. YET DURING 1983 MANUFACTURING PRODUCTIVITY GREW BY 6 PER CENT WITH NO SIGN OF SLOWING DOWN. UNIT LABOUR COSTS ACROSS THE WHOLE ECONOMY ARE LIKELY TO SHOW THE SMALLEST ANNUAL INCREASE SINCE THE 1960s. THIS HAS ALLOWED A WELCOME AND NECESSARY RECOVERY IN REAL LEVELS OF PROFITABILITY.

/HIGHER PROFITS



BUDGET SECRET

13. HIGHER PROFITS LEAD TO MORE JOBS. THE NUMBER OF PEOPLE IN WORK INCREASED BY ABOUT 80,000 BETWEEN MARCH AND SEPTEMBER LAST YEAR. THE LOSS OF JOBS IN MANUFACTURING HAS SLOWED DOWN SHARPLY, WHILE JOBS IN SERVICES INCREASED BY ALMOST 200,000 IN THE FIRST NINE MONTHS OF LAST YEAR.

14. BUT FURTHER PROGRESS IS NEEDED: ALTHOUGH OUR UNIT WAGE COSTS IN MANUFACTURING ROSE BY UNDER 3 PER CENT LAST YEAR, OUR THREE BIGGEST COMPETITORS, THE US, JAPAN AND GERMANY, DID BETTER. THE EMPLOYMENT PROSPECT WOULD BE SIGNIFICANTLY IMPROVED IF A BIGGER CONTRIBUTION TO IMPROVED COST PERFORMANCE WERE TO COME FROM LOWER PAY RISES.

15. DEMAND, OUTPUT, PROFITS AND EMPLOYMENT ALL ROSE LAST YEAR. HOME DEMAND HAS PLAYED THE MAJOR PART IN THE RECOVERY SO FAR. LOWER INFLATION REDUCED PEOPLE'S NEED TO SAVE, AND REAL INCOMES ROSE. PERSONAL CONSUMPTION INCREASED BY OVER 3½ PER

/CENT COMPARED



BUDGET SECRET

CENT COMPARED WITH 1982. FIXED INVESTMENT ROSE RATHER FASTER THAN CONSUMPTION, WITH INVESTMENT IN HOUSING AND SERVICES PARTICULARLY STRONG.

16. OUR RATE OF ECONOMIC GROWTH LAST YEAR WAS THE HIGHEST IN THE EUROPEAN COMMUNITY. FOR MUCH OF 1983 OUR EXPORT PERFORMANCE WAS AFFECTED BY WEAK DEMAND IN MANY OF OUR OVERSEAS MARKETS, WHILE IMPORTS ROSE SLIGHTLY FASTER THAN HOME DEMAND. BUT BY THE END OF LAST YEAR WORLD TRADE WAS CLEARLY MOVING AHEAD AGAIN, AND IN THE THREE MONTHS TO JANUARY MANUFACTURING EXPORTS INCREASED VERY SUBSTANTIALLY. THE BALANCE OF PAYMENTS ON CURRENT ACCOUNT LAST YEAR IS ESTIMATED TO HAVE BEEN IN SURPLUS BY ABOUT £2 BILLION.

17. OUR CRITICS HAVE BEEN CONFOUNDED BY THIS COMBINATION OF RECOVERY AND LOW INFLATION. EVEN THE PESSIMISTS HAVE BEEN FORCED TO ACKNOWLEDGE THE DURABILITY OF THE RECOVERY. IT IS SET TO CONTINUE

/THROUGHOUT



BUDGET SECRET

THROUGHOUT THIS YEAR AT AN ANNUAL RATE OF 3 PER CENT. INFLATION IS EXPECTED TO REMAIN LOW, EDGING BACK DOWN TO 4½ PER CENT BY THE END OF THIS YEAR. WITH RISING INCOMES AND LOW INFLATION, CONSUMPTION WILL CONTINUE TO GROW. AND, ENCOURAGED BY IMPROVED PROFITABILITY AND BETTER LONG-TERM GROWTH PROSPECTS, INVESTMENT IS EXPECTED TO RISE BY A GOOD 6 PER CENT THIS YEAR.

18. LOOKING ABROAD, TOO, ECONOMIC PROSPECTS ARE MORE FAVOURABLE THAN FOR SOME TIME. OUTPUT IN THE UNITED STATES SHOULD CONTINUE TO GROW STRONGLY THIS YEAR. AND RECOVERY IS SPREADING TO THE REST OF THE WORLD.

19. OF COURSE, THERE ARE INEVITABLE RISKS AND UNCERTAINTIES. THE SIZE AND CONTINUED GROWTH OF THE UNITED STATES BUDGET DEFICIT IS A CAUSE OF WIDESPREAD CONCERN AND KEEPS INTEREST RATES HIGH, EXACERBATING THE PROBLEMS OF THE DEBTOR COUNTRIES.

/AND THE NEED



BUDGET SECRET

AND THE NEED TO FINANCE THE US DEFICIT BY INFLOWS OF FOREIGN CAPITAL HAS KEPT THE DOLLAR ARTIFICIALLY HIGH AND LED TO A MASSIVE AND GROWING TRADE DEFICIT, GREATLY INCREASING THE PRESSURES FOR PROTECTIONISM WITHIN THE UNITED STATES.

20. A SECOND POTENTIAL RISK IS DISRUPTION IN THE OIL MARKET. THE UNITED KINGDOM, AND INDEED THE WORLD ECONOMY, INEVITABLY REMAIN VULNERABLE TO ANY MAJOR DISTURBANCES IN THIS MARKET.

21. BUT DESPITE THESE RISKS THERE IS A GROWING SENSE THROUGHOUT THE INDUSTRIALISED WORLD THAT THE RECOVERY THIS TIME IS ONE WHICH CAN BE SUSTAINED. THE ESSENTIAL REQUIREMENT IS THE CONTINUED PURSUIT OF PRUDENT MONETARY AND FISCAL POLICIES.



## THE MTFS

22. FOR THE UNITED KINGDOM, THE MEDIUM TERM FINANCIAL STRATEGY HAS BEEN THE CORNERSTONE OF SUCH POLICIES. IT WILL CONTINUE TO PLAY THAT ROLE; TO PROVIDE A FRAMEWORK AND DISCIPLINE FOR GOVERNMENT AND TO SET OUT CLEARLY, TO INDUSTRY AND THE FINANCIAL MARKETS, THE GUIDELINES OF POLICY. TOO OFTEN IN THE PAST GOVERNMENTS ABANDONED FINANCIAL DISCIPLINE WHENEVER THE GOING GOT ROUGH, AND STAGGERED FROM ONE SHORT-TERM POLICY EXPEDIENT TO ANOTHER. THE TEMPTATION TO ACCOMMODATE INFLATIONARY PRESSURES PROVED IRRESISTIBLE, AND THE NATION'S LONGER-TERM ECONOMIC PERFORMANCE WAS PROGRESSIVELY UNDERMINED.

/THE MTFS WAS



BUDGET SECRET

23. THE MTFS WAS DESIGNED TO REMEDY THIS, BY IMPOSING A DISCIPLINED FINANCIAL FRAMEWORK WHICH WOULD ALSO ENSURE CONSISTENCY BETWEEN MONETARY AND FISCAL POLICIES. AND A PROPER BALANCE IN THE ECONOMY. IT IS SO DESIGNED TO ENSURE THAT THE MORE INFLATION AND INFLATIONARY EXPECTATIONS COME DOWN, THE MORE ROOM IS AVAILABLE FOR OUTPUT AND EMPLOYMENT TO GROW.

24. PEOPLE NOW KNOW THAT THE GOVERNMENT INTENDS TO STICK TO ITS MEDIUM TERM OBJECTIVES. THEY UNDERSTAND THAT THE FASTER INFLATION COMES DOWN, THE FASTER OUTPUT AND EMPLOYMENT ARE LIKELY TO RECOVER. THE INCREASING DEGREE OF REALISM AND FLEXIBILITY IN THE ECONOMY OWES MUCH TO THE PURSUIT OF FIRM AND CONSISTENT POLICIES WITHIN THE MTFS FRAMEWORK.

25. ORIGINALLY THE MTFS COVERED FOUR YEARS. IN THIS FIRST BUDGET OF A NEW PARLIAMENT IT IS

/APPROPRIATE TO



## BUDGET SECRET

APPROPRIATE TO CARRY IT FORWARD FOR FIVE YEARS. SO THE MTFS PUBLISHED TODAY IN THE FINANCIAL STATEMENT AND BUDGET REPORT -THE RED BOOK - SHOWS A CONTINUING DOWNWARD PATH FOR THE MONETARY TARGET RANGES OVER THE NEXT FIVE YEARS, AND A PATH FOR PUBLIC BORROWING CONSISTENT WITH THAT REDUCTION. IT TAKES FULL ACCOUNT OF IMPORTANT INFLUENCES SUCH AS THE PATTERN OF NORTH SEA OIL REVENUES, AND THE LEVEL OF ASSET SALES ARISING FROM THE PRIVATISATION PROGRAMME. FOR THE LAST TWO YEARS OF THE NEW MTFS, WHICH LIE BEYOND THE PERIOD COVERED IN LAST YEARS PUBLIC EXPENDITURE SURVEY AND LAST MONTH'S WHITE PAPER, THE GOVERNMENT HAS NOT YET MADE FIRM PLANS FOR PUBLIC SPENDING. BUT THE MTFS ASSUMPTION - AND AT PRESENT IT IS NO MORE THAN AN ASSUMPTION - IS THAT THE LEVEL OF PUBLIC SPENDING IN 1987-88 AND 1988-89 WILL BE THE SAME IN REAL TERMS AS THAT CURRENTLY PLANNED FOR 1986-87.

/THE PRECISE



BUDGET SECRET

26. THE PRECISE FIGURES SET OUT IN THE MTFS ARE NOT OF COURSE AN <sup>ABSOLUTELY</sup> RIGID FRAMEWORK, LACKING ALL FLEXIBILITY. AS IN THE PAST, THERE MAY WELL NEED TO BE ADJUSTMENTS TO TAKE ACCOUNT OF CHANGING CIRCUMSTANCES. BUT NO CHANGES WILL BE MADE THAT MIGHT JEOPARDISE THE CONSISTENT PURSUIT OF THE GOVERNMENT'S OBJECTIVES.



**MONETARY POLICY**

27. MONETARY POLICY WILL CONTINUE TO PLAY A CENTRAL ROLE. FURTHER REDUCTIONS IN MONETARY GROWTH ARE NEEDED TO ACHIEVE STILL LOWER INFLATION.

28. OVER THE TWELVE MONTHS TO MID-FEBRUARY THE GROWTH OF £M3 HAS BEEN WELL WITHIN THE 7-11 PER CENT TARGET RANGE, WITH M1 AND PSL2 AT OR A LITTLE ABOVE THE TOP OF IT. WHILE IN THE EARLY MONTHS OF THE TARGET PERIOD MOST MEASURES OF MONEY SHOWED SIGNS OF ACCELERATING, SINCE THE SUMMER GROWTH IN ALL THE TARGET AGGREGATES HAS BEEN COMFORTABLY WITHIN THE RANGE. AND NOMINAL INTEREST RATES HAVE CONTINUED TO DECLINE IN LINE WITH ~~FALLING~~ INFLATION.

*lower*

/OTHER EVIDENCE



BUDGET SECRET

29. OTHER EVIDENCE CONFIRMS THAT MONETARY CONDITIONS ARE SATISFACTORY. THE EFFECTIVE EXCHANGE RATE HAS REMAINED FAIRLY STABLE, DESPITE THE INTERNATIONAL UNCERTAINTIES WHICH I HAVE DESCRIBED.

30. IF MONETARY POLICY IS TO STAY ON TRACK ITS PRACTICAL IMPLEMENTATION MUST ADAPT TO CHANGES IN THE FINANCIAL SYSTEM AND IN THE SIGNIFICANCE OF DIFFERENT MEASURES OF MONEY. THERE IS NOTHING NEW IN THIS. OVER THE YEARS WE HAVE MORE THAN ONCE ALTERED THE TARGET RANGES AND AGGREGATES TO TAKE ACCOUNT OF SUCH CHANGES. BUT THE THRUST OF THE STRATEGY HAS BEEN MAINTAINED.

31. ONE IMPORTANT DEVELOPMENT HAS BEEN THE ATTEMPT TO GIVE A MORE EXPLICIT ROLE TO THE NARROW MEASURES OF MONEY.  $\text{£M3}$  AND THE OTHER BROAD AGGREGATES GIVE A GOOD INDICATION OF THE GROWTH OF LIQUIDITY. BUT A LARGE PROPORTION OF THIS MONEY IS IN REALITY A FORM

/OF SAVINGS,



BUDGET SECRET

OF SAVINGS, INVESTED FOR THE INTEREST IT CAN EARN. IN DEFINING POLICY IT IS HELPFUL ALSO TO MAKE SPECIFIC REFERENCE TO MEASURES OF MONEY WHICH RELATE MORE NARROWLY TO BALANCES HELD FOR CURRENT SPENDING.

32. IT WAS FOR THIS REASON THAT M1 WAS INTRODUCED AS A TARGET AGGREGATE, BUT IT HAS NOT PROVED ENTIRELY SATISFACTORY FOR THAT PURPOSE. WITH THE RAPID GROWTH OF INTEREST-BEARING SIGHT DEPOSITS, M1 HAS BECOME AN INCREASINGLY POOR MEASURE OF MONEY HELD TO FINANCE CURRENT SPENDING. THE SIGNS ARE THAT <sup>TREND</sup> THIS WILL CONTINUE.

33. OTHER MEASURES OF NARROW MONEY HAVE NOT BEEN DISTORTED TO THE SAME EXTENT. IN PARTICULAR, M0, WHICH CONSISTS MAINLY OF CURRENCY, IS LIKELY TO BE A BETTER INDICATOR OF FINANCIAL CONDITIONS THAN M1. THERE IS ALSO THE NEW AGGREGATE M2, WHICH WAS SPECIFICALLY DEvised TO PROVIDE A COMPREHENSIVE MEASURE OF TRANSACTIONS BALANCES. THIS MAY ALSO BE

/A USEFUL GUIDE



## BUDGET SECRET

A USEFUL GUIDE BUT, BEING NEW, STILL NEEDS TO BE INTERPRETED WITH PARTICULAR CARE.

34. IN THE PAST TWO YEARS, IT HAS BEEN POSSIBLE TO SET A SINGLE TARGET RANGE FOR BOTH BROAD AND NARROW MEASURES OF MONEY. BUT THIS WILL NOT NORMALLY BE THE CASE; FOR NARROW MONETARY AGGREGATES TEND IN THE LONG RUN TO GROW MORE SLOWLY THAN BROADER MEASURES. THUS THIS YEAR'S RED BOOK SETS OUT TWO SEPARATE (THOUGH OVERLAPPING) RANGES.

35. THE TARGET RANGE FOR BROAD MONEY WILL CONTINUE TO APPLY TO  $\text{EM3}$ , AND FOR THE COMING YEAR WILL BE SET AT 6-10 PER CENT, AS INDICATED IN LAST YEAR'S MTF'S. THE TARGET RANGE FOR NARROW MONEY WILL APPLY TO  $\text{M0}$  AND FOR NEXT YEAR WILL BE SET AT 4-8 PER CENT. TO AVOID ANY POSSIBLE MISUNDERSTANDING, LET ME STRESS THAT THE USE OF  $\text{M0}$  AS A TARGET AGGREGATE WILL NOT INVOLVE ANY CHANGE IN METHODS OF MONETARY CONTROL.

/THE TWO TARGET



BUDGET SECRET

36. THE TWO TARGET AGGREGATES WILL HAVE EQUAL IMPORTANCE IN THE CONDUCT OF POLICY. AND THE AUTHORITIES WILL CONTINUE TO TAKE INTO ACCOUNT OTHER MEASURES OF MONEY, ESPECIALLY M2 AND PSL2, WHICH INCLUDE BUILDING SOCIETY LIABILITIES, AS WELL AS WIDER EVIDENCE OF FINANCIAL CONDITIONS, INCLUDING THE EXCHANGE RATE. AS IN THE PAST, MONETARY CONDITIONS WILL BE KEPT UNDER CONTROL BY AN APPROPRIATE COMBINATION OF FUNDING AND OPERATIONS IN THE MONEY MARKET.

37. SO FAR AS FUNDING IS CONCERNED, THE PUBLIC SECTOR'S BORROWING REQUIREMENT, AS I SHALL SHORTLY EXPLAIN, WILL BE SIGNIFICANTLY LOWER IN THE COMING YEAR. IN FINANCING IT, THE ROLE OF THE NATIONAL SAVINGS WILL REMAIN IMPORTANT. THIS YEAR'S NATIONAL SAVING'S TARGET OF £3 BILLION IS LIKELY TO BE ACHIEVED: THE TARGET FOR THE COMING YEAR WILL AGAIN BE £3 BILLION.

/PRECISE MONETARY



BUDGET SECRET

38. PRECISE MONETARY TARGETS FOR THE LATER YEARS WILL BE DECIDED NEARER THE TIME. BUT TO GIVE A BROAD INDICATION OF THE OBJECTIVES OF MONETARY POLICY, THE NEW MTF'S, LIKE PREVIOUS VERSIONS, SHOWS MONETARY RANGES FOR A NUMBER OF YEARS AHEAD. THESE RANGES ARE CONSISTENT WITH A CONTINUING DOWNWARD TREND IN INFLATION: THEY DEMONSTRATE THE GOVERNMENT'S INTENTION TO MAKE FURTHER PROGRESS TOWARDS STABLE PRICES.



**PUBLIC SECTOR BORROWING**

39. I TURN NOW TO PUBLIC BORROWING. JUST AS THE CLASSICAL FORMULA FOR FINANCIAL DISCIPLINE -THE GOLD STANDARD AND THE BALANCED BUDGET - HAD BOTH A MONETARY AND A FISCAL COMPONENT, SO DOES THE MEDIUM TERM FINANCIAL STRATEGY.

40. THE MTFS HAS ALWAYS ENVISAGED THAT THE PUBLIC SECTOR BORROWING REQUIREMENT WOULD FALL AS A PERCENTAGE OF GROSS DOMESTIC PRODUCT OVER THE MEDIUM TERM. BY 1981-82 WE HAD BROUGHT IT DOWN TO 3½ PER CENT OF GDP.

41. SINCE THEN THERE HAS BEEN LITTLE FURTHER FALL. THE LATEST ESTIMATE OF THE PSBR FOR THE CURRENT YEAR, 1983-84, REMAINS WHAT IT WAS IN NOVEMBER:

/AROUND £10 BILLION



BUDGET SECRET

AROUND £10 BILLION, EQUIVALENT TO  $3\frac{1}{4}$  PER CENT OF GDP. THIS IS SIGNIFICANTLY ABOVE WHAT WAS INTENDED AT THE TIME OF LAST YEAR'S BUDGET, AND WOULD OF COURSE HAVE BEEN HIGHER STILL HAD IT NOT BEEN FOR THE JULY MEASURES.

42. WE NOW NEED A FURTHER SUBSTANTIAL REDUCTION IN BORROWING, IN ORDER TO HELP BRING INTEREST RATES DOWN FURTHER AS MONETARY GROWTH SLOWS DOWN. STERLING INTEREST RATES ARE, OF COURSE, ALSO INFLUENCED BY DOLLAR INTEREST RATES; BUT THAT MAKES IT ALL THE MORE IMPORTANT TO CURB DOMESTIC PRESSURES. IN CONTRAST TO VIRTUALLY THE WHOLE OF THE POST-WAR PERIOD, UK LONGER-TERM RATES ARE NOW ~~LONGER THAN~~ AMERICAN RATES. AS LONG AS AMERICAN RATES REMAIN NEAR THEIR CURRENT LEVEL, IT IS HIGHLY DESIRABLE THAT THIS ADVANTAGE BE MAINTAINED.

*Also shorter  
BELOW*

43. THE HIGHER LEVEL OF ASSET SALES WE ARE PLANNING AS THE PRIVATISATION PROGRAMME GATHERS PACE IS A

/FURTHER REASON



BUDGET SECRET

FURTHER REASON FOR REDUCING THE PSBR SIGNIFICANTLY IN THE COMING YEAR. ASSET SALES REDUCE THE GOVERNMENT'S NEED TO BORROW. BUT THEIR EFFECT ON INTEREST RATES MAY BE LESS THAN THE EFFECT OF MOST OTHER REDUCTIONS IN GOVERNMENT SPENDING PROGRAMMES.

44. LAST YEAR'S MTFS SHOWED AN ILLUSTRATIVE PSBR FOR 1984-85 OF 2½ PER CENT OF GDP, EQUIVALENT TO AROUND £8 MILLION. BUT I BELIEVE THAT IT IS POSSIBLE, AND INDEED PRUDENT, TO AIM FOR A SOMEWHAT LOWER FIGURE. I AM THEREFORE PROVIDING FOR A PSBR NEXT YEAR OF 2¼ PER CENT OF GDP, OR £7¼ BILLION.

45. THE HOUSE WILL RECALL THAT IN NOVEMBER I WARNED THAT ON CONVENTIONAL ASSUMPTIONS, INCLUDING THE 1983 RED BOOK'S PSBR FIGURE OF £8 BILLION FOR NEXT YEAR, I MIGHT HAVE TO INCREASE TAXES SLIGHTLY IN THE BUDGET. I AM GLAD TO REPORT THAT THE LATEST, AND MORE BUOYANT, FORECASTS OF TAX REVENUE IN THE COMING YEAR HAVE IMPROVED THE PICTURE. A PSBR OF

/£7¼ BILLION



BUDGET SECRET

£7½ BILLION WILL REQUIRE NO OVERALL NET INCREASE TAXATION.

*? nearly £2bn*

46. MOREOVER, WHILE THE MEASURES I SHALL SHORTLY ANNOUNCE WILL, AFTER INDEXATION, BE BROADLY NEUTRAL IN THEIR EFFECTS ON REVENUE IN 1984-85, THEY WILL REDUCE TAXATION IN 1985-86 BY WELL OVER £1½ BILLION. AND THE MTFS PUBLISHED TODAY SHOWS THAT THERE SHOULD BE ROOM FOR FURTHER TAX CUTS NOT ONLY IN 1985-86, BUT THROUGHOUT THE REMAINDER OF THIS PARLIAMENT, PROVIDED THAT WE STICK FIRMLY TO OUR PUBLISHED PLANS FOR PUBLIC EXPENDITURE TO 1986-87, AND MAINTAIN AN EQUALLY FIRM CONTROL OF PUBLIC SPENDING THEREAFTER.



**PUBLIC EXPENDITURE**

47. THE PUBLIC EXPENDITURE WHITE PAPER SETTING OUT OUR SPENDING PLANS FOR THE NEXT THREE YEARS WAS APPROVED BY THE HOUSE LAST WEEK. TODAY I WANT TO CONSIDER THE IMPORTANT ISSUE OF GOVERNMENT SPENDING IN A RATHER WIDER PERSPECTIVE.

48. FOR FAR TOO LONG, PUBLIC SPENDING HAS GROWN FASTER THAN THE ECONOMY AS A WHOLE. AS A RESULT, THE TAX BURDEN HAS STEADILY INCREASED AND INCOME TAX HAS EXTENDED STEADILY LOWER DOWN THE WAGE SCALE.

49. WE HAVE SEEN A MASSIVE ENLARGEMENT IN THE ROLE OF THE STATE, AT THE EXPENSE OF THE INDIVIDUAL, AND A CORRESPONDING INCREASE IN THE DEAD WEIGHT OF TAXATION HOLDING BACK OUR ECONOMIC PROGRESS AS A NATION.

/THIS PROCESS



BUDGET SECRET

50. THIS PROCESS HAS TO STOP. BUT IT HAS ARISEN BECAUSE MUCH PUBLIC SPENDING IS DIRECTED TO EMINENTLY DESIRABLE ENDS. THIS RAISES DIFFICULT ISSUES WHICH DESERVE THE WIDEST POSSIBLE CONSIDERATION AND DEBATE.

51. THE GOVERNMENT IS THEREFORE PUBLISHING TODAY, IN ADDITION TO THE CUSTOMARY BUDGET DOCUMENTS, A GREEN PAPER ON THE PROSPECTS FOR PUBLIC SPENDING AND TAXATION OVER THE NEXT TEN YEARS. IT EXAMINES PAST TRENDS; DISCUSSES THE PRESSURES FOR STILL HIGHER SPENDING; AND EXAMINES THE REWARDS FOR THE INDIVIDUAL AND THE BENEFITS FOR THE ECONOMY IF THESE PRESSURES CAN BE CONTAINED.

52. THE GREEN PAPER CONCLUDES THAT, WITHOUT FIRM CONTROL OVER PUBLIC SPENDING, THERE CAN BE NO PROSPECT OF BRINGING THE BURDEN OF TAX BACK TO MORE REASONABLE LEVELS. ON THE ASSUMPTIONS MADE IN THE GREEN PAPER, THE BURDEN OF TAXATION WILL BE REDUCED

/TO THE LEVELS



BUDGET SECRET

TO THE LEVELS OF THE EARLY 1970s ONLY IF PUBLIC SPENDING IS KEPT BROADLY STABLE IN REAL TERMS OVER THE NEXT TEN YEARS.

53. THE GOVERNMENT BELIEVES THAT THE ISSUES DISCUSSED IN THE GREEN PAPER MERIT THE ATTENTION OF THE HOUSE AND THE COUNTRY.

54. IN CONTRAST TO PREVIOUS YEARS, I HAVE NO PACKAGE OF PUBLIC EXPENDITURE MEASURES TO ANNOUNCE IN THIS BUDGET. THE WHITE PAPER PLANS STAND.

55. I CAN HOWEVER MAKE ONE ANNOUNCEMENT, WHICH I THINK THE HOUSE WILL WELCOME. WITHIN THE PUBLISHED PLANS THE GOVERNMENT HAVE BEEN ABLE TO PROVIDE THE NATIONAL HERITAGE MEMORIAL FUND WITH ADDITIONAL RESOURCES WHICH WILL ENABLE THEM AMONG OTHER THINGS TO SECURE THE FUTURE OF CALKE ABBEY. MY RT HON FRIEND THE SECRETARY OF STATE FOR THE ENVIRONMENT WILL BE ANNOUNCING THE DETAILS SHORTLY.

/THE HOUSE WILL



BUDGET SECRET

56. THE HOUSE WILL RECALL THAT PROPOSALS FOR THE NEW RATES OF SOCIAL SECURITY BENEFIT TO COME INTO FORCE IN NOVEMBER ARE NOT NOW MADE AT THE TIME OF THE BUDGET. FOLLOWING LAST YEAR'S LEGISLATION TO RETURN TO THE HISTORIC METHOD OF UPDATING, PRICE PROTECTION IS MEASURED BY REFERENCE TO THE RETAIL PRICE INDEX FOR MAY. MY RT HON FRIEND THE SECRETARY OF STATE FOR SOCIAL SERVICES WILL BE ANNOUNCING THE NEW RATES OF SOCIAL SECURITY BENEFITS, INCLUDING CHILD BENEFIT, WHEN THE MAY RPI IS KNOWN.

57. BEFORE LEAVING GOVERNMENT SPENDING, I SHOULD ADD A WORD ON PUBLIC SECTOR MANPOWER. AT THE BEGINNING OF THE LAST PARLIAMENT, THE GOVERNMENT SET ITSELF THE TARGET OF REDUCING THE SIZE OF THE CIVIL SERVICE FROM 732,000 IN APRIL 1979 TO 630,000 BY APRIL OF THIS YEAR. THAT TARGET WILL BE ACHIEVED. WE HAVE NOW SET OURSELVES THE FURTHER TARGET OF 593,000 BY APRIL 1988. I AM CONFIDENT THAT A

/SMALLER CIVIL



BUDGET SECRET

SMALLER CIVIL SERVICE WILL CONTINUE TO IMPROVE ITS EFFICIENCY. THE TAX CHANGES I SHALL BE ANNOUNCING TODAY WILL REDUCE MANPOWER REQUIREMENTS BY AT LEAST 1,000 IN MY OWN DEPARTMENTS, WHICH WILL HELP TOWARDS MEETING THE 1988 TARGET.



**TAX REFORM**

58. I MENTIONED AT THE OUTSET THAT THIS WILL BE A RADICAL, TAX-REFORMING, BUDGET. IT WILL ALSO SIGNIFICANTLY REDUCE THE OVERALL BURDEN OF TAX OVER THE NEXT TWO YEARS TAKEN TOGETHER. AND I HOPE TO HAVE SCOPE FOR FURTHER REDUCTIONS IN SUBSEQUENT BUDGETS.

59. MY PROPOSALS FOR REFORM ARE GUIDED BY TWO BASIC PRINCIPLES. FIRST, THE NEED TO MAKE CHANGES THAT WILL IMPROVE OUR ECONOMIC PERFORMANCE OVER THE LONGER TERM. SECOND, THE DESIRE TO MAKE LIFE A LITTLE SIMPLER FOR THE TAXPAYER.

60. BUT I AM WELL AWARE THAT THE TAX REFORMER'S PATH IS A STONY ONE. ANY CHANGE IN THE SYSTEM IS BOUND, AT LEAST IN THE SHORT TERM, TO BRING BENEFITS

/TO SOME AND



## BUDGET SECRET

TO SOME AND DISADVANTAGES TO OTHERS. AND THE DISAPPROVAL OF THE LATTER GROUP TENDS TO BE RATHER MORE AUDIBLE THAN THE MURMURINGS OF SATISFACTION FROM THE FORMER.

61. SOME COMMENTATORS HAVE SUGGESTED THAT OUR ENTIRE INCOME-BASED TAX SYSTEM SHOULD BE REPLACED WITH AN EXPENDITURE-BASED SYSTEM. EVEN IF A ROOT-AND-BRANCH CHANGE OF THIS KIND WERE DESIRABLE, IT WOULD, I BELIEVE, BE WHOLLY IMPRACTICAL AND UNREALISTIC.

62. BUT I DO NOT BELIEVE WE CAN AFFORD TO OPT FOR THE QUIET LIFE AND DO NOTHING. SO I HAVE CHOSEN THE MIDDLE WAY: TO INTRODUCE REFORMS, SOME OF THEM OF A MAJOR NATURE, WITHIN THE FRAMEWORK OF OUR EXISTING INCOME-BASED SYSTEM. I SHALL ALSO BE PROPOSING TRANSITIONAL ARRANGEMENTS WHERE I BELIEVE IT FAIR AND APPROPRIATE TO DO SO.

/THE CHANGES



BUDGET SECRET

63. THE CHANGES I SHALL BE PROPOSING TODAY FALL INTO THREE BROAD CATEGORIES. THESE ARE THE TAXATION OF SAVINGS AND INVESTMENT, BUSINESS TAXATION, AND THE TAXATION OF PERSONAL INCOME AND SPENDING.



**SAVINGS AND INVESTMENT**

64. FIRST, THE TAXATION OF SAVINGS AND INVESTMENT. THE PROPOSALS I AM ABOUT TO MAKE SHOULD IMPROVE THE DIRECTION AND QUALITY OF BOTH. AND THEY WILL CONTRIBUTE FURTHER TO THE CREATION OF A PROPERTY-OWNING AND SHARE-OWING DEMOCRACY, IN WHICH MORE DECISIONS ARE MADE BY INDIVIDUALS RATHER THAN BY INTERMEDIARY INSTITUTIONS.

65. I START WITH STAMP DUTY. THIS WAS DOUBLED FROM ITS LONG-STANDING 1 PER CENT BY THE POST-WAR LABOUR GOVERNMENT IN 1947, REDUCED BY THE MACMILLAN GOVERNMENT IN 1963, AND ONCE AGAIN DOUBLED TO 2 PER CENT BY LABOUR IN THE FIRST BUDGET PRESENTED BY THE RT HON MEMBER FOR LEEDS EAST IN 1974. AT ITS PRESENT LEVEL IT IS AN IMPEDIMENT TO MOBILITY AND

/INCOMPATIBLE



BUDGET SECRET

INCOMPATIBLE WITH THE FORCES OF COMPETITION NOW AT WORK IN THE CITY, FOLLOWING THE WITHDRAWAL OF THE STOCK EXCHANGE CASE FROM THE RESTRICTIVE PRACTICES COURT.

66. I THEREFORE PROPOSE TO HALVE THE RATE OF STAMP DUTY TO 1 PER CENT. WITH THE EXCEPTION OF THOSE DOCUMENTS WHICH HAVE TO BE STAMPED BEFORE 20 MARCH, THE CHANGE WILL TAKE EFFECT FROM TODAY.

67. FOR THE HOME BUYER, THE NEW FLAT RATE 1 PER CENT STAMP DUTY WILL START AT £30,000. BELOW THIS LEVEL NO DUTY WILL BE PAYABLE. AS A RESULT OF THIS £5,000 INCREASE IN THE THRESHOLD, 90 PER CENT OF FIRST TIME HOME BUYERS WILL NOT HAVE TO PAY STAMP DUTY AT ALL.

68. REDUCING THE RATE OF DUTY ON SHARE TRANSFERS WILL REMOVE AN ~~IMPORTANT~~ DISINCENTIVE TO INVESTMENT IN EQUITIES AND INCREASE THE

/INTERNATIONAL



BUDGET SECRET

INTERNATIONAL COMPETITIVENESS OF OUR STOCK MARKET. IT SHOULD ALSO HELP BRITISH COMPANIES TO RAISE EQUITY FINANCE.

69. IN ADDITION, I HAVE THREE PROPOSALS TO ENCOURAGE THE ISSUE OF CORPORATE BONDS. I SHALL GO AHEAD WITH THE NEW ARRANGEMENTS FOR DEEP DISCOUNT STOCK AND THE RELIEFS FOR COMPANIES ISSUING EURO BONDS AND CONVERTIBLE LOAN STOCK WHICH WERE ANNOUNCED BUT NOT ENACTED LAST YEAR. AND I PROPOSE TO EXEMPT FROM CAPITAL GAINS TAX MOST CORPORATE FIXED INTEREST SECURITIES PROVIDED THEY ARE HELD FOR MORE THAN A YEAR. SINCE SUCH SECURITIES ARE ALREADY EXEMPT FROM STAMP DUTY THIS MEANS THAT THE TAX CONCESSIONS FOR PRIVATE SECTOR BORROWING IN THE CORPORATE BOND MARKET WILL NOW BE VIRTUALLY THE SAME AS FOR GOVERNMENT BORROWING IN THE GILT-EDGED MARKET.

/THE REDUCTIONS



BUDGET SECRET

70. THE REDUCTIONS IN STAMP DUTY WILL COST £450 MILLION IN 1984-85, OF WHICH £160 MILLION IS THE COST OF THE RELIEF ON SHARE TRANSFERS, AND £290 MILLION THE COST OF THE RELIEF ON TRANSFERS OF HOUSES AND OTHER BUILDINGS AND LAND.

71. NEXT, LIFE ASSURANCE. THE MAIN EFFECT OF LIFE ASSURANCE PREMIUM RELIEF TODAY IS UNDULY TO FAVOUR INSTITUTIONAL RATHER THAN DIRECT INVESTMENT. IT HAS ALSO SPAWNED A MULTIPLICITY OF WELL-ADVERTISED TAX MANAGEMENT SCHEMES. I THEREFORE PROPOSE TO WITHDRAW THE RELIEF ON ALL NEW CONTRACTS MADE AFTER TODAY. <sup>X</sup> I STRESS THAT THIS CHANGE WILL APPLY ONLY TO NEW (OR NEWLY ENHANCED) POLICIES, TAKEN OUT OR INCREASED AFTER TODAY. EXISTING POLICIES WILL NOT BE AFFECTED AT ALL. THE CHANGE IS ESTIMATED TO YIELD ABOUT £90 MILLION IN 1984-85.

72. I AM ALSO PROPOSING TO WITHDRAW THE SPECIAL - BUT UNFORTUNATELY WIDELY ABUSED - PRIVILEGES FOR

/WHAT ARE KNOWN

*X But policies which still meet criteria and thus will continue to benefit from pegged rate and tax free proceeds on maturity*



BUDGET SECRET

WHAT ARE KNOWN AS 'TAX EXEMPT' FRIENDLY SOCIETIES, AND BRING THEM INTO LINE WITH THE NORMAL RULES FOR FRIENDLY SOCIETIES DOING 'MIXED' BUSINESS. HOWEVER THE LIMITS WITHIN WHICH IN FUTURE ALL FRIENDLY SOCIETIES WILL BE ABLE TO WRITE ASSURANCE ON A TAX EXEMPT BASIS WILL BE INCREASED FROM £500 TO £750.

73. I HAVE ALSO REVIEWED THE TAX TREATMENT OF DIRECT PERSONAL INVESTMENT. THE INVESTMENT INCOME SURCHARGE IS AN UNFAIR AND ANOMALOUS TAX ON SAVINGS AND ON THE REWARDS OF SUCCESSFUL ENTERPRISE. IT HITS THE SMALL BUSINESSMAN WHO REACHES RETIREMENT WITHOUT THE CUSHION OF A COMPANY PENSION SCHEME, AND IMPEDES THE CREATION OF FARM TENANCIES. IN THE VAST MAJORITY OF CASES IT IS A TAX ON SAVINGS MADE OUT OF HARD-EARNED AND FULLY-TAXED INCOME. MORE THAN HALF OF THOSE WHO PAY THE INVESTMENT INCOME SURCHARGE ARE OVER 65, AND OF THESE HALF WOULD OTHERWISE BE LIABLE TO TAX AT ONLY THE BASIC RATE.

/I HAVE THEREFORE



BUDGET SECRET

74. I HAVE THEREFORE DECIDED THAT THE INVESTMENT INCOME SURCHARGE SHOULD BE ABOLISHED. THE COST IN 1984-85 WILL BE SOME £25 MILLION, BUILDING UP TO £360 MILLION IN A FULL YEAR.

75. FINALLY, I PROPOSE TO DRAW MORE CLOSELY TOGETHER THE TAX TREATMENT OF DEPOSITORS IN BANKS AND BUILDING SOCIETIES. THESE INSTITUTIONS COMPETE IN THE SAME MARKET FOR PERSONAL DEPOSITS. I BELIEVE THAT THEY SHOULD BE ABLE TO DO SO ON MORE EQUAL TERMS AS FAR AS TAX IS CONCERNED. ONE SOURCE OF UNEQUAL TREATMENT HAS ALREADY BEEN REMOVED, WITH THE RECENT CHANGE MADE ON LEGAL ADVICE IN THE TAX TREATMENT OF BUILDING SOCIETIES' PROFITS FROM GILT-EDGED SECURITIES. THEY ARE NOW TREATED IN THE SAME WAY AS THOSE OF THE BANKS HAVE ALWAYS BEEN.

/BUT THE MAJOR



BUDGET SECRET

76. BUT THE MAJOR SOURCE OF UNEQUAL TREATMENT, AGAINST WHICH THE BANKS IN PARTICULAR HAVE FREQUENTLY COMPLAINED, IS THE SPECIAL ARRANGEMENT FOR INTEREST PAID BY BUILDING SOCIETIES. THE SOCIETIES PAY TAX AT A SPECIAL RATE - THE "COMPOSITE RATE" - ON THE INTEREST PAID TO THE DEPOSITOR, WHO RECEIVES CREDIT FOR INCOME TAX AT THE FULL BASIC RATE.

77. THIS SYSTEM, WHICH HAS WORKED WELL FOR THE PAST 90 YEARS, HAS BOTH AN ADVANTAGE AND A DISADVANTAGE. THE DISADVANTAGE IS THAT A MINORITY OF DEPOSITORS, WHO ARE BELOW THE INCOME TAX THRESHOLD, STILL HAVE TAX DEDUCTED AT THE COMPOSITE RATE. IT HAS NOT HOWEVER STOPPED MANY OF THEM USING BUILDING SOCIETIES BECAUSE OF THE COMPETITIVE RATES THEY HAVE OFFERED. THE ADVANTAGE OF THE SCHEME IS ITS EXTREME SIMPLICITY, PARTICULARLY FOR THE TAXPAYER; MOST TAXPAYERS ARE SPARED THE BOTHER OF PAYING TAX ON INTEREST THROUGH PAYE OR INDIVIDUAL ASSESSMENT,

/WHILE THE REVENUE



BUDGET SECRET

WHILE THE REVENUE ARE SPARED THE NEED TO RECRUIT UP TO 2000 EXTRA STAFF TO COLLECT THE TAX DUE ON INTEREST PAID WITHOUT DEDUCTION.

78. IN COMMON WITH MY PREDECESSORS OF ALL PARTIES OVER THE PAST 90 YEARS, I AM SATISFIED THAT THE ADVANTAGE OF THE COMPOSITE RATE ARRANGEMENT OUTWEIGHS THE DISADVANTAGE. IT FOLLOWS THAT EQUAL TREATMENT OF BUILDING SOCIETIES AND BANKS SHOULD BE ACHIEVED, NOT BY REMOVING THE COMPOSITE RATE FROM THE SOCIETIES, BUT BY EXTENDING IT TO THE BANKS AND OTHER LICENSED DEPOSIT TAKERS.

79. NON-TAXPAYERS WILL CONTINUE TO BE ABLE TO RECEIVE INTEREST GROSS, SHOULD THEY WISH TO DO SO, BY PUTTING THEIR MONEY INTO APPROPRIATE NATIONAL SAVINGS FACILITIES. BUT THE PURPOSE OF THE MOVE IS NOT, OF COURSE, TO ATTRACT SAVINGS INTO GOVERNMENT HANDS: AS I HAVE ALREADY ANNOUNCED, NEXT YEAR'S TARGET FOR NATIONAL SAVINGS WILL BE THE SAME AS THIS

/YEAR'S AND



BUDGET SECRET

YEAR'S AND LAST YEAR'S; AND THE TOTAL GOVERNMENT APPETITE FOR SAVINGS, WHICH IS MEASURED BY THE SIZE OF THE PUBLIC SECTOR BORROWING REQUIREMENT, IS BEING SIGNIFICANTLY REDUCED.

80. THE TRUE PURPOSE OF THE MOVE IS SIMPLE: FAIRER COMPETITION AND SIMPLICITY ITSELF. UNLESS THEY ARE HIGHER RATE TAXPAYERS, INDIVIDUAL BANK CUSTOMERS WILL, WHEN IT COMES TO TAX, BE ABLE TO FORGET ABOUT BANK INTEREST ALTOGETHER, FOR ALL THE TAX DUE ON IT WILL ALREADY HAVE BEEN PAID. AND IT WILL BE EASIER FOR PEOPLE TO COMPARE THE TERMS OFFERED FOR THEIR SAVINGS BY BANKS AND BUILDING SOCIETIES. THERE WILL BE NO DIRECT GAIN TO THE EXCHEQUER. HOWEVER, THE INLAND REVENUE WILL BE ABLE TO MAKE STAFF SAVINGS OF UP TO AN EXTRA 1000 CIVIL SERVANTS. MOREOVER, THIS FIGURE TAKES NO ACCOUNT OF THE SUBSTANTIAL NUMBERS OF ADDITIONAL INLAND REVENUE STAFF WHO WOULD HAVE BEEN REQUIRED TO OPERATE THE PRESENT SYSTEM AS THE TREND TOWARDS THE PAYMENT OF INTEREST ON CURRENT ACCOUNTS DEVELOPS.

Still enters  
in tax  
returns

/ACCORDINGLY,



BUDGET SECRET

81. ACCORDINGLY, I PROPOSE TO EXTEND THE COMPOSITE RATE ARRANGEMENTS TO INTEREST RECEIVED BY UK RESIDENT INDIVIDUALS FROM BANKS AND OTHER LICENSED DEPOSIT TAKERS WITH EFFECT FROM 1985-86. THE COMPOSITE RATE WILL NOT APPLY EITHER TO NON-RESIDENTS OR TO THE CORPORATE SECTOR. ARRANGEMENTS WILL ALSO BE MADE TO EXCLUDE FROM THE SCHEME CERTIFICATES OF DEPOSIT AND TIME DEPOSITS OF £50,000 OR MORE.

82. TAKEN TOGETHER, THE MAJOR PROPOSALS I HAVE JUST ANNOUNCED ON STAMP DUTY, LIFE ASSURANCE PREMIUM RELIEF, THE INVESTMENT INCOME SURCHARGE, AND THE COMPOSITE RATE, COUPLED WITH OTHER MINOR PROPOSALS, WILL PROVIDE A SIMPLER AND MORE STRAIGHTFORWARD TAX SYSTEM FOR SAVINGS AND INVESTMENT. THEY WILL REMOVE BIASES WHICH HAVE DISCOURAGED THE INDIVIDUAL SAVER FROM INVESTING DIRECTLY IN INDUSTRY. AND THEY WILL REINFORCE THE GOVERNMENT'S POLICY OF ENCOURAGING COMPETITION IN THE FINANCIAL SECTOR, AS IN THE ECONOMY AS A WHOLE.



**BUSINESS TAXATION**

83. I NOW TURN TO BUSINESS TAXATION. HERE, GOVERNMENT HAS TWO RESPONSIBILITIES TOWARDS BRITISH BUSINESS AND INDUSTRY. THE FIRST IS TO ENSURE THAT THEY DO NOT HAVE TO BEAR AN EXCESSIVE BURDEN OF TAXATION. THE SECOND IS TO ENSURE THAT, GIVEN A PARTICULAR BURDEN, IT IS STRUCTURED IN THE WAY THAT DOES LEAST DAMAGE TO THE NATION'S ECONOMIC PERFORMANCE.

84. THE MEASURES I AM ANNOUNCING TODAY WILL, TAKING THE NEXT TWO YEARS TOGETHER, RESULT IN A SUBSTANTIAL REDUCTION IN THE BURDEN OF TAXATION ON BRITISH BUSINESS. AND IN ADDITION I SHALL BE PROPOSING A FAR-REACHING REFORM OF THE STRUCTURE OF COMPANY TAXATION.

/RESPONSES TO THE



BUDGET SECRET

85. RESPONSES TO THE CORPORATION TAX GREEN PAPER IN 1982 SHOWED A STRONG GENERAL DESIRE TO RETAIN THE IMPUTATION SYSTEM. I ACCEPT THAT. BUT OTHER CHANGES ARE NEEDED.

86. THE CURRENT RATES OF CORPORATION TAX ARE FAR TOO HIGH, PENALISING PROFIT AND SUCCESS, AND BLUNTING THE CUTTING EDGE OF ENTERPRISE. THEY ARE THE PRODUCT OF TOO MANY SPECIAL RELIEFS, INDISCRIMINATELY APPLIED AND OF DIMINISHING RELEVANCE TO THE CONDITIONS OF TODAY. SOME OF THESE RELIEFS REFLECT ECONOMIC PRIORITIES OR CIRCUMSTANCES WHICH HAVE LONG VANISHED, AND NOW SERVE ONLY TO DISTORT INVESTMENT DECISIONS AND CHOICES ABOUT FINANCE. OTHERS WERE INTRODUCED TO MEET SHORT-TERM PRESSURES, NOTABLY THE UPWARD SURGE OF INFLATION. WITH INFLATION DOWN TO TODAY'S LOW LEVELS, THIS IS CLEARLY THE TIME TO TAKE A FRESH LOOK. AND WITH UNEMPLOYMENT AS HIGH AS IT IS TODAY, IT IS PARTICULARLY DIFFICULT TO JUSTIFY A TAX SYSTEM

/WHICH ENCOURAGES



BUDGET SECRET

WHICH ENCOURAGES LOW-YIELDING OR EVEN LOSS-MAKING INVESTMENT AT THE EXPENSE OF JOBS.

87. MY PURPOSE THEREFORE IS TO PHASE OUT SOME UNNECESSARY RELIEFS, IN ORDER TO BRING ABOUT, OVER TIME, A MARKEDLY LOWER RATE OF TAX ON COMPANY PROFITS.

88. FIRST, CAPITAL ALLOWANCES. OVER VIRTUALLY THE WHOLE OF THE POST-WAR PERIOD THERE HAVE BEEN INCENTIVES FOR INVESTMENT IN BOTH PLANT AND MACHINERY AND INDUSTRIAL (THOUGH NOT COMMERCIAL) BUILDINGS. BUT THERE IS LITTLE EVIDENCE THAT THESE INCENTIVES HAVE STRENGTHENED THE ECONOMY OR IMPROVED THE QUALITY OF INVESTMENT. QUITE THE CONTRARY: THE EVIDENCE SUGGESTS THAT BUSINESSES HAVE INVESTED SUBSTANTIALLY IN ASSETS YIELDING A LOWER RATE OF RETURN THAN THE INVESTMENTS MADE BY OUR PRINCIPAL COMPETITORS. TOO MUCH OF BRITISH INVESTMENT HAS BEEN MADE BECAUSE THE TAX ALLOWANCES

/MAKE IT LOOK



BUDGET SECRET

MAKE IT LOOK PROFITABLE, RATHER THAN BECAUSE IT WOULD BE TRULY PRODUCTIVE. WE NEED INVESTMENT DECISIONS BASED ON FUTURE MARKET ASSESSMENTS, NOT FUTURE TAX ASSESSMENTS.

89. I PROPOSE TO RESTRUCTURE THE CAPITAL ALLOWANCES IN THREE ANNUAL STAGES. IN THE CASE OF PLANT AND MACHINERY, AND ASSETS WHOSE ALLOWANCES ARE LINKED WITH THEM, THE FIRST YEAR ALLOWANCE WILL BE REDUCED FROM 100 PER CENT TO 75 PER CENT FOR ALL SUCH EXPENDITURE INCURRED AFTER TODAY, AND TO 50 PER CENT FOR EXPENDITURE INCURRED AFTER 31 MARCH NEXT YEAR. AFTER 31 MARCH 1986 THERE WILL BE NO FIRST YEAR ALLOWANCES, AND ALL EXPENDITURE ON PLANT AND MACHINERY WILL QUALIFY FOR ANNUAL ALLOWANCES ON A 25 PER CENT REDUCING BALANCE BASIS.

90. IN ADDITION, FROM NEXT YEAR ANNUAL ALLOWANCES WILL BE GIVEN AS SOON AS THE EXPENDITURE IS INCURRED, AND NOT, AS THEY ARE TODAY, WHEN THE ASSET

/COMES INTO USE.



BUDGET SECRET

COMES INTO USE. THIS WILL BRING FORWARD THE ENTITLEMENT TO ANNUAL ALLOWANCES FOR THOSE ASSETS, SUCH AS SHIPS AND OIL RIGS, FOR WHICH SOME PAYMENT IS NORMALLY MADE WELL BEFORE THEY ARE BROUGHT INTO USE.

91. FOR INDUSTRIAL BUILDINGS, I PROPOSE THAT THE INITIAL ALLOWANCE SHOULD FALL FROM 75 PER CENT TO 50 PER CENT FROM TONIGHT, AND BE FURTHER REDUCED TO 25 PER CENT FROM 31 MARCH NEXT YEAR. AFTER 31 MARCH 1986 THE INITIAL ALLOWANCE WILL BE ABOLISHED, AND EXPENDITURE WILL BE WRITTEN OFF ON AN ANNUAL 4 PER CENT STRAIGHT LINE BASIS. I SHOULD ADD THAT, WHEN THESE CHANGES HAVE ALL TAKEN PLACE, TAX ALLOWANCES FOR BOTH PLANT AND MACHINERY AND INDUSTRIAL BUILDINGS WILL STILL ON AVERAGE BE RATHER MORE GENEROUS THAN WOULD BE PROVIDED BY A STRICT SYSTEM OF ECONOMIC DEPRECIATION.

/THE CHANGES



BUDGET SECRET

92. THE CHANGES IN THE RATES OF ALLOWANCES WILL NOT APPLY TO PAYMENTS UNDER BINDING CONTRACTS ENTERED INTO ON OR BEFORE TODAY, PROVIDED THAT THE EXPENDITURE IS INCURRED WITHIN THE NEXT THREE YEARS.

93. THERE WILL BE TRANSITIONAL TAX ARRANGEMENTS FOR CERTAIN INVESTMENT PROJECTS IN THE DEVELOPMENT AREAS AND SPECIAL DEVELOPMENT AREAS. WHEN A PROJECT IN THOSE AREAS HAS HAD AN OFFER OF INDUSTRY ACT SELECTIVE FINANCIAL ASSISTANCE AND ALSO ATTRACTS REGIONAL DEVELOPMENT GRANTS, THE EXISTING CAPITAL ALLOWANCES WILL CONTINUE TO APPLY TO THE EXPENDITURE TO WHICH THE SELECTIVE ASSISTANCE IS RELATED. THESE ARRANGEMENTS WILL COVER PROJECTS FOR WHICH OFFERS HAVE ALREADY BEEN MADE BETWEEN 1 APRIL 1980 AND TODAY. SIMILAR ARRANGEMENTS FOR REGIONAL DEVELOPMENT GRANTS WERE ANNOUNCED BY MY RT. HON. FRIEND THE SECRETARY OF STATE FOR TRADE AND INDUSTRY IN HIS WHITE PAPER LAST DECEMBER.

/OVER THE SAME



BUDGET SECRET

94. OVER THE SAME PERIOD TO 31 MARCH 1986 MOST OTHER CAPITAL ALLOWANCES WILL BE BROUGHT INTO LINE WITH THE MAIN CHANGES I HAVE ANNOUNCED. THE INLAND REVENUE WILL BE ISSUING A PRESS NOTICE TONIGHT GIVING FULL DETAILS OF THESE PROPOSALS.

95. NEXT, STOCK RELIEF. AS THE HOUSE WILL RECALL, THIS WAS INTRODUCED BY THE LAST LABOUR GOVERNMENT AS A FORM OF EMERGENCY HELP TO BUSINESSES FACING THE RAVAGES OF HIGH INFLATION. THOSE DAYS ARE PAST; AND THE RELIEF IS NO LONGER NECESSARY. COMPANY LIQUIDITY HAS IMPROVED AND, ABOVE ALL, INFLATION HAS FALLEN SHARPLY. ACCORDINGLY, I PROPOSE TO ABOLISH STOCK RELIEF FROM THIS MONTH.

*What about past relief  
ie. rephrase to make sure clear abolition of past relief is not being suggested.*

96. THE CHANGES I HAVE JUST ANNOUNCED, IN CAPITAL ALLOWANCES AND STOCK RELIEF, ENABLE ME TO EMBARK ON A MAJOR PROGRAMME OF PROGRESSIVE REDUCTIONS IN THE MAIN RATE OF CORPORATION TAX. FOR PROFITS EARNED IN THE YEAR JUST ENDING, ON WHICH TAX IS GENERALLY

/PAYABLE IN



BUDGET SECRET

PAYABLE IN 1984-85, THE RATE WILL BE CUT FROM 52 PER CENT TO 50 PER CENT. FOR PROFITS EARNED IN 1984-85 THE RATE WILL BE FURTHER CUT TO 45 PER CENT. LOOKING FURTHER AHEAD, TO PROFITS EARNED IN 1985-86, THE RATE WILL GO DOWN TO 40 PER CENT; AND FOR PROFITS EARNED IN 1986-87 THE MAIN RATE OF CORPORATION TAX WILL BE 35 PER CENT - NO LESS THAN 17 PERCENTAGE POINTS BELOW THE CURRENT RATE, *a reduction of approximately one third and*

97. ALL THESE RATES FOR THE YEARS AHEAD WILL BE INCLUDED IN THIS YEAR'S FINANCE BILL. AND WHEN THESE CHANGES ARE COMPLETE, OUR RATES OF CAPITAL ALLOWANCES FOR THE GENERALITY OF PLANT AND MACHINERY WILL BE COMPARABLE WITH THOSE IN MOST OTHER COUNTRIES, WHILE THE RATE OF TAX WILL BE SIGNIFICANTLY LOWER.

98. THE SUBSTANTIAL REDUCTION IN THE RATE OF CORPORATION TAX WILL BRING A FURTHER BENEFIT. OUR

/IMPUTATION SYSTEM



## BUDGET SECRET

IMPUTATION SYSTEM ALLOWS A COMPANY TO OFFSET IN FULL ALL INTEREST PAID. BUT ONLY A PARTIAL OFFSET FOR DIVIDENDS IS ALLOWED. COMPANIES THUS HAVE A CLEAR INCENTIVE TO FINANCE THEMSELVES THROUGH BORROWING, IN PARTICULAR BANK BORROWING, RATHER THAN BY RAISING EQUITY CAPITAL. THE CLOSER THE CORPORATION TAX RATE COMES TO THE BASIC RATE OF INCOME TAX, THE SMALLER THIS UNDESIRABLE DISTORTION BECOMES.

99. OF COURSE, THE MAJORITY OF COMPANIES ARE NOT LIABLE TO PAY THE MAIN RATE OF CORPORATION TAX AT ALL. FOR THEM IT IS THE SMALL COMPANIES' RATE, AT PRESENT 38 PER CENT, WHICH APPLIES. I PROPOSE TO REDUCE THIS RATE FORTHWITH TO 30 PER CENT, FOR PROFITS EARNED IN 1983-84 AND THEREAFTER. A TAX REGIME FOR SMALL COMPANIES WHICH IS ALREADY GENEROUS BY INTERNATIONAL STANDARDS WILL THUS BECOME MARKEDLY MORE GENEROUS.

/THE CORPORATION



BUDGET SECRET

100. THE CORPORATION TAX MEASURES I HAVE JUST ANNOUNCED WILL COST £280 MILLION IN 1984-85. IN 1985-86 THE COST WILL BE £450 MILLION - MADE UP OF £1,100 MILLION BY WAY OF REDUCTIONS IN THE RATES, ONLY PARTIALLY OFFSET BY A £650 MILLION REDUCTION IN THE VALUE OF THE RELIEFS. DURING THE TRANSITIONAL PERIOD AS A WHOLE, THESE MEASURES SHOULD HAVE A BROADLY NEUTRAL EFFECT ON THE FINANCIAL POSITION OF COMPANIES. BUT WHEN THE CHANGES HAVE FULLY WORKED THROUGH, COMPANIES WILL ENJOY VERY SUBSTANTIAL REDUCTIONS IN THE TAX THEY PAY.

101. BUSINESS AND INDUSTRY CAN GO AHEAD CONFIDENTLY ON THE BASIS OF THE CORPORATION TAX RATES I HAVE ANNOUNCED TODAY, WHICH SET THE FRAMEWORK OF COMPANY TAXATION FOR THE REST OF THIS PARLIAMENT.

102. OVER THE NEXT TWO YEARS, THESE CHANGES WILL CAUSE SOME INVESTMENT TO BE BROUGHT FORWARD, TO TAKE ADVANTAGE OF HIGH FIRST YEAR CAPITAL ALLOWANCES

/ - A PROSPECT MADE



BUDGET SECRET

- A PROSPECT MADE ALL THE MORE ALLURING FOR BUSINESS SINCE THE PROFITS EARNED WILL BE TAXED AT THE NEW, LOWER, RATES. BUT THE MORE IMPORTANT AND LASTING EFFECT WILL BE TO ENCOURAGE THE SEARCH FOR INVESTMENT PROJECTS WITH A GENUINELY WORTHWHILE RETURN, AND TO DISCOURAGE UNECONOMIC INVESTMENT.

103. IT IS DOUBTFUL WHETHER IT WAS EVER REALLY SENSIBLE TO SUBSIDISE CAPITAL INVESTMENT IRRESPECTIVE OF THE TRUE RATE OF RETURN. CERTAINLY, WITH OVER THREE MILLION UNEMPLOYED IT CANNOT MAKE SENSE TO ~~DO SO~~. *SUBSIDIZE CAPITAL SO HEAVILY AT THE EXPENSE OF LABOUR*

104. THESE CHANGES HOLD OUT AN EXCITING OPPORTUNITY FOR BRITISH INDUSTRY AS A WHOLE: AN OPPORTUNITY FURTHER TO IMPROVE ITS PROFITABILITY, AND TO EXPAND, BUILDING ON THE RECOVERY THAT IS ALREADY WELL UNDER WAY. HIGHER PROFITS AFTER TAX WILL ENCOURAGE AND REWARD ENTERPRISE, STIMULATE INNOVATION IN ALL ITS FORMS, AND CREATE MORE JOBS.

/I NOW TURN



BUDGET SECRET

105. I NOW TURN TO SOME MORE DETAILED MEASURES AFFECTING BUSINESS.

106. THE BUSINESS EXPANSION SCHEME, INTRODUCED LAST YEAR AS A SUCCESSOR TO THE BUSINESS START UP SCHEME, HAS BEEN WIDELY WELCOMED AS A HIGHLY IMAGINATIVE SCHEME FOR ENCOURAGING INDIVIDUALS TO INVEST IN SMALL COMPANIES. IT IS ALREADY PROVING A CONSIDERABLE SUCCESS. IT NOW NEEDS TIME TO SETTLE DOWN, AND I HAVE ONLY ONE CHANGE TO PROPOSE THIS YEAR.

107. THE SCHEME WAS DESIGNED TO OFFER GENEROUS INCENTIVES FOR INVESTMENT BY NEW OR EXPANDING COMPANIES IN HIGH RISK AREAS. THE OWNERSHIP OF FARMLAND CANNOT BE SAID TO FALL WITHIN THIS CATEGORY, AND I THEREFORE PROPOSE THAT FROM TODAY FARMING SHOULD CEASE TO BE TREATED AS A QUALIFYING TRADE UNDER THE SCHEME.

/NEXT, IN KEEPING



BUDGET SECRET

108. NEXT, IN KEEPING WITH WHAT I HAVE SAID ABOUT REMOVING DISTORTIONS, I PROPOSE TO ABOLISH TWO RELIEFS IN THE PERSONAL TAX FIELD WHICH WERE INTRODUCED AT A TIME WHEN THIS COUNTRY SUFFERED FROM EXCESSIVELY HIGH RATES OF INCOME TAX. AS WE HAVE REDUCED THOSE RATES, THE RELIEFS ARE NO LONGER JUSTIFIED.

109. THE FIRST DISTORTION IS THE 50 PER CENT TAX RELIEF (FALLING AFTER 9 YEARS TO 25 PER CENT) APPLIED TO THE EMOLUMENTS OF FOREIGN-DOMICILED EMPLOYEES WORKING HERE FOR FOREIGN EMPLOYERS. THESE EMPLOYEES ARE OFTEN PAYING MUCH LESS TAX HERE THAN THEY WOULD EITHER IN THEIR OWN COUNTRY OR IN MOST OTHER EUROPEAN COUNTRIES. AT PRESENT INCOME TAX RATES, THE NEED FOR THIS RELIEF HAS CLEARLY DISAPPEARED. MOREOVER, IT IS OPEN TO WIDESPREAD ABUSE. IT IS, FOR EXAMPLE, POSSIBLE FOR THE SON OF AN IMMIGRANT, WORKING HERE FOR A FOREIGN COMPANY, TO ENJOY THIS RELIEF EVEN IF HE HAS LIVED IN THIS

/COUNTRY ALL HIS



BUDGET SECRET

COUNTRY ALL HIS LIFE. I THEREFORE PROPOSE TO WITHDRAW THE RELIEF FOR ALL NEW CASES FROM TODAY. FOR EXISTING BENEFICIARIES, THE 25 PER CENT RELIEF WILL CEASE ON 6 APRIL, AND THE 50 PER CENT RELIEF WILL BE PHASED OUT OVER THE NEXT FIVE YEARS.

110. I ALSO PROPOSE TO WITHDRAW THE FOREIGN EARNINGS RELIEF FOR UNITED KINGDOM RESIDENTS WHO WORK AT LEAST 30 DAYS ABROAD IN A TAX YEAR. THIS RELIEF TOO HARKS BACK TO THE DAYS OF PENALLY HIGH INCOME TAX RATES. IT TOO HAS BEEN EXPLOITED, IN PARTICULAR BY THOSE WHO PROLONG THEIR OVERSEAS VISITS PURELY IN ORDER TO GAIN A TAX ADVANTAGE. I PROPOSE TO WITHDRAW THE MATCHING RELIEF FOR THE SELF-EMPLOYED WHO SPEND 30 DAYS ABROAD, AND FOR THOSE RESIDENT IN THE UK WHO HAVE SEPARATE EMPLOYMENTS OR SEPARATE TRADES CARRIED ON WHOLLY ABROAD. THE RELIEF WILL BE HALVED TO 12½ PER CENT IN 1984- 85 AND REMOVED ENTIRELY FROM 6 APRIL 1985. HOWEVER, I AM NOT MAKING ANY CHANGE TO THE 100 PER

/CENT REDUCTION



BUDGET SECRET

CENT DEDUCTION GIVEN FOR ABSENCES ABROAD OF 365 DAYS OR MORE. IN ADDITION, I HAVE AUTHORISED CONSULTATIONS BY THE INLAND REVENUE ABOUT A POSSIBLE RELAXATION IN THE RULES GOVERNING THE TAXATION OF EXPENSES REIMBURSED TO EMPLOYEES FOR TRAVEL OVERSEAS.

111. THE ABOLITION OF THESE RELIEFS WILL EVENTUALLY YIELD REVENUE SAVINGS OF OVER £150 MILLION; AND REPRESENTS ANOTHER USEFUL STEP IN THE REMOVAL OF COMPLEXITY AND DISTORTIONS IN THE TAX SYSTEM.

112. I NEED TO SET THE CAR BENEFIT SCALES FOR 1985-86 FOR THOSE PROVIDED WITH THE USE OF A CAR BY THEIR EMPLOYER. DESPITE THE INCREASES OVER RECENT YEARS, THE LEVELS STILL FALL SHORT OF ANY REALISTIC MEASURE OF THE TRUE BENEFIT. I AM PROPOSING AN INCREASE OF 10 PER CENT IN BOTH THE CAR AND CAR FUEL SCALES WITH EFFECT FROM APRIL 1985.

/UNNECESSARILY



BUDGET SECRET

113. UNNECESSARILY HIGH RATES OF TAX DISCOURAGE ENTERPRISE AND RISK TAKING. THIS IS TRUE OF THE CAPITAL TAXES, JUST AS IT IS OF THE CORPORATION AND INCOME TAXES. IT IS A MATTER OF PARTICULAR CONCERN TO THOSE INVOLVED IN RUNNING UNQUOTED FAMILY BUSINESSES. THE HIGHEST RATES OF CAPITAL TRANSFER TAX ARE FAR TOO HIGH AND BADLY OUT OF LINE WITH COMPARABLE RATES ABROAD. I PROPOSE THEREFORE, IN ADDITION TO STATUTORY INDEXATION, TO REDUCE THE HIGHEST RATE OF CAPITAL TRANSFER TAX FROM 75 PER CENT TO 60 PER CENT. FOR LIFETIME GIFTS I PROPOSE TO SIMPLIFY THE SCALE SO THAT THE RATE IS ALWAYS ONE-HALF OF THAT ON DEATH.

114. FOR CAPITAL GAINS TAX I WILL, AS PROMISED, BRING FORWARD IN THE FINANCE BILL PROPOSALS TO DOUBLE THE LIMIT FOR RETIREMENT RELIEF TO A FIGURE OF £100,000, BACKDATED TO APRIL 1983. A CONSULTATIVE DOCUMENT ON OTHER POSSIBLE CHANGES IN THIS RELIEF IS BEING ISSUED NEXT WEEK. I AM

/PROPOSING NO



BUDGET SECRET

PROPOSING NO OTHER CHANGES THIS YEAR IN CAPITAL GAINS TAX BEYOND THE STATUTORY INDEXATION OF THE EXEMPT AMOUNT FROM £5,300 TO £5,600. HOWEVER, THE TAX CONTINUES TO ATTRACT CRITICISM -NOT LEAST FOR ITS COMPLEXITY - AND THAT IS A MATTER TO WHICH I HOPE TO RETURN IN A LATER YEAR.

115. WE HAVE DONE MUCH TO IMPROVE THE DEVELOPMENT LAND TAX. EARLY IN THE LAST PARLIAMENT, MY PREDECESSOR INCREASED THE THRESHOLD FROM £10,000 TO £50,000. I NOW PROPOSE A FURTHER INCREASE TO £75,000, WHICH WILL REDUCE THE NUMBER OF CASES LIABLE TO THE TAX BY MORE THAN ONE-THIRD.

116. NEXT SHARE OPTIONS. THE MEASURES INTRODUCED IN THE LAST PARLIAMENT TO IMPROVE EMPLOYEE INVOLVEMENT THROUGH PROFIT-SHARING AND SAVINGS-RELATED SHARE OPTIONS SCHEMES HAVE BEEN A NOTABLE SUCCESS. THE NUMBER OF THESE EMPLOYEE SCHEMES OPEN TO ALL EMPLOYEES HAS INCREASED FROM ABOUT 30 IN 1979 TO

/OVER 670 NOW,



BUDGET SECRET

OVER 670 NOW, BENEFITING SOME HALF A MILLION EMPLOYEES. TO MAINTAIN AND BUILD ON THIS PROGRESS I PROPOSE TO INCREASE THE MONTHLY LIMIT ON CONTRIBUTIONS TO SAVINGS-RELATED SHARE OPTION SCHEMES FROM £50 TO £100. I HAVE ALSO AUTHORISED THE INLAND REVENUE TO DOUBLE THE TAX-FREE LIMITS UNDER THE CONCESSION ON LONG SERVICE AWARDS, AND TO INCLUDE WITHIN THESE LIMITS THE GIFT OF SHARES IN THE EMPLOYEE'S COMPANY.

117. BUT BEYOND THIS, I AM CONVINCED THAT WE NEED TO DO MORE TO ATTRACT TOP CALIBRE COMPANY MANAGEMENT AND TO INCREASE THE INCENTIVES AND MOTIVATION OF EXISTING EXECUTIVES AND KEY PERSONNEL BY LINKING THEIR REWARDS TO PERFORMANCE. I PROPOSE THEREFORE THAT, SUBJECT TO CERTAIN NECESSARY LIMITS AND CONDITIONS, SHARE OPTIONS GENERALLY WILL BE TAKEN OUT OF INCOME TAX, LEAVING ANY GAIN TO BE CHARGED TO CAPITAL GAINS TAX ON ULTIMATE DISPOSAL OF THE SHARES. THE NEW RULES WILL APPLY TO OPTIONS MEETING THE CONDITIONS WHICH ARE GRANTED FROM 6 APRIL.

/I AM SURE



BUDGET SECRET

118. I AM SURE THAT ALL THESE CHANGES WILL BE WELCOMED AS MEASURES TO ENCOURAGE THE COMMITMENT OF EMPLOYEES TO THE SUCCESS OF THEIR COMPANIES AND TO IMPROVE THE PERFORMANCE, COMPETITIVENESS AND PROFITABILITY OF BRITISH INDUSTRY.

119. AS THE HOUSE KNOWS, THE GOVERNMENT IS DEEPLY CONCERNED AT THE THREAT WHICH THE SPREAD OF UNITARY TAXATION IN CERTAIN US STATES HAS POSED TO THE US SUBSIDIARIES OF BRITISH FIRMS. WITH OUR EUROPEAN PARTNERS WE ARE MONITORING THE SITUATION CLOSELY, AND AWAIT WITH KEEN INTEREST THE IMMINENT REPORT OF US TREASURY SECRETARY REGAN'S WORKING GROUP. IT IS ESSENTIAL THAT A SATISFACTORY SOLUTION IS FOUND AND SPEEDILY IMPLEMENTED.

120. US FIRMS OPERATING IN THIS COUNTRY ARE NOT OF COURSE TAXED ON A UNITARY BASIS.

/I NOW TURN



BUDGET SECRET

121. I NOW TURN TO OIL TAXATION. LAST YEAR'S NORTH SEA TAX CHANGES WERE WELL RECEIVED, AND THERE HAS BEEN A SUBSTANTIAL INCREASE IN THE NUMBER OF DEVELOPMENT PROJECTS COMING FORWARD, AND A NEW SURGE IN EXPLORATION. THE GOVERNMENT IS ALREADY COMMITTED TO A STUDY OF THE ECONOMICS OF INVESTMENT IN INCREMENTAL DEVELOPMENT IN EXISTING FIELDS. THIS IS OF INCREASING IMPORTANCE, AND IN CONSULTATION WITH MY RT HON FRIEND THE SECRETARY OF STATE FOR ENERGY I THEREFORE PROPOSE TO REVIEW THIS AREA WITH THE INDUSTRY, AND TO LEGISLATE AS APPROPRIATE NEXT YEAR TO IMPROVE THE POSITION. TO PREVENT PROJECTS BEING DEFERRED PENDING THIS REVIEW, ANY CHANGES WILL APPLY TO ALL PROJECTS WHICH RECEIVE DEVELOPMENT CONSENT AFTER TODAY.

122. MEANWHILE, I AM TAKING TWO MEASURES TO PREVENT AN UNJUSTIFIED LOSS OF TAX IN THE NORTH SEA. FIRST, IN ADDITION TO THE PRT MEASURES ON FARMOUTS WHICH I ANNOUNCED LAST SEPTEMBER, I AM LIMITING THE

/POTENTIAL



BUDGET SECRET

POTENTIAL CORPORATION TAX COST OF SUCH DEALS. SECOND, I PROPOSE TO REPEAL THE PROVISION WHICH ALLOWS ADVANCE CORPORATION TAX TO BE REPAID WHERE CORPORATION TAX IS REDUCED BY PRT. I HAVE ALSO REVIEWED THE CASE FOR EXTENDING LAST YEAR'S FUTURE FIELD CONCESSIONS TO THE SOUTHERN BASIN, BUT HAVE CONCLUDED THAT ADDITIONAL INCENTIVES HERE ARE NOT NEEDED.

123. I HAVE JUST TWO FURTHER CHANGES AFFECTING BUSINESS TO PROPOSE, BOTH OF WHICH WILL COME INTO FORCE ON 1 OCTOBER.

124. EVER SINCE VAT WAS INTRODUCED IN THIS COUNTRY, WE HAVE TREATED IMPORTS DIFFERENTLY FROM THE WAY OUR MAIN EUROPEAN COMMUNITY COMPETITORS TREAT THEM. WHILE THEY REQUIRE VAT ON IMPORTED GOODS TO BE PAID IN THE SAME WAY AS CUSTOMS DUTIES, WE DO NOT. UNDER OUR SYSTEM AN IMPORTER DOES NOT HAVE TO ACCOUNT FOR VAT ON HIS IMPORTS UNTIL HE MAKES HIS NORMAL VAT

/RETURN,



BUDGET SECRET

RETURN, ON AVERAGE SOME 11 WEEKS LATER. DURING THIS TIME THE IMPORTER ENJOYS FREE CREDIT AT THE TAXPAYER'S EXPENSE. BUT BUSINESSES BUYING FROM UK SUPPLIERS HAVE TO PAY VAT STRAIGHT AWAY.

125. THE EUROPEAN COMMISSION HAS FOR SOME YEARS NOW BEEN SEEKING, WITH OUR FULL SUPPORT, TO GET A SYSTEM LIKE OURS ADOPTED THROUGHOUT THE COMMUNITY. BUT THE PLAIN FACT IS THAT IN ALL THAT TIME THE COMMISSION HAS MADE NO PROGRESS WHATEVER.

126. I MUST TELL THE HOUSE HAVE I AM NOT PREPARED TO PUT BRITISH INDUSTRY AT A COMPETITIVE DISADVANTAGE IN THE HOME MARKET ANY LONGER. SHOULD OUR EUROPEAN PARTNERS AT ANY TIME UNDERGO A DAMASCENE CONVERSION, AND AGREE THAT THE COMMISSION'S PROPOSAL SHOULD BE ACCEPTED AFTER ALL, THEN OF COURSE WE WOULD REVERT TO THE PRESENT SYSTEM. BUT IN THE MEANTIME I PROPOSE TO MOVE TO THE SYSTEM USED BY OUR EUROPEAN COMPETITORS. WE SHALL PROVIDE THE SAME FACILITIES

/FOR PAYMENT



## BUDGET SECRET

FOR PAYMENT OF VAT ON IMPORTS AS APPLY TO CUSTOMS DUTIES. THAT MEANS THAT MOST IMPORTERS WILL BE ABLE TO DEFER PAYMENT OF VAT BY ON AVERAGE ONE MONTH FROM THE DATE OF IMPORTATION. BUT THAT IS ALL.

127. AS I HAVE SAID, THIS CHANGE WILL APPLY FROM 1 OCTOBER. BY BRINGING FORWARD VAT RECEIPTS, IT WILL BRING IN AN EXTRA £1.2 BILLION IN 1984-85, SOME OF WHICH WILL BE BORNE BY FOREIGN PRODUCERS AND MANUFACTURERS. THERE WILL OF COURSE BE NO INCREASED REVENUE IN SUBSEQUENT YEARS.

128. THE SECOND CHANGE I PROPOSE TO MAKE ON 1 OCTOBER CONCERNS THE NATIONAL INSURANCE SURCHARGE. THIS TAX ON JOBS WAS INTRODUCED BY THE LABOUR GOVERNMENT IN 1977 AT THE RATE OF 2 PER CENT, AND FURTHER INCREASED BY THE RT. HON. MEMBER FOR LEEDS EAST IN 1978 TO 3½ PER CENT. DURING THE LAST PARLIAMENT, THIS GOVERNMENT REDUCED IT TO 1 PER CENT, AND WE ARE PLEDGED TO ABOLISH IT DURING THE LIFETIME OF THIS PARLIAMENT.

/GIVEN THE IMPACT



BUDGET SECRET

129. GIVEN THE IMPACT THAT THIS TAX HAS, NOT ONLY ON INDUSTRIAL COSTS BUT ALSO - AT A TIME OF HIGH UNEMPLOYMENT - ON JOBS, I HAVE DECIDED TO TAKE THE OPPORTUNITY OF THIS MY FIRST BUDGET TO FULFIL THAT PLEDGE. ABOLITION OF THE NATIONAL INSURANCE SURCHARGE FROM OCTOBER WILL REDUCE PRIVATE SECTOR EMPLOYERS' COSTS BY ALMOST £350 MILLION IN 1984-85, AND OVER £850 MILLION IN A FULL YEAR. IT WILL THUS BE OF CONTINUING HELP TO BRITISH INDUSTRY. AS BEFORE, THE BENEFIT WILL BE CONFINED TO THE PRIVATE SECTOR.

130. THE HOUSE WILL I AM SURE AGREE THAT A BUDGET WHICH ABOLISHES THE NATIONAL INSURANCE SURCHARGE, AND CUTS THE RATES AND SIMPLIFIES THE STRUCTURE OF CORPORATION TAX, IS A BUDGET FOR JOBS AND FOR ENTERPRISE. IT OFFERS BRITISH INDUSTRY AN OPPORTUNITY WHICH I AM CONFIDENT IT WILL SEIZE.

/HAVING



**INDIRECT TAXES**

131. HAVING ANNOUNCED MAJOR REFORMS OF BOTH THE TAXATION OF SAVINGS AND INVESTMENT AND THE TAXATION OF BUSINESS, I TURN NOW TO THE THIRD AND FINAL AREA IN WHICH I PROPOSE TO MAKE PROGRESS ON TAX REFORM. THIS IS THE TAXATION OF PERSONAL INCOME AND SPENDING.

132. THE BROAD PRINCIPLE WAS CLEARLY SET OUT IN THE MANIFESTO ON WHICH WE WERE FIRST ELECTED IN 1979. THIS EMPHASISED THE NEED FOR A SWITCH FROM TAXES ON EARNINGS TO TAXES ON SPENDING. MY PREDECESSOR MADE AN IMPORTANT MOVE IN THIS DIRECTION IN HIS FIRST BUDGET, AND THE TIME HAS COME TO MAKE A FURTHER MOVE TODAY. TO REDUCE DIRECT TAXATION BY THIS MEANS IS IMPORTANT IN TWO WAYS. IT IMPROVES INCENTIVES AND MAKES IT MORE WORTHWHILE TO WORK, AND IT INCREASES THE FREEDOM OF CHOICE OF THE INDIVIDUAL.

/HAVING REGARD



BUDGET SECRET

133. HAVING REGARD TO THE REPRESENTATIONS I HAVE RECEIVED ON HEALTH GROUNDS, I THEREFORE PROPOSE AN INCREASE IN THE TOBACCO DUTY WHICH, INCLUDING VAT, WILL PUT 10P ON THE PRICE OF A PACKET OF CIGARETTES, WITH CORRESPONDING INCREASES FOR HAND-ROLLING TOBACCO AND CIGARS. THIS WILL DO NO MORE THAN RESTORE THE TAX ON TOBACCO TO ITS 1965 LEVEL. THESE CHANGES WILL TAKE EFFECT FROM MIDNIGHT ON THURSDAY. I DO NOT PROPOSE ANY INCREASE IN THE DUTY ON PIPE TOBACCO.

134. I PROPOSE TO RAISE MOST OF THE OTHER EXCISE DUTIES BROADLY IN LINE WITH INFLATION, SO AS TO MAINTAIN THEIR REAL VALUE: NOT TO DO SO WOULD RUN COUNTER TO THE PHILOSOPHY I OUTLINED A MOMENT AGO. BUT WITH INFLATION AS LOW AS IT NOW IS, THE NECESSARY INCREASES ARE ON THE WHOLE MERCIFULLY MODEST.

/I PROPOSE TO



BUDGET SECRET

135. I PROPOSE TO INCREASE THE DUTIES ON PETROL AND DERY BY AMOUNTS WHICH, INCLUDING VAT, WILL RAISE THE PRICE AT THE PUMPS BY 4½P AND 3½P A GALLON RESPECTIVELY. THIS DOES NO MORE THAN KEEP PACE WITH INFLATION. THE CHANGES WILL TAKE EFFECT FOR OIL DELIVERED FROM REFINERIES AND WAREHOUSES FROM SIX O'CLOCK THIS EVENING. I DO NOT PROPOSE TO INCREASE THE DUTY ON HEAVY FUEL OIL, WHICH IS OF PARTICULAR IMPORTANCE TO INDUSTRIAL COSTS.

136. THERE IS ONE EXCISE DUTY WHICH I PROPOSE TO DO AWAY WITH ALTOGETHER. MANY OF THOSE WHO FIND IT HARDEST TO MAKE ENDS MEET, INCLUDING IN PARTICULAR MANY PENSIONERS, USE PARAFFIN STOVES TO HEAT THEIR HOMES, AND IT IS WITH THEM IN MIND THAT I PROPOSE TO ABOLISH THE DUTY ON KEROSENE FROM SIX O'CLOCK TONIGHT. I AM SURE THAT THIS WILL BE WELCOMED ON ALL SIDES OF THE HOUSE.

/THE VARIOUS RATES



BUDGET SECRET

137. THE VARIOUS RATES OF VEHICLE EXCISE DUTY WILL, ONCE AGAIN, GO UP ROUGHLY IN LINE WITH PRICES. THUS THE DUTY FOR CARS AND LIGHT VANS WILL BE INCREASED BY £5, FROM £85 TO £90 A YEAR. HOWEVER, IN THE LIGHT OF THE REASSESSMENT BY MY RT HON FRIEND THE SECRETARY OF STATE FOR TRANSPORT OF THE WEAR AND TEAR THAT VARIOUS TYPES OF VEHICLE CAUSE TO THE ROADS, THERE WILL BE REDUCTIONS IN DUTY FOR THE LIGHTEST LORRIES, OFFSET BY HIGHER INCREASES FOR SOME HEAVIER LORRIES. ALL THESE CHANGES IN VEHICLE EXCISE DUTY WILL TAKE EFFECT FROM TOMORROW.

138. HOWEVER, I PROPOSE TO EXEMPT FROM VEHICLE EXCISE DUTY ALL RECIPIENTS OF THE WAR PENSIONERS' MOBILITY SUPPLEMENT. IN ADDITION, THE EXISTING VAT RELIEF FOR MOTOR VEHICLES DESIGNED OR ADAPTED FOR USE BY THE HANDICAPPED WILL BE EXTENDED, AND MATCHED BY A NEW CAR TAX RELIEF. THE EFFECT WILL BE THAT NEITHER VAT NOR CAR TAX WILL APPLY TO FAMILY CARS DESIGNED FOR DISABLED PEOPLE OR SUBSTANTIALLY ADAPTED FOR THEIR USE.

/I NOW COME



BUDGET SECRET

139. I NOW COME TO THE MOST DIFFICULT DECISION I HAVE TO TAKE IN THE EXCISE DUTY FIELD. AS THE HOUSE WILL BE AWARE, THE RULES OF THE EUROPEAN COMMUNITY, SO FAR AS ALCOHOLIC DRINKS ARE CONCERNED, ARE DESIGNED TO PREVENT A MEMBER STATE FROM PROTECTING ITS OWN DOMESTIC PRODUCT BY IMPOSING A SIGNIFICANTLY HIGHER DUTY ON COMPETING IMPORTS. IN PURSUIT OF THIS, THE COMMISSION HAS TAKEN A NUMBER OF COUNTRIES TO THE EUROPEAN COURT OF JUSTICE.

140. IN OUR CASE, THE COMMISSION CONTENDED THAT WE WERE PROTECTING BEER BY UNDER-TAXING IT IN RELATION TO WINE. WE FOUGHT THE CASE, BUT LOST; AND I AM NOW IMPLEMENTING THE JUDGEMENT HANDED DOWN BY THE COURT LAST YEAR. ACCORDINGLY, I PROPOSE TO INCREASE THE DUTY ON BEER BY THE MINIMUM AMOUNT NEEDED TO COMPLY WITH THE JUDGEMENT AND MAINTAIN REVENUE: 2P ON A TYPICAL PINT OF BEER, INCLUDING VAT. AT THE SAME TIME, THE DUTY ON TABLE WINE WILL BE REDUCED BY THE EQUIVALENT OF ABOUT 18P A BOTTLE, AGAIN INCLUDING VAT.

/WE HAVE THUS



BUDGET SECRET

141. WE HAVE THUS COMPLIED WITH THE COURT'S JUDGEMENT. AND I AM HAPPY TO BE ABLE TO TELL THE HOUSE THAT THE ITALIAN GOVERNMENT HAVE, AFTER DISCUSSIONS, GIVEN US AN UNDERTAKING THAT THEY WILL COMPLY WITH AN EARLIER COURT RULING ON DISCRIMINATION AGAINST SCOTCH WHISKY AND OTHER IMPORTED SPIRITS.

142. AS FOR THE REST OF THE ALCOHOLIC DRINKS, CIDER, WHICH INCREASINGLY COMPETES WITH BEER BUT ATTRACTS A LOWER DUTY, WILL GO UP BY 3P A PINT. THE DUTIES ON MADE-WINE WILL BE ALIGNED WITH THOSE ON OTHER WINE. AND I PROPOSE TO INCREASE THE DUTY ON SPARKLING WINE, FORTIFIED WINE AND SPIRITS BY ABOUT 10P A BOTTLE, INCLUDING VAT. ALL THESE CHANGES WILL TAKE EFFECT FROM MIDNIGHT TONIGHT.

143. THESE CHANGES IN EXCISE DUTIES WILL, ALL TOLD, BRING IN SOME £840 MILLION IN 1984-85, SOME £200M MORE THAN IS REQUIRED TO KEEP PACE WITH INFLATION.

/THE ADDITION



BUDGET SECRET

THE ADDITION IS OF COURSE DUE TO THE INCREASE IN TOBACCO DUTY.

144. THE REMAINDER OF THE EXTRA REVENUE I NEED TO MAKE A SUBSTANTIAL SWITCH THIS YEAR FROM TAXES ON EARNINGS TO TAXES ON SPENDING WILL COME FROM VAT. I PROPOSE NO CHANGE IN THE RATE OF VAT. INSTEAD, I INTEND TO BROADEN THE BASE OF THE TAX BY EXTENDING THE 15 PER CENT RATE TO TWO AREAS OF EXPENDITURE THAT HAVE HITHERTO BEEN ZERO-RATED.

145. FIRST, ALTERATIONS TO BUILDINGS. AT PRESENT REPAIRS AND MAINTENANCE ARE TAXED, BUT ALTERATIONS ARE NOT. THE BORDERLINE BETWEEN THESE TWO CATEGORIES IS THE MOST CONFUSED IN THE WHOLE FIELD OF VAT. I PROPOSE TO END THIS CONFUSION AND ILLOGICALITY BY BRINGING ALL ALTERATIONS INTO TAX. I RECOGNISE THAT THIS WILL BE UNWELCOME NEWS FOR THE CONSTRUCTION INDUSTRY, BUT CONSTRUCTION WILL OF COURSE BENEFIT GREATLY FROM THE REDUCTION IN THE

/RATE OF STAMP



BUDGET SECRET

RATE OF STAMP DUTY WHICH I HAVE ALREADY ANNOUNCED. £290 MILLION OF THE COST OF THAT REDUCTION IN 1984-85 RELATES TO TRANSFERS OF LAND AND BUILDINGS, AND OF THAT £290 MILLION SOME 90 PER CENT RELATES TO BUILDINGS AND BUILDING LAND. NEVERTHELESS, TO ALLOW A REASONABLE TIME FOR EXISTING COMMITMENTS TO BE COMPLETED OR ADJUSTED, THE VAT CHANGE WILL BE DEFERRED UNTIL 1 JUNE.

146. SECONDLY, FOOD. MOST FOOD IS ZERO-RATED. BUT FOOD SERVED IN RESTAURANTS IS TAXED, TOGETHER WITH A MISCELLANEOUS RANGE OF ITEMS INCLUDING ICE-CREAM, CONFECTIONERY, SOFT DRINKS AND CRISPS, WHICH WERE BROUGHT INTO TAX BY THE RT HON MEMBER FOR LEEDS EAST. TAKE-AWAY FOOD CLEARLY COMPETES WITH OTHER FORMS OF CATERING, AND I THEREFORE INTEND TO BRING INTO TAX HOT TAKE-AWAY FOOD AND DRINKS, WITH EFFECT FROM 1 MAY.

/THE TOTAL EFFECT



BUDGET SECRET

147. THE TOTAL EFFECT OF THE EXTENSIONS OF THE VAT COVERAGE WHICH I HAVE PROPOSED WILL BE TO INCREASE THE YIELD OF THE TAX BY £375 MILLION IN 1984-85 AND BY £650 MILLION IN A FULL YEAR.

148 THE TOTAL IMPACT EFFECT ON THE RETAIL PRICE INDEX OF THE VAT CHANGES AND EXCISE DUTY CHANGES TAKEN TOGETHER WILL BE LESS THAN THREE-QUARTERS OF ONE PER CENT. THIS HAS ALREADY BEEN TAKEN INTO ACCOUNT IN THE FORECAST WHICH I HAVE GIVEN TO THE HOUSE OF A DECLINE IN INFLATION TO  $4\frac{1}{2}$  PER CENT BY THE END OF THE YEAR.

149. THE EXTRA REVENUE RAISED IN THIS WAY WILL ENABLE ME, WITHIN THE OVERALL FRAMEWORK OF A NEUTRAL BUDGET, TO LIGHTEN THE BURDEN OF INCOME TAX.



**INCOME TAX**

151. SINCE WE TOOK OFFICE IN 1979, WE HAVE CUT THE BASIC RATE OF INCOME TAX FROM 33 PER CENT TO 30 PER CENT AND SHARPLY REDUCED THE CONFISCATORY HIGHER RATES INHERITED FROM THE LAST LABOUR GOVERNMENT. WE HAVE INCREASED THE MAIN TAX ALLOWANCES NOT SIMPLY IN LINE WITH PRICES BUT BY AROUND 8 PER CENT IN REAL TERMS. IT IS A GOOD RECORD. BUT IT IS NOT ENOUGH. THE BURDEN OF INCOME TAX IS STILL TOO HEAVY.

152. DURING THE LIFETIME OF THIS PARLIAMENT, I INTEND TO CARRY FORWARD THE PROGRESS WE HAVE ALREADY MADE. FOR THE MOST PART, THIS WILL HAVE TO WAIT FOR FUTURE BUDGETS, PARTICULARLY SINCE I HAVE THOUGHT IT RIGHT THIS YEAR TO CONCENTRATE ON SETTING A NEW REGIME OF BUSINESS TAXATION FOR THE LIFETIME OF A PARLIAMENT - AND BEYOND. BUT AS A RESULT OF THE CHANGES TO TAXES ON SPENDING WHICH I HAVE JUST ANNOUNCED, I CAN TAKE A FURTHER STEP IN THIS BUDGET.

/I PROPOSE



BUDGET SECRET

153. I PROPOSE TO MAKE NO CHANGE THIS YEAR IN THE RATES OF INCOME TAX. SO FAR AS THE ALLOWANCES AND THRESHOLDS ARE CONCERNED, I MUST CLEARLY INCREASE THESE BY THE AMOUNTS SET OUT IN THE STATUTORY INDEXATION FORMULA, BASED ON THE 5.3 PER CENT INCREASE IN THE RETAIL PRICE INDEX TO DECEMBER. THE QUESTION IS HOW MUCH MORE I CAN DO, AND HOW TO DIRECT IT.

154. I HAVE DECIDED THAT, THIS YEAR, THE RIGHT COURSE IS TO USE EVERY PENNY I HAVE IN HAND, WITHIN THE FRAMEWORK OF A REVENUE NEUTRAL BUDGET, TO LIFT THE LEVEL OF THE BASIC TAX THRESHOLDS, FOR THE MARRIED AND SINGLE ALIKE. IT MAKES VERY LITTLE SENSE TO BE COLLECTING INCOME TAX FROM PEOPLE WHO ARE AT THE SAME TIME RECEIVING MEANS-TESTED BENEFITS. MOREOVER LOW TAX THRESHOLDS WORSEN THE POVERTY AND UNEMPLOYMENT TRAPS, SO THAT THERE IS LITTLE IF ANY FINANCIAL INCENTIVE TO FIND A BETTER JOB OR EVEN ANY JOB AT ALL. THERE IS, ALAS, NO

/QUICK OR CHEAP



BUDGET SECRET

QUICK OR CHEAP SOLUTION TO THESE PROBLEMS. BUT THAT IS ALL THE MORE REASON TO MAKE A FURTHER MOVE TOWARDS SOLVING THEM NOW.

155. I PROPOSE TO INCREASE THE OTHER THRESHOLDS IN LINE WITH THE STATUTORY INDEXATION REQUIREMENT, AND BY NO MORE. THE FIRST HIGHER RATE OF 40 PER CENT WILL APPLY WHEN TAXABLE INCOME REACHES £15,400 A YEAR AND THE TOP RATE OF 60 PER CENT TO TAXABLE INCOME OF £38,100 OR MORE. THE SINGLE AGE ALLOWANCE WILL RISE FROM £2,360 TO £2,490 AND THE MARRIED AGE ALLOWANCE FROM £3,755 TO £3,955.

156. FOR THE BASIC THRESHOLDS, STATUTORY INDEXATION WOULD MEAN PUTTING THE SINGLE AND MARRIED ALLOWANCES UP BY £100 AND £150 RESPECTIVELY. I AM GLAD TO SAY THAT I CAN DO CONSIDERABLY BETTER THAN THAT. I PROPOSE TO INCREASE THE BASIC THRESHOLDS BY WELL OVER DOUBLE WHAT IS REQUIRED BY INDEXATION. THE SINGLE PERSON'S THRESHOLD WILL BE INCREASED BY £220,

/FROM £1,785



BUDGET SECRET

FROM £1,785 TO £2,005; AND THE MARRIED THRESHOLD BY £360, FROM £2,795 TO £3,155.

157. THIS IS AN INCREASE OF AROUND 12½ PER CENT, OR SOME 7 PER CENT IN REAL TERMS. IT BRINGS THE MARRIED MAN'S TAX THRESHOLD FOR 1984-85 TO ITS HIGHEST LEVEL IN REAL TERMS SINCE THE WAR. IT MEANS THAT THE GREAT MAJORITY OF MARRIED COUPLES WILL ENJOY AN INCOME TAX CUT OF AT LEAST £2 A WEEK. AND IT MEANS THAT A LARGE NUMBER OF PEOPLE, THOSE WITH THE SMALLEST INCOMES OF ALL, ARE TAKEN OUT OF INCOME TAX ALTOGETHER. SOME 850,000 PEOPLE - OVER 100,000 OF THEM WIDOWS - WHO WOULD HAVE PAID TAX IF THRESHOLDS HAD NOT BEEN INCREASED, WILL PAY NO TAX IN 1984-85. THAT IS 400,000 ~~FEWER~~ THAN IF THE ALLOWANCES HAD MERELY BEEN INDEXED.

MORE

158. ALL THESE CHANGES WILL TAKE EFFECT UNDER PAYE ON THE FIRST PAY DAY AFTER 10 MAY. THEIR COST IS CONSIDERABLE: SOME £1.8 BILLION IN 1984-85, OF

/WHICH ROUGHLY



BUDGET SECRET

WHICH ROUGHLY HALF REPRESENTS THE COST OF INDEXATION.

159. THIS IS AS FAR AS I CAN GO ON INCOME TAX THIS YEAR, WITHIN A BROADLY REVENUE-NEUTRAL BUDGET FOR 1984-85. BUT AS I HAVE ALREADY SAID, SO LONG AS WE HOLD TO OUR PUBLISHED PLANNED LEVELS OF PUBLIC SPENDING, THERE IS AN EXCELLENT PROSPECT OF FURTHER CUTS IN INCOME TAX IN NEXT YEAR'S BUDGET. THESE WOULD BE ON TOP OF THE MEASURES I HAVE ANNOUNCED IN THIS BUDGET WHICH, AS I HAVE ALREADY TOLD THE HOUSE, WILL REDUCE TAXATION IN 1985-86 BY WELL OVER £1½ BILLION, WITH BUSINESS TAKING THE LION'S SHARE.



CODING

*NA done*  
*E (Monck Phs)*

- A Chief Secretary
- B Financial Secretary
- C Minister of State
- D Economic Secretary
  
- E Mr Ridley
- F Mr Lord
- G Mr Portillo
  
- H Sir P Middleton
- I Sir T Burns
- J Mr Bailey
- K Mr Littler
- L Mr Anson
- M Mr Cassell
- N Mr Monck
- O Mr Battishill
- P Mr Evans
- Q Mr Lankester
- R Mr Monger
- S Mr Odling-Smee
- T Mr Folger
- U Mr Hall
- V Mr Kemp
  
- Y Inland Revenue
- Z Customs and Excise

*? King GTR  
- 2 officials  
2 Tony Clarke*

\* Letters in the margin indicate main source of textual amendments or suggestions.



BLOCK J: Taxation of profits and capital

Para. 2

This misses a trick, failing to bring out the ridiculous vicious circle by which high tax rates breeds special reliefs and more special reliefs require still higher tax rates. Perhaps one could begin the paragraph on something like the following lines:

"Once tax rates are allowed to become too high they tend to feed on themselves in a dangerous way which is worth underlining today. **For once** they become high, the ~~ir~~ unfairness leads to understandable calls for special reliefs, ~~where~~ the damage they do is greatest. Unfortunately it costs money to finance such reliefs - so existing and already excessive tax rates have to be raised higher still to finance them. In other words one is confronted with the classic vicious circle, which we are now determined to reverse. As we do so, it follows that we shall reduce both the excessive rates of tax and the number and generosity of those special reliefs. The case for such action is strengthened by the fact that many of these special reliefs are very indiscriminate, and not relevant to today's and tomorrow's conditions. Some were introduced...  
[Carry on as in the third line of the present §2]



- Para. 5 Would it not help to say that we are talking about advance Corporation Tax in the second paragraph?
- Para. 7 It is a bit much to describe the previous Chancellor's reforms to stock relief as "patching [up]"!
- Para. 8 The justification for lowering capital allowances raises a question of fundamental principle. The present justification is an empirical one, which is not easy to sustain. Would it not be better to parade more abstract arguments, which are nonetheless impossible to refute, dealing with the discrepancies between pre- and post-tax rates of return inherent in the present system?
- Para. 14 Should one not indicate somewhere that the benefits of the Corporation Tax will be significantly greater in later years?
- Para. 19 Surely it is better to say that there is an objective reason for removing the foreign emoluments and foreign earnings reliefs, rather than merely to pin it all on the Chancellor's judgement, as the last sentence does?
- Para. 23 Here is a heaven sent opportunity to do a little education of the general public and to indicate by how much the present and future car benefit scales will fall short of any realistic measure of their true benefit. A figure like  $\frac{1}{2}$  or  $\frac{2}{3}$  will shake many people and help explain why the Government has to continue to raise the value of these scales.

*Final Comments on Sections 12 to the end to follow shortly.*

*AK 1/3*





HOUSE OF COMMONS  
LONDON SW1A 0AA

NB: These  
two pages  
(pages 36-43)  
w/ still go @ end,  
after Income Tax

36. Finally, I have two further changes to propose [affecting businesses,] both of which will come into force on 1st October.

37. ~~For many~~ Ever since VAT was introduced in this country, we have treated imports differently from the way in which they are treated by all our main European Community competitors. In a nutshell, they charge VAT on imported goods/and we do not. Of course, ~~the VAT is eventually~~ even under our system the VAT is eventually paid, when the importer sells to his customer; but that is on average some three months later, during which time the importer has enjoyed free credit at the <sup>taxpayer's</sup> expense. ~~the VAT is eventually~~ This gives the imported product a small but unmistakable edge over its home-produced equivalent, since businesses buying from a UK supplier have to pay VAT straight away.

38. The UK system does indeed have many advantages, which is why the European Commission has for some years now been seeking to get it adopted throughout the Community, with the full support of both my predecessor and myself. But the plain fact is that in all that time the Commission has made no progress whatever, and we remain the odd man out.

39. I must tell the House that I am not prepared to put British industry at a competitive disadvantage any longer. Should our European partners at any time undergo a Damascene conversion, and all agree that the Commission's proposal should be accepted after all, then of course we would <sup>gladly</sup> revert to the present system. But in the meantime I propose to move to the system that prevails throughout the rest of the Community, and charge VAT on imports.





HOUSE OF COMMONS  
LONDON SW1A 0AA

40. In order to avoid ~~the risk of~~ congestion at the ports, I ~~propose~~ <sup>intend</sup> to make the same facilities for deferring payment as ~~have always~~ apply to customs duties. That means that most importers will be able to defer payment of VAT by on average one month after the date of importation. But that is all.

*(By bringing forward VAT receipts,*

41. As I have said, this change will apply from 1st October. <sup>extra</sup> It will bring in an ~~additional~~ £1.2 billion ~~in~~ in 1984-85, but there will of course be no increased ~~revenue~~ revenue in subsequent years.

42. The second change I propose to make on 1st October concerns the National Insurance Surcharge. This, once again, was a brainchild of the rt hon Member for Leeds East. Introduced in 1976 at the rate of ~~3 1/2~~ 2 1/2 per cent, he then raised it in 1978 ~~to~~ (check both dates) to 3 1/2 per cent. During the last Parliament, my predecessor succeeded in reducing it to 1 per cent, and we are ~~committed~~ pledged to abolish it during the lifetime of this Parliament.

~~43. In the Budget I have announced the Surcharge will be reduced to 1 per cent~~

43. Given the impact that this tax has, not only on industrial costs but also - at a time of high unemployment - on jobs, I have decided to take the opportunity of this my first Budget to fulfil that pledge. <sup>(Abolition of the National Insurance Surcharge)</sup> This will save private sector employers almost £350 million in 1984-85, and getting on for ~~a~~ £1 billion in 1985-86.

*add the run-up para on Surcharge*



Block K: Savings and Investment(a) Paragraph 16. IIS. Economic Secretary's comment:

"Since it will be difficult to sell the decision on IIS, I wonder whether you could set it in a broader theme. In 1979 we inherited a system with tax rates at confiscatory levels on income and capital. Geoffrey Howe reduced the top rate of tax on earned income to 60 per cent and DLT to the same figure. We are now proposing to remove the remaining punitive rates by abolishing IIS and reducing the top rate of CTT to 60 per cent also. (I am not sure whether there are any other taxes which stand above 60 per cent, but if so we ought perhaps to deal with them at the same time in this context). It would be easier to defend these decisions politically by deploying the argument that all rates above 60 per cent are punitive than by justifying them individually."

But Financial Secretary has advised caution. He wonders:

"Whether it will in fact be wise to make too much of the reduction of rates to 60 per cent. The only tax he can think of off hand which has a nominal rate above 60 per cent is Petroleum Revenue Tax. But we do risk criticism from the poverty trap lobby, who will point to marginal rates, of tax/loss of benefits, of more than 100 per cent. And if we say that all rates above 60 per cent are punitive, a number of Government supporters will protest immediately that rates a good deal less than 60 per cent are also punitive."

... (b) Further comments below from Mr Ridley.



(c) Stamp Duty: Convertible loan stock (Starter 160).  
The Financial Secretary wonders whether it would be worth mentioning in the Speech that loan stock convertible into other loan stock is already covered by the stamp duty exemption. If so it could come at paragraph 12.



Ridley

BLOCK K: Savings and Investment

A very general comment is appropriate here. There are many technical issues dealt with in this Section, which need very careful attention. In some cases - e.g. the composite rate - we assume a degree of knowledge which is excessive. In others - e.g. para 6 on Corporation Tax on Building Societies - it is impossible to know what is being referred to without detailed knowledge of the background.

Building Society taxation. In others still - e.g. para. 5 on the composite rate/<sup>on</sup>banks - we explain something will be simplified, without it being obvious in the slightest degree as to why there will be any simplification. In general this needs to be written with a much sharper eye to the ordinary listener, and to the many plus points which can be made. This also means explaining the rationale for some measures clearly, such as the life assurance premium in para. 7.

Para.7 Detailed Comments. I would extend this vital paragraph considerably, for example on something like the following lines:

"The original reason for this relief was to encourage life assurance in the strict sense of the term. For a long time now, however, life assurance policies have in truth very largely amounted to a way of saving, while the insurance element in a typical policy can become quite trivial. The effect of the relief is therefore to give a special privilege to money saved through this institutionalised route, and thus to discourage direct investment by and at the discretion of the individual in whatever kind of savings instrument he may chose. Clearly this is no good reason for, or advantage in, especially and generously bias in savings which are undertaken through an institutional route such as this; and there is every reason for eliminating the relative disadvantage which at present attaches to direct savings and investment by the individual. So I propose to withdraw..."



- Paras. 10 and 11 These would come far better before paragraph 9, which would then lead straight into the point about helping companies raise equity finance in para. 12.
- Para. 12. If we are not too worried about length, this might be a point at which to underline the importance of improving corporate finance, and referring to the already substantial increase in capital issues in the last two years.
- Para. 15. There could be a case for putting this after the first reference to stamp duty in para. 12, leaving the stamp duty section ending on the climax of paras. 13 and 14.
- Para. 19. Very few people have any inkling as to what Ramsay and Furniss amount to. Should we not at least say what kinds of tax they deal with? To the extent that we can?
- Para. 20. This is also very obscure. In particular one is at a total loss to know what is meant by the "reductions in the highest nominal rates of tax" at the end of the para. Rates of DLT and CTT? If that is the purpose, then we are suggesting that the value of these changes is far greater than they will in fact be, which will elicit needless hostility from the opposition and others.



*Block A*

continuing to rise at an annual rate of 3 per cent in 1984 we can be confident that the outlook for employment will continue to improve. *Expect*

THE MTFS

1. ~~16.~~ The Medium Term Financial Strategy has been the cornerstone of this Government's monetary and fiscal policy. It will continue to play that role; to provide a framework and discipline for Government itself and to spell out clearly to ~~businesses and consumers~~ *Industry & the financial markets* the clear guidelines of Government policy. Too often in the past Governments have ~~conducted monetary and fiscal policy in an ad hoc fashion, responding to each event as it happened.~~ *abandoned any attempt at financial discipline whenever the gov't got rough, and simply staggered from one to the next. This has proved the temptation* Such short-term policy expedients were damaging to longer term performance with the inevitable ~~tendency~~ *prone* to accommodate inflationary pressures, ~~and longer-term economic performance was progressively~~ *undermined.*

2. ~~17.~~ The MTFS was designed to remedy this, by imposing a discipline ~~on monetary and fiscal policies.~~ *framework which* It has been clearly successful. It has meant taking account of the effects of policies over a span of years and resisting the temptation to take the easy, inflationary way out. ~~It~~ *has* also ensured consistency between monetary and fiscal policies and a proper balance in the economy. *It is designed too, so that the more inflation comes down the more room is available for output & employment to grow.*

3. ~~18.~~ People now understand that the Government intends to stick to its medium term objectives. It is widely understood that output and employment will recover faster the more quickly inflation is reduced. The increasing realism and flexibility of the economy owes much to the pursuit of firm and consistent policies within the MTFS framework.

4. ~~19.~~ Originally the MTFS covered four years. In this first Budget of a new Parliament it is appropriate to carry the MTFS forward for five years. That is what I have done in the MTFS published to-day in the Financial Statement and Budget Report - the Red Book.

The objectives of policy are high employment, sustainable growth and ultimately price stability. The MTFS presents the monetary and fiscal framework designed to achieve these objectives. *Shows* It presents a continuing downward path for the monetary target

ranges over the next five years and a path for public borrowing consistent with ~~it.~~ *this. It* These take full account, ~~as they must,~~ of important influences such as the ~~pattern~~ *pattern* of our North Sea oil revenues, and the ~~programme~~ *level of* asset sales, ~~arising out of the privatization programme.~~ *For the last two years of the new MTFS, which it began the plan was in last month's Public Expenditure White Paper, the Government has not yet made firm plans for public spending. It is therefore assumed, for the purpose of the plan, that the level of public spending for 1988-89 is updated, in real terms, to 1987-88.*



20. The MTF S is designed to create the conditions in which sustainable growth and price stability can be achieved. Of course, the Government alone cannot determine precisely what happens to growth or inflation. How far the growth in demand is dissipated in rising prices and how far it comes in leads to higher output depends on the behaviour of employers and employees, on productivity on efficiency and on attitudes to pay.

21. The MTF S is designed so that the more inflation comes down the more room is available for output and employment to grow. Lower inflation and lower interest rates help cash flow, and encourage spending by companies and households. Public spending programmes drawn up in cash terms go further with lower inflation. And, most important of all, with low inflation, slower growth in pay makes room for more jobs.

22. The precise figures set out in the MTF S are not <sup>of course</sup> a rigid framework, lacking <sup>all</sup> any flexibility. As in the past, there may well need to be adjustments to take account of changing circumstances. But ~~it is the~~ <sup>it is</sup> the ~~strength of a medium-term strategy that such changes can be made~~ <sup>will</sup> without ~~jeopardising the consistent pursuit of the Government's objectives.~~ <sup>only if they can be</sup>

23. The winning combination of falling inflation and rising output which we have seen in the last two years is no accident. It has come about as the result of responsible financial policies, consistently applied, and increasingly better understood. At the heart of the MTF S is a recognition of the crucial importance of sound money, and proper monetary control. It is to monetary policy that I turn next.



~~RETRACT OF BLOCKS BC AND D BY SIR T. BURNS.~~

# THE ECONOMIC BACKGROUND

## DOMESTIC ECONOMY

1. There is now convincing evidence of low inflation and <sup>as</sup> recovery of output based upon the ~~the~~ pursuit of prudent monetary and fiscal policies.

2. Since 1980, inflation has fallen steadily from <sup>a)</sup> ~~the~~ peak of <sup>over</sup> more than 20 per cent. <sup>Last year</sup> In 1983 it was down to 4.6 per cent, the lowest <sup>figure</sup> ~~rate~~ since <sup>the</sup> ~~the~~ ~~late~~ ~~1970s~~. ~~Interest rates have fallen.~~ And low inflation has <sup>single</sup> ~~single~~ <sup>low</sup> ~~low~~ <sup>interest rates.</sup>

3. At the same time the <sup>underlying</sup> strength of the recovery has become widely recognised. Unlike previous cycles this recovery has not come from any self defeating stimulus to <sup>monetary</sup> demand but from re-establishing sound finance and ~~sound~~ <sup>house</sup> money. Lower inflation and lower interest rates have produced a better environment for industry and for business and consumer confidence. Recovery has emerged as a result of falling inflation making room for real growth, as we always said it would.

4. Across the economy, total money incomes <sup>grew</sup> in 1983 by about 8 per cent, <sup>of which</sup> ~~This well below the growth in the seventies but on this occasion, instead of being overwhelmingly represented by inflation last year 3 per cent represented real growth in output.~~ Although there is still room for improvement this is a <sup>very</sup> much healthier division between inflation and real growth than <sup>(with experience)</sup> in the 1970's. We now estimate that output in the second half of 1983 <sup>is now reckoned to have exceeded the 1979 pre-recession peak and previous peak in 1979, before the last recession, and is still rising strongly.</sup> ~~was above its peak level in 1979 before the world recession.~~

5. Productivity has continued to improve at a rapid pace. Just as many have erroneously and prematurely predicted an end to recovery so it has been suggested that the sharp rise in productivity <sup>the</sup> ~~was~~ <sup>(remarked on by my predecessor last year)</sup> ~~was~~ <sup>a flash in the pan. yet during 1983</sup> ~~one-off or 'short lived'.~~ Yet by the end of 1983, productivity in manufacturing industries ~~was~~ <sup>at</sup> about 10 per cent above the level three years earlier. Last year manufacturing productivity grew by 6 per cent with no sign of <sup>slowdown</sup> ~~slowdown~~ through the ~~year~~. We saw the smallest annual increase <sup>in</sup> ~~in~~ unit labour costs in manufacturing since records were first collected in 1970. It has allowed a ~~significant~~ <sup>(and necessary)</sup> ~~and~~ welcome ~~recovery~~ in real levels of profitability. But further progress is needed: although our increase in unit labour costs in 1983 was probably no more than (3) per cent, <sup>our three biggest competitors the</sup> ~~the three major large economies -~~ (US, Japan, <sup>and</sup> Germany - <sup>all</sup> secured a fall in unit labour costs over the latest 12 month period. ~~We~~ welcome the growth in productivity and its contribution to lower



unit labour costs, but the employment prospect would ~~obviously be still better~~ <sup>be significantly improved</sup> if ~~more of the necessary adjustments were to fall on wage costs,~~ <sup>a bigger contribution were made by lower pay rises.</sup>

6. Demand, output, profits and employment all rose <sup>last year.</sup> during 1983. Domestic demand has played a major part in <sup>the</sup> recovery so far. Lower inflation reduced ~~consumers' need~~ <sup>rose.</sup> to save and real incomes ~~are rising.~~ <sup>are rising.</sup> Personal consumption <sup>increase</sup> rose by nearly 4 per cent compared with 1982. Fixed investment rose rather faster than consumption, with investment in housing and services ~~being~~ particularly strong. ~~Total domestic demand grew by an estimated (4 1/2) per cent.~~

people's

7. Imports rose a little faster than <sup>home</sup> domestic demand last year, as ~~we~~ <sup>main</sup> emerged from recession ahead of our trading partners. ~~The~~ exports grew less rapidly than <sup>home</sup> domestic demand ~~reflecting weak world demand.~~ <sup>for the same reason.</sup> However, by the end of <sup>last year</sup> 1983 world trade was clearly moving ahead again and in the three months to January manufacturing exports increased substantially compared with the previous three months. The balance of payments on current account <sup>last year</sup> in 1983 is estimated to have been in surplus by about £2 1/2 billion, enabling us to secure a further increase in our <sup>income-earning</sup> assets overseas.

No UK

our own rate of economic growth last year has the highest in the European Community.

8. The UK is no longer regarded as the poor relation of the industrial world. We have emerged from the recession ahead of most of Europe, with the fastest rate of growth in the European Community last year.

*The sharp increase in profitability during the present recovery is particularly welcome, not least because higher profits*

9. ~~Growth in output and profitability~~ leads to more jobs. The number of people in employment increased by an estimated 87,000 between March and September last year. The loss of jobs in manufacturing has slowed down sharply, while <sup>last year.</sup> jobs in services increased by nearly 200,000 in the first nine months of 1983. This is encouraging news for the unemployed and those who will be leaving school ~~later~~ <sup>later</sup> this year. <sup>Summer.</sup>

10. <sup>Our</sup> Critics have been confounded by <sup>this</sup> the combination of recovery and low inflation. Even the pessimists <sup>have been forced to acknowledge</sup> can no longer doubt the strength of ~~the~~ recovery and that it is set to continue <sup>throughout this year.</sup> through 1984. Inflation is expected to remain low, edging down to 4 1/2 per cent by the end of this year. ~~Personal consumption,~~ <sup>personal consumption</sup> with rising incomes and low inflation, will continue to grow, but the recovery is already becoming more broadly based. Encouraged by higher profitability and better long-term growth prospects, investment



is forecast <sup>(expect)</sup> to rise by 6 per cent ~~in 1984~~. <sup>this year.</sup>

11. And as world trade expands, there will be increasing opportunities for exports. World economic prospects are more favourable now than for some time. Output in the United States should continue to grow strongly, ~~this year~~. And the recovery <sup>in spending (S)</sup> in the rest of the world ~~is spreading~~ with activity rising in Japan, and signs that the long-awaited upturn is at last getting under way <sup>(continued)</sup> in Europe. The benefits are beginning to spread to other countries and the pace of world trade is accelerating. <sup>British exports</sup> ~~In the UK we~~ stand to benefit from this recovery. over

Take  
in  
(A)  
what

12. Of course, there are inevitable uncertainties, and some real risks. The size and continued growth of United States budget deficit causes widespread concern. US interest rates, and - under their influence - international interest rates, are high, posing a threat to the revival of much needed investment and an immediate heavy burden on debtor countries. The US has hitherto attracted foreign capital to match an enormous and still rising current account deficit, and the dollar has been very strong. But this adds to the pressures for protectionism now and increased the risks of more volatile exchange rates later.

13. A second potential risk is disruption in the oil market. The immediate prospects <sup>are</sup> may be less obviously volatile than <sup>they were a year ago. But</sup> on some past occasions, and the <sup>uncertainties remain, and the United Kingdom market remains vulnerable to</sup> prospects of continuing gradual world recovery should be a steadying influence. But we cannot afford to overlook the disruptions which could be caused, particularly for the United Kingdom, by any major disturbances in these markets.

14. <sup>But</sup> Despite these risks there is a growing sense <sup>throughout the industrial</sup> in North America, Japan and Europe <sup>world that the</sup> that the world recovery this time is not <sup>months</sup> ~~simply~~ cyclical, but one which can be sustained. The essential requirement is the pursuit of prudent monetary and fiscal policies.

15. <sup>(continued)</sup> That is the way forward for the UK ~~also~~ and the path we intend to take. Inflation has fallen, and is set to fall further. Output has been recovering steadily, ~~for two years~~, and there are sound reasons for expecting this growth to continue. It can no longer be doubted that steady growth can be combined with falling inflation if the <sup>appropriate</sup> ~~right~~ policies are followed. And with output <sup>continuing to rise at an annual rate of 3 per cent in 1984</sup> the outlook for employment <sup>should improve still further.</sup>



12. of cont.

There are inevitable uncertainties, and some real risks.

(not leak within the United States itself. As a direct consequence of their deficit,)  
The size and continued growth of United States budget deficits <sup>has</sup> is causing cause widespread concern, US interest rates, and ~~under their~~

<sup>thus</sup> influence international interest rates, <sup>(abnormally)</sup> are high, posing a ~~threat~~ <sup>in real terms,</sup>

~~threat to the revival of much needed investment and an~~ <sup>imposing no progress toward recovery and thereby exacerbating the</sup>

~~immediate heavy burden on debtor countries.~~ <sup>(To finance its massive budget deficit)</sup> The US has

~~hitherto attracted foreign capital to match an enormous and~~ <sup>The US has to attract</sup> on a vast scale, thus producing

~~still rising current account deficit, and the dollar has been very~~ <sup>an increasingly strong dollar and hence a growing balance of</sup>

~~strong.~~ <sup>payments deficit on current account. (within the United States)</sup> But this adds to the pressures for protectionism now

and increases the risks of more volatile exchange rates later.

A

ADLA

BUDGET-SECRET



- 21. [BES & farming: to be drafted to minimise awkwardness of the selective & arguably distortionary nature of the relief, but rather better than IR's attempt]
- 22. [LGS: probably not in at all; but have a cockshy - you know my views]
- 23. [former 18 as amended]
- 24. [former 19 as amended] [...but add reference to abuses]
- 25. [former 20 as amended, but add colourful example of abuse]
- 26. " 21 " " " " " " " "
- 27/35 " 22/30 " " \*

*NB: Paras (old) 19-23, 27 & 28  
 are in fact all income tax matters,  
 and do not pass (?) go in that  
 section. But no first time to  
 do it get no drafting work.  
 \* at the start of it*



B(84) 785

FROM: A M W BATTISHILL  
DATE: 2 March 1984

COPY NO:

CHANCELLOR OF THE EXCHEQUER

- cc Chief Secretary
- Financial Secretary
- Minister of State
- Economic Secretary
- Sir P Middleton
- Sir T Burns
- Mr Littler
- Mr Bailey
- Mr Anson
- Mr Cassell
- Mr Monck
- Mr Evans
- Mr Lankester
- Mr Monger
- Mr Odling-Smee
- Mr Ridley
- Mr Lord
- Mr Hall
- Mr Portillo
- Sir L Airey ) IR
- Mr Painter )
- Mr Fraser ) C&E
- Mr Wilmott )

all  
without  
attachments

BUDGET SPEECH

... Attached to this minute is a copy of the second draft of the Budget Speech, annotated with comments and suggestions from Ministers, Advisers and officials (Mr Kerr's minute to me of 28 February). For ease of identification, comments from your Ministerial colleagues are shown in red. And we have used a simple coding for the remainder.

2. Inevitably some passages have attracted comments from several quarters; and we have had to use a certain amount of editorial discretion in showing alternative suggestions. But even so, there are some genuinely conflicting suggestions which you need to see; and I apologise for the fact that in one or two places the drafting becomes a little difficult to untangle. We have had to use manuscript in order to squeeze as much as possible onto each page. In one or two cases, where comments are more substantial or involve complete restructuring of passages, it seemed more helpful to show you these separately, alongside the relevant Sections.

*AWB*  
A M W BATTISHILL



4. At this stage figures in the text are not all necessarily up-to-date. Nor have we been able to reflect in this draft the changes decided this morning in the phasing out of the foreign earnings and foreign emoluments deductions. But these can come in on the next round.

5. The draft has come out no shorter than last week: indeed, I am afraid it is a shade longer. But once the general shape and structure is in place it should not be difficult to reduce the number of words.

amb/

A M W BATTISHILL



BUDGET SPEECH: SECOND DRAFT

Block

- ✓ A Introduction
- ✓ B <sup>Economic</sup> World Background
- ~~C Domestic Economy~~
- ✓ D MTFS
- \* E Monetary Policy
- ✓ F Public ~~Expenditure~~ <sup>Expenditure</sup>
- ✓ G Public ~~Borrowing and Interest Rates~~
- ✓ H Tax Reform
- ✓ I ~~Indirect Taxes~~ <sup>Savings & Investment</sup>
- ✓ J Taxation of ~~Profits and Capital~~ <sup>Business</sup>
- ✓ K ~~Savings and Investment~~ <sup>Phase Tax / Indirect taxes</sup>
- ✓ L Income Tax
- \* M Conclusion

Para on CS numbers  
for drafts by JOK  
& make something

Positioning  
arguments  
for 2 regions

last para 9-?

Call for  
P. J. ...



[block J - PAS] NEW Customs DRAFT

7

20. I am also making changes in the system by which VAT is charged on the importation of goods into the United Kingdom. Businesses buying from UK suppliers have to pay VAT, and must rely on whatever commercial credit is available to finance it before they can claim it back from the Customs. But importers do not have to finance the VAT due on their imports - it is effectively the Government that does so. Our main EEC competitors apply a different system, and generally charge VAT at import. I propose now to adopt the same procedure. But I intend to make available the same facilities for deferring payment as for customs duties. This means that most importers will be able to pay VAT on average 4 weeks after the date of importation.

21. I am aware of the European Commission's proposals to harmonise on the basis of our present system, in the interests of simplifying customs formalities and freeing the flow of goods. If other Member States were to agree to this approach, there would be a good case for reconsidering the United Kingdom position. But until this happens - and there are no signs of it at present - I see no reason to continue as 'odd-man-out' in Europe.

22. This change will apply from 1 October, and will provide a once-for-all revenue gain of the order of £1.2 billion.