

PO-CH/NL/0013

PART E



PO CH/NL/0013  
PART. E

PO. CH/NL/0013  
PART. E.

1987 BUDGET  
STATEMENTS.

DD's 2548 NAJG  
14/11/96.

THIS FOLDER HAS BEEN  
REGISTERED ON THE  
REGISTRY SYSTEM



PWF

From: N MONCK

Date: 12 March 1987

PRINCIPAL PRIVATE SECRETARY

cc Financial Secretary

Sir P Middleton

Mr Scholar

Miss O'Mara

Miss Sinclair

Mr P Gray

Mr Hudson

Mr McManus, IR

Mr P Lewis, IR

BUDGET STATEMENT : FIFTH DRAFT

After discussion involving the Revenue, Miss Sinclair and me, I should like to propose a redraft which I hope is both more precise and clearer. In particular, it would bring out two points: that the main aim of the new proposal is to cover training paid for by an employer for an employee who is about to leave his existing employer; and that the change will help both the employer and the employee. The proposed text is:

"Training and retraining are vital to a flexible and competitive economy. Some employers may be willing to help with the retraining of workers who are leaving their current employment, perhaps for another job or to become self-employed. At present if employers finance such training, the employee and in some cases the employer will generally be liable to tax on the cost. I propose that both employers and employees should be exempt from tax in this kind of case. This should encourage both employers and employees to undertake training in new skills for new jobs."

2. I also have comments on paragraph B6 which describes recent employment measures.

3. In line 5 I suggest splitting the long first sentence after "the long term unemployed." then cut out "so that," so that the next sentence can begin "Starting next month ...".

4. Delete "Again," at the beginning of the second line: it might suggest that there had also been a quadrupling of the Enterprise Allowance mentioned in the



previous sentence. The next few lines could be amended as follows:

"And once fully under way, the new Job Training Scheme will give a quarter of a million others, most of them young people, vocational training leading to recognised qualifications. These measures give carefully targetted and practical help to the unemployed. Together with our other schemes, including the two year YTS, this Government has developed its employment and training programmes on a scale no other country can match. But the best hope ..."

Ask | 5. The point of the changes is that Lord Young does not like YTS being treated as a way of reducing unemployment and similarly prefers to stress the training rather than the work experience content of the JTS. I have cleared the proposed text with my opposite number at DE. This overtakes but is consistent with Mr Rayner's note of 11 March.

R Jachse  
pp N MONCK



From: N MONCK

Date: 12 March 1987

P. W. P.

PRINCIPAL PRIVATE SECRETARY

cc Financial Secretary

Sir P Middleton

Mr Scholar

Miss O'Mara

Miss Sinclair

Mr P Gray

Mr Hudson

Mr McManus, IR

Mr P Lewis, IR

Mr Hudson  
 Here is my sketch. Delay  
 due to Mrs to check in int  
 FP + 102. But I have found.

BUDGET STATEMENT : FIFTH DRAFT

Mar 12/3

After discussion involving the Revenue, Miss Sinclair and me, I should like to propose a redraft which I hope is both more precise and clearer. In particular, it would bring out two points: that the main aim of the new proposal is to cover training paid for by an employer for an employee who is about to leave his existing employer; and that the change will help both the employer and the employee. The proposed text is:

"Training and retraining are vital to a flexible and competitive economy. Some employers may be willing to help with the retraining of workers who are leaving their current employment, perhaps for another job or to become self-employed. At present if employers finance such training, the employee and in some cases the employer will generally be liable to tax on the cost. I propose that both employers and employees should be exempt from tax in this kind of case. This should encourage both employers and employees to undertake training in new skills for new jobs."

2. I also have comments on paragraph B6 which describes recent employment measures.
3. In line 5 I suggest splitting the long first sentence after "the long term unemployed." then cut out "so that," so that the next sentence can begin "Starting next month ...".
4. Delete "Again," at the beginning of the second line: it might suggest that there had also been a quadrupling of the Enterprise Allowance mentioned in the



From: N MONCK

Date: 12 March 1987

PRINCIPAL PRIVATE SECRETARY

cc Financial Secretary

Sir P Middleton

Mr Scholar

Miss O'Mara

Miss Sinclair

Mr P Gray

Mr Hudson

Mr McManus, IR

Mr P Lewis, IR

BUDGET STATEMENT : FIFTH DRAFT

After discussion involving the Revenue, Miss Sinclair and me, I should like to propose a redraft which I hope is both more precise and clearer. In particular, it would bring out two points: that the main aim of the new proposal is to cover training paid for by an employer for an employee who is about to leave his existing employer; and that the change will help both the employer and the employee. The proposed text is:

"Training and retraining are vital to a flexible and competitive economy. Some employers may be willing to help with the retraining of workers who are leaving their current employment, perhaps for another job or to become self-employed. At present if employers finance such training, the employee and in some cases the employer will generally be liable to tax on the cost. I propose that both employers and employees should be exempt from tax in this kind of case. This should encourage both employers and employees to undertake training in new skills for new jobs."

2. I also have comments on paragraph B6 which describes recent employment measures.
3. In line 5 I suggest splitting the long first sentence after "the long term unemployed." then cut out "so that," so that the next sentence can begin "Starting next month ...".
4. Delete "Again," at the beginning of the second line: it might suggest that there had also been a quadrupling of the Enterprise Allowance mentioned in the



previous sentence. The next few lines could be amended as follows:

"And once fully under way, the new Job Training Scheme will give a quarter of a million others, most of them young people, vocational training leading to recognised qualifications. These measures give carefully targetted and practical help to the unemployed. Together with our other schemes, including the two year YTS, this Government has developed its employment and training programmes on a scale no other country can match. But the best hope ..."

5. The point of the changes is that Lord Young does not like YTS being treated as a way of reducing unemployment and similarly prefers to stress the training rather than the work experience content of the JTS. I have cleared the proposed text with my opposite number at DE. This overtakes but is consistent with Mr Rayner's note of 11 March.

pp R Jackson  
N MONCK



## BUDGET CONFIDENTIAL



FROM: P D P BARNES

DATE: 12 MARCH 1987

✓  
 PS/CHANCELLOR

AAH For ACSA.

cc PS/Chief Secretary  
 PS/Financial Secretary  
 PS/Minister of State  
 Sir P Middleton  
 Sir T Burns  
 Sir G Littler  
 Mr F E R Butler  
 Mr Wilson  
 Mr Cassell  
 Mr Monck  
 Mr Scholar  
 Mr Sedgwick  
 Mr Odling-Smee  
 Mr Culpin  
 Miss O'Mara  
 Miss Sinclair  
 Miss Evans  
 Mr Cropper  
 Mr Tyrie  
 Mr Ross Goobey  
 Mr Battishill IR  
 Mr Isaac IR  
 Mr Painter IR  
 Mr Beighton IR  
 Mr McManus IR  
 Sir Angus Fraser C&E  
 Mr Knox C&E  
 Mr Wilmott C&E  
 Mr Bone C&E

## BUDGET STATEMENT SECOND DRAFT

The Economic Secretary has seen your minute to Mr Scholar of 11 March.

2. He had the following further comments:-

- (i) C5. He thinks this looks a bit spare. He wondered whether this would not come better, with minor adjustments, before Cl.

*You are considering anyway.*



BUDGET CONFIDENTIAL

(ii) D4. The Economic Secretary thinks that the phrase "an increasingly profitable business and industry" reads oddly. He wondered whether the Chancellor had meant to say this.

Could say  
"business sector"  
industry

(iii) F25. The Economic Secretary thought that the first sentence might read better if it began "As for the other Capital Taxes, their severity has also been significantly eased since we first took office, with the consequence that the yield....."

P. Cropper  
You accepted  
P. Cropper's redraft  
here, which I prefer.

(iv) H8. The Economic Secretary thinks that "marginal rate" is jargon and would be incomprehensible to most people. He thinks he may have made this point before, but wonders whether "only rate" would not be preferable.

He has, & you  
didn't take it!

RB

P D P BARNES  
Private Secretary



## BUDGET SECRET

COPY NO 1 OF 3 COPIES

From: SIR PETER MIDDLETON

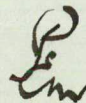
Date: 12 March 1987

CHANCELLOR

*Last done -  
 best letter  
 compromise  
 for the House  
 by White  
 reason:*

BUDGET SPEECH

The speech reads well now. But I still dislike paragraph C5. It has a strangely defensive ring in an otherwise positive presentation. And following C4 it means there are three references to non-House events. The point is a good one, but it might be left for your speech in the Debate, or for use with the press. It is, of course, an excellent Select Committee point.



P E MIDDLETON



FROM: SIR T BURNS

DATE: 12 March 1987

CHANCELLOR

cc Sir Peter Middleton  
 Mr Cassell  
 Mr Odling Smee  
 Mr Scholar  
 Mr Sedgwick  
 Mr Culpin  
 Miss O'Mara  
 Mr Ross Goobey

*Thanks  
 my formulation, but  
 like Terry's  
 approach as well  
 in the budget.*

BUDGET STATEMENT

We spoke earlier today about paragraph B3 which says;

"Indeed, we have now enjoyed the longest period of steady growth, at a rate approaching 3 per cent, that the UK economy has known since the War."

Your interpretation of this was that the annual growth rate over each of the past 4 years had been above 2 1/2 per cent. The complication is that the 4 years, 1976-79 were not so different.

You were inclined to change the formulation to include the projected figure for 1987 as you can say, unambiguously, that there is no other 5 year period of growth consistently above 2 1/2 per cent. But the statement would rely on a forecast.

Another approach is to use the fact that the standard deviation of the growth rate over the past five years is the lowest since the war. The figures are shown on the attached table along with similar figures for 6 and 7 year periods. By this criterion, the five years to 1986 is the "stadiest five year period of growth



since the war". This could be combined with the achieved average growth rate to produce the following statement;

"Indeed, over the past five years we have enjoyed the steadiest period of growth that the UK economy has known since the War, at a rate approaching 3 per cent."



T BURNS



# GOP at constant factor cost

## Annual Growth Rate

1949	3.70
1950	3.57
1951	1.83
1952	0.60
1953	3.76
1954	4.20
1955	3.48
1956	1.42
1957	1.57
1958	-0.34
1959	3.97
1960	5.64
1961	2.51
1962	1.38
1963	4.08
1964	5.52
1965	2.89
1966	1.74
1967	2.23
1968	4.24
1969	2.34
1970	2.05
1971	1.42
1972	2.56
1973	7.26
1974	-1.69
1975	-0.97
1976	2.61
1977	2.65
1978	2.89
1979	2.61
1980	-2.25
1981	-1.20
1982	1.52
1983	3.39
1984	2.80 →
1985	3.38
1986	2.63

P. Almon + 5388

### MOVING AVERAGE OF GROWTH RATES

### STANDARD DEVIATION OF GROWTH RATES

	MOVING AVERAGE OF GROWTH RATES			STANDARD DEVIATION OF GROWTH RATES		
	5yo	6yo	7yo	5yo	6yo	7yo
1953	2.69			1.42		
1954	2.79			1.52		
1955	2.77	2.94		1.51	1.41	
1956	2.69	2.91	3.02	1.59	1.39	1.30
1957	2.89	2.55	2.69	1.59	1.46	1.39
1958	2.06	2.50	2.41	1.30	1.49	1.38
1959	2.02	2.35	2.10	1.80	1.76	1.73
1960	2.45	2.38	2.58	1.74	1.79	1.72
1961	2.67	2.62	2.85	2.35	2.14	2.05
1962	2.63	2.46	2.61	2.28	2.10	1.96
1963	2.63	2.45	2.31	2.31	2.11	1.96
1964	3.51	2.87	2.69	1.63	2.15	2.02
1965	3.82	3.85	3.25	1.87	1.67	2.20
1966	3.27	3.67	3.71	1.58	1.71	1.57
1967	3.12	3.02	3.39	1.71	1.55	1.72
1968	3.29	2.97	2.91	1.52	1.57	1.44
1969	3.32	3.45	3.15	1.54	1.42	1.51
1970	2.69	3.16	3.29	0.96	1.44	1.36
1971	2.52	2.58	3.00	0.99	0.90	1.38
1972	2.46	2.34	2.42	1.06	0.99	0.93
1973	2.52	2.47	2.37	1.05	0.95	0.91
1974	3.13	3.31	3.16	2.35	2.15	2.01
1975	2.32	2.32	2.60	3.22	2.88	2.73
1976	1.72	1.77	1.85	3.55	3.18	2.91
1977	1.95	1.86	1.89	3.57	3.20	2.92
1978	1.97	2.07	1.98	3.57	3.20	2.93
1979	1.10	2.12	2.19	2.23	3.21	2.94
1980	1.96	1.35	2.19	1.64	2.09	2.94
1981	1.70	1.26	0.83	2.21	2.76	2.34
1982	0.94	1.22	0.91	2.46	2.31	2.26
1983	0.71	1.04	1.26	2.31	2.21	2.11
1984	0.81	1.16	1.37	2.44	2.34	2.21
1985	0.85	1.14	1.39	2.47	2.33	2.22
1986	1.98	1.27	1.46	1.93	2.44	2.29
	2.74	2.09	1.47	0.76	1.75	2.29



COPY NO / OF 8 COPIES

FROM: SIR T BURNS

DATE: 12 March 1987

CHANCELLOR

*Thanks. On aspect  
TJBs, says of say  
'since 1950?'*

- cc Sir Peter Middleton
- Mr Odling Smee
- Mr Scholar
- Mr Sedgwick
- Mr Culpin
- Miss O'Mara
- Mr Ross Goobey

*P.S. In this para  
take a PSBR than.  
The purchaser  
protects  
add-back  
is a - 11-*

BUDGET STATEMENT

I mentioned to you earlier today that the final sentence of paragraph D7 may not be correct. I attach a table of relevant information that Mr Odling Smee has put together.

The PSBR as a percentage of GDP has only been less than 1 per cent of GDP in two years since 1952 when our figures begin. But we do have figures for the PSFD before 1952. These show a surplus in the late 1940's and if we were able to compute the PSBR I am reasonably confident it would be less than 1 per cent.

6. I would prefer to say;

"That will maintain a level for the PSBR that, until this year, had been recorded on only two occasions since the early 1950's."

T BURNS



PSBR and PSFD as % of GDP

	PSBR	PSFD	Difference (PSBR - PSFD)	
1946	n.a.	(6.2) <sup>1</sup>		
1947	n.a.	(1.3) <sup>1</sup>		<sup>1</sup> GDP figures approximate
1948	n.a.	-2.2		
1949	n.a.	-2.4		
1950	n.a.	-2.6		indicates
1951	n.a.	1.6		PSBR ≤ 1.0
1952	5.0	3.5	1.5	PSFD ≤ 2.3
1953	3.5	4.1	-0.6	
1954	2.1	2.4	-0.3	
1955	2.4	2.0	0.4	
1956	2.7	2.6	0.1	
1957	2.2	2.4	-0.2	
1958	2.1	1.9	0.2	
1959	2.3	2.2	0.1	
1960	2.7	2.7	0.0	
1961	2.5	2.6	-0.1	
1962	1.9	1.8	0.1	
1963-64	3.3	3.3	0.0	
1964-65	2.6	2.3	0.3	
1965-66	2.6	1.7	0.9	
1966-67	2.9	2.6	0.3	
1967-68	4.9	4.2	0.7	
1968-69	0.8	0.8	0.0	
1969-70	-1.2	-1.7	0.5	
1970-71	1.5	-0.5	2.0	
1971-72	1.6	1.1	0.5	
1972-73	3.6	3.0	0.6	
1973-74	5.8	4.6	1.2	
1974-75	9.0	6.7	2.3	
1975-76	9.3	7.4	1.9	
1976-77	6.4	5.8	0.6	
1977-78	3.6	4.4	-0.8	
1978-79	5.3	4.9	0.4	
1979-80	4.8	3.9	0.9	
1980-81	5.4	5.0	0.4	
1981-82	3.3	2.2	1.1	
1982-83	3.1	3.0	0.1	
1983-84	3.2	4.0	-0.8	
1984-85	3.1	4.2	-1.1	
1985-86	1.6	2.3	-0.7	
1986-87	1.1	2.8	-1.7	
1987-88	1.0	2.3	-1.3	





FROM: FINANCIAL SECRETARY  
DATE: 12 March 1987

CHANCELLOR

cc Chief Secretary  
Economic Secretary  
Minister of State  
Sir P Middleton  
Sir T Burns  
Mr Scholar  
Mr Culpin  
Miss O'Mara  
Mr Cropper  
Mr Ross Goobey  
Mr Tyrie  
Mr Prescott IR

*Ask. A. Davis, with Mr. ...*

**BUDGET STATEMENT: FIFTH DRAFT**

I have three comments on your latest draft.

2. As it stands the Statement makes no mention of the three measures we are taking to help the continued growth of employee share ownership - the "material interest" changes; permitting share options to be "rolled over" when a company is taken over; and the review of Section 79 (which, I am sure, will be widely welcomed). I do think there is a good story to tell here, and this bundle of (admittedly small) measures is a useful peg on which to hang it!

*Quite. Reject? FS? can do*

*all this himself on Wednesday night.*

3. On the pensions issue, do you think it might be sensible to stress that "personal pensions" are not simply about choice and flexibility, they are the best way to ensure that, in the long-term, there is adequate provision for old age?

*✓ Could say <sup>this</sup> at end of ~~the~~ F7. But ARG thinks it's too complex, & I also think it's controversial - what about dig at SERPS. Ignore?*



4. In the income tax section could we not inject just a hint of the "lower taxes - more revenue" argument in suitably guarded terms? My suggestion would be to insert a new passage after the first sentence in H3:

"Those who criticise tax cuts and advocate more public spending pose a false choice. Lower direct taxes can bring higher revenues by improving the performance and the growth rate of the economy <sup>EST</sup> and indeed they have done so."

5. You could also add as a final sentence in this paragraph:

"Equally, higher income taxes will mean slower growth, fewer jobs and less money to spend on public services."

*N*

NORMAN LAMONT



*flw*

FROM: FINANCIAL SECRETARY  
DATE: 13 March 1987

CHANCELLOR

cc Chief Secretary  
Economic Secretary  
Minister of State  
Mr Scholar  
Miss O'Mara  
Mr Hudson  
Mr Cropper  
Mr Tyrie  
Mr Ross Goobey  
Mr Mace IR

**BUDGET STATEMENT: SIXTH DRAFT**

I have just two further comments on your draft speech.

2. In H-11, I would delete "a married man" in the last line and insert "anyone, single or married". The background is in my note of today on "Who Gains Most?" which you will have seen. The point is that unlike changes in allowances, a cut in the basic rate is worth more to single people than married couples (except at the top-end of the income distribution).

3. Concentrating our presentation on the married man is appropriate for when we raise allowances, but focussing on single people is better when we are able to cut the basic rate.

4. Second, as you know I do think there are strong political arguments for hinting at the "cut taxes to increase receipts" issue. (See my note of 12 March and Ian Stewart's of 13 March).

NORMAN LAMONT



**BUDGET SECRET  
BUDGET LIST ONLY**

REF: M 87/8  
**NOT TO BE COPIED**  
COPY NO 2 OF 5

**BUDGET**

FROM: A P HUDSON  
DATE: 12 March 1987

CHANCELLOR

cc Mr A C S Allan

**BUDGET STATEMENT**

I attach the present draft, incorporating the amendments you made yesterday evening.

**SECRET**

*Nigel Jones*  
pp. A P HUDSON

**B.L.O.**

**SECRET**

**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**A. INTRODUCTION**

A1. The setting for this year's Budget is more favourable than it has been for very many years. We are entering our seventh successive year of steady growth, at the top of the international league table. We are entering the fifth year in which this steady growth has been combined with low inflation. The public finances are sound and strong, and unemployment is falling.

A2. These are the fruits of the Government's determination, in bad times as well as good, to hold firmly to our policies of sound money and free markets. Once again, I reaffirm those policies.

A3. So the Budget I present today is a Budget built on success, and a Budget for success.

A4. I shall begin, as usual, by reviewing the economic background to the Budget. I shall then turn to monetary policy and to the fiscal prospect this year and next. Finally, I shall propose some changes in taxation designed to improve still further the prospects that lie before us. A number of press releases, filling out the details of my proposals, will be available from the Vote Office as soon as I have sat down.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**B. THE ECONOMIC BACKGROUND**

B1. I start with the economic background.

B2. Nineteen eighty-six was dominated by the sudden collapse of the oil price. Our own economy was affected not only directly, as a major oil producer and exporter, but also by the pause in world growth as the world economy adjusted to what has been described as the third oil shock. Despite this dislocation, however, the economy has developed in most respects as I foreshadowed a year ago.

B3. In 1986 as a whole output grew by a further  $2\frac{1}{2}$  per cent or so, which compares well with the experience of other industrialised countries. ~~Indeed, we have now enjoyed the longest period of steady growth, at a rate approaching 3 per cent, that the UK economy has known since the war. It is also~~ worth recalling that in the 1960s, and again in the 1970s, Britain's growth rate was the lowest of all the major European economies. By contrast, during the 1980s, our growth rate has been the highest of all the major European economies.

B3A. And this greatly improved growth performance has coincided with falling inflation, which at



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



3½ per cent in 1986 recorded the lowest figure for almost 20 years. Over the lifetime of this Parliament, inflation has averaged less than 5 per cent.

B4. During the first half of last year exports and hence output were affected by the pause in world growth to which I have already referred. But since the middle of the year exports have grown strongly. Indeed, over the last three months the volume of non-oil visible exports was almost 10 per cent higher than a year earlier - a better performance than that of any other major economy. This pattern was reflected in the rapid growth of manufacturing output in the second half of last year.

B5. This resurgence of economic growth, coupled with the special measures we have taken, has brought about a welcome fall in the number of people out of work. Since August unemployment has fallen by more than 100,000; the largest six-monthly fall since 1973. Though the numbers out of work are still far too high, both youth unemployment and long-term unemployment are now lower than they were a year ago.

B6. I announced a number of specific employment measures in my last Budget, and since then, my Rt Hon and Noble Friend the Secretary of State for



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



BUDGET

Employment has further extended the successful Restart programme for the long-term unemployed. Starting next month, all those who have been unemployed for more than six months will be offered Restart interviews twice a year, to give them individual advice and help. There will also be more places on the successful Enterprise Allowance Scheme, helping unemployed people to set up their own businesses. Again, the number of Jobclubs is to be quadrupled, with room for 150,000 people a year. And once fully under way, the new Job Training Scheme will give a quarter of a million others, most of them young people, work experience and vocational training. Together with the Youth Training Scheme and other programmes, what this means is that this Government has developed its employment and training measures on a scale which no other country can match. But the best hope of all for the unemployed lies in the continuing vigour of the economy.

5  
B7. Since the early months of last year, there has been a further surge in manufacturing productivity. This continues the remarkable improvement in productivity growth achieved by British industry throughout the 1980s. In the 1960s, and again in the 1970s, growth in manufacturing productivity in the UK was the lowest of all the seven major industrial countries in the world. During the



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



1980s, our annual rate of growth of output per head in manufacturing has been the highest of all the seven major industrial countries.

<sup>9</sup>B8. The recorded current account of the balance of payments went into deficit in 1986 by around £1 billion. This followed a cumulative current account surplus of some £20 billion between 1979 and 1985. Some deterioration in our current account was inevitable in the face of a £5 billion loss of earnings on oil trade virtually overnight. But the significance of this should not be exaggerated. The exchange rate adjustment that followed the fall in the oil price is already contributing to an improved non-oil trade performance. And earnings from the massive stock of net overseas assets we have acquired since 1979, which at well over £100 billion is second only to that of Japan, will provide a continuing support to the current account in the years ahead.

<sup>10</sup>B9. Looking ahead, I expect 1987 to be another year of steady, balanced growth with low inflation. Total output is forecast to rise by 3 per cent, with exports and investment up rather more than that. Manufacturing industry, in particular, should do well, <sup>in 1987.</sup> And with the non-oil economy set to grow at 3½ per cent, there is every prospect of unemployment continuing to fall throughout <sup>the year.</sup> 1987. In last year's

BUDGET

SECRET

BUDGET

SECRET

By then we will have registered the longest period of steady growth, at a rate approaching 3 per cent a year, that no one could have known since the war.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



Budget Speech I said that the outlook for jobs depended on a sustained improvement in the performance of business and industry. That sustained improvement in economic performance has occurred and is continuing.

B10. Despite the strong growth in exports, it will inevitably take time for the full effect of the exchange rate adjustment to work through. The current account is thus likely to remain in deficit this year, by some £2½ billion, around half of one per cent of GDP.

B11. As I foreshadowed in the Autumn Statement, inflation may continue to edge up for a time, perhaps to a little over 4½ per cent by the Summer, before falling back to 4 per cent by the end of the year. While short-term fluctuations are inescapable, it remains the Government's prime objective to keep inflation on an unambiguously downward underlying trend. ◊

B12. Given the continuation of present policies in this country, the biggest risk to the excellent prospect I have outlined is that of a downturn in the world economy as a whole. There are still serious imbalances afflicting the three major economies - the United States on the one hand and Japan and Germany on the other - which, if not



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



handled properly, could lead to a simultaneous downturn in all three. And this in turn could be exacerbated by renewed turmoil in the foreign exchange markets, whose tendency to overshoot is as notorious as it is damaging.

<sup>4</sup>Bl3. It was to address these dangers that the Finance Ministers and Central Bank Governors of six major nations met in Paris last month, and agreed among other things to co-operate closely in fostering a period of exchange rate stability. In my Budget Speech last year, I said:

"Provided we are not over-ambitious, I believe that the Plaza accord is something we can usefully build on."

That is what we have now done, with Plaza II. But it would be idle to deny that the wider risks still remain.

<sup>5</sup>Bl4. Short of a world downturn, which can and must be avoided, British industry now has an outstanding opportunity, with growing markets at home and overseas, low inflation, rapidly growing productivity and greatly improved profitability. Provided it can control its costs and maintain its present competitive advantage, and assuming the continuation of present policies, we can look forward to many more years of strong growth combined with low inflation.



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**

**C. MONETARY POLICY**

C1. For its part, the Government will keep in place a sound and prudent financial framework. That means, as it has done since 1980, the medium-term financial strategy.

C2. The central objective of the MTFS is steadily to reduce the growth of money GDP over the medium term, so as to squeeze inflation out of the system and ultimately to achieve price stability.

C3. This requires monetary discipline buttressed by low public sector borrowing. The essential instrument of monetary policy must remain short term interest rates. These will continue to be set in the light of monetary conditions as indicated principally by the growth of narrow and broad money and the behaviour of the exchange rate.

C4. For narrow money, M0, the target range for next year will be 2 to 6 per cent, as foreshadowed in last year's MTFS. For broad money, however, as the Governor of the Bank of England cogently argued in his Loughborough lecture last October, in current circumstances it is probably wiser to eschew an explicit target altogether. But broad money will continue to be taken into account in assessing

**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**

monetary conditions, as of course will the exchange rate.

C5. In my Lombard Association speech last April, I set out at considerable length precisely how in practice monetary policy is operated. While I note that in some quarters this was felt to be unclear or in some other way unsatisfactory, I am struck by the fact that Mr Paul Volcker, Chairman of the United States Federal Reserve Board, in his written testimony to the Senate last month, explained how the Fed operates monetary policy in remarkably similar terms.

**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**D. PUBLIC SECTOR BORROWING**

D1. I mentioned a moment ago the need to keep public sector borrowing low.

D2. The final outturn for the public sector borrowing requirement last year, 1985-86, was just under £6 billion, equivalent to  $1\frac{1}{2}$  per cent of GDP, the lowest level since 1970-71. In my Budget last year, faced with a massive loss of what now looks like £7 billion of North Sea oil revenue, I nonetheless decided to hold the PSBR for this year, 1986-87, to £7 billion, or  $1\frac{3}{4}$  per cent of GDP.

D3. In the event, this year's PSBR looks like turning out at only £4 billion, or 1 per cent of GDP: the second successive year of significant undershoot.

D4. This successful outcome is chiefly attributable to the remarkable buoyancy of non-oil tax revenues. And this in turn is due not to some short-term surge in consumer spending, but in particular to an increase over last year of no less than a third in the yield of Corporation Tax from an increasingly profitable business and industry.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



D5. Looking ahead, there is still a degree of uncertainty surrounding oil prices, and I have therefore stuck to the assumption I made last year that the North Sea price will average \$15 a barrel. But it is clear that the increased flow of non-oil tax revenues, coupled with the prospective further growth of the economy in excess of the growth of public expenditure, puts the public finances in an exceptionally strong position.

D6. I intend to keep it that way. Last year's MTFS indicated a PSBR for 1987-88 of £7 billion, or  $1\frac{3}{4}$  per cent of GDP; and, as the House will recall, I gave an assurance at the time of the Autumn Statement, when I announced a £4 $\frac{3}{4}$  billion increase in planned public spending in 1987-88, that on no account would I exceed that figure.

D7. Indeed, I believe it is right to go below it. Since its inception in 1980, the MTFS has indicated a steadily declining path for the PSBR expressed as a percentage of GDP. We have now reached what I judge to be its appropriate destination: a PSBR of 1 per cent of GDP. I intend to stick to that figure. This will maintain a degree of fiscal prudence that, until this year, had been recorded on only two occasions since the War.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



D8. Accordingly, I have decided to provide for a PSBR in 1987-88 of £4 billion.

D9. Inevitably, this greatly diminishes the scope I have this year for reducing the burden of taxation, which of course remains a major objective of Government policy. But I am sure it is right to err on the side of prudence and caution, and to build a still firmer base for the future. That is the principle on which both I and my predecessor have consistently conducted economic policy these past eight years, and I see no reason to depart from it now.

D10. Meanwhile, I would make one further observation, of a different nature. Economic arguments are seldom concluded, one way or another. This is chiefly because it is unusual for economic policies to be held in place long enough to provide sufficient evidence. But the 1980s have been different; and, as a result, one critically important economic argument has now been concluded, finally and decisively.

D11. Throughout our period of office, our critics have consistently maintained not only that a fiscal stimulus would produce real economic growth, but that without an expansionary fiscal policy



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**

sustained growth was impossible. They were wrong, and have been proved wrong. The British economy is now embarking on its seventh successive year of steady growth, at an average rate of getting on for 3 per cent a year. And during that time the PSBR, even if privatisation proceeds are added back, has been deliberately and steadily reduced from a shade under 6 per cent of GDP to a little over 2 per cent. Indeed, had I or my predecessor at any time heeded the advice of our so-called expansionist critics, the British economy would never have been in the unprecedentedly favourable position it is in today.

**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**X. EXCHANGE CONTROL**

X1. Before I turn to my proposals for changes in taxation, I have one other important change of a specific nature to announce.

X2. In 1979, a few months after the present Government had first taken office, my predecessor announced the abolition of exchange controls, which had been in continuous operation ever since the outbreak of war in 1939. That bold action has, over the past 7½ years, proved wholly beneficial to the British economy; and I am glad to note that other European countries are now moving in the same direction.

X3. But although the operation of exchange control has ceased, the Exchange Control Act itself remains on the Statute book. So long as it does, there is likely to persist a nagging fear that, in certain circumstances, exchange control might be reimposed; and such uncertainty could be damaging.

X4. I have therefore concluded that the time has come to repeal the Act. The necessary legislation will be contained in this year's Finance Bill.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**

X5. I note that, in what was clearly intended to be a major speech in New York in September, the Deputy-Leader of the Labour Party declared that, and I quote:

"The Labour Party has no intention of reintroducing statutory exchange controls".

I am confident, therefore, that the proposal I have just made will be welcomed on all sides of the House.

**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**E. BUSINESS AND ENTERPRISE**

E1. I now turn to taxation. First, taxes on business.

E2. The fundamental reform of the Corporation Tax system which I introduced in 1984 came fully into effect last April. The new system has undoubtedly improved the quality of business investment decisions in Britain, and is also encouraging more overseas companies to set up here.

E3. During the transition to the new system, companies were given advance notice of the main rate of Corporation Tax for the year ahead. This helped them in their forward planning, and I intend as far as possible to continue the practice of setting the rate in advance. Accordingly, I can announce now that the main rate of Corporation Tax in 1987-88 will be unchanged at 35 per cent - lower than in any other major industrial nation, though the United States is now set to emulate us.

E4. The low rate of Corporation Tax enables me to introduce a further simplification into the system.



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



E5. At present, while companies' capital gains are liable to Corporation Tax, the amount of such gains is first adjusted by a certain fraction so that the effective rate of tax is the same as that on capital gains made by individuals. This dates back to the time when the two rates of tax were far apart.

E6. This is no longer the case: indeed, the Corporation Tax rate for small companies is now below the Capital Gains Tax rate.

E7. I therefore propose that, from today, companies' capital gains be charged at the appropriate Corporation Tax rate, without adjustment, save for the indexation which applies to all post-1982 gains.

E8. It has, however, been argued that it is wrong that, where companies distribute capital gains as dividends, the gains are taxed twice, once in the hands of the company and once in the hands of the shareholder. I believe there is some justice in this complaint. Accordingly, I propose to remedy it by allowing companies to set payments of Advance Corporation Tax against their liability to tax on capital gains.



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



E9. Taken together, these changes should yield £60 million in 1988-89.

E10. I also have some further simplification and rationalisation of the Corporation Tax system to announce.

E11. At present, some companies established before 1965 do not have to pay their Corporation Tax until up to 21 months after the end of the period for which it is due, whereas companies established since 1965 have to pay their tax after 9 months - and some building societies have to pay sooner still.

E12. This difference in treatment cannot be justified. Moreover, it is open to an abuse which could put the timing of a substantial proportion of the total Corporation Tax yield at risk.

E13. I therefore propose that all companies and building societies should be treated the same way, with all liable to pay Corporation Tax nine months after the end of the accounting period on which the tax is due. The change will be phased in, but I would expect it to yield around £100 million in 1988-89.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



E14. I also propose to legislate now to pave the way for a new method of collecting Corporation Tax, to be known as Pay and File. At present, many company accounts are not received in time to agree the tax liability before payment is due. So there is a laborious process of an estimated assessment from the Inland Revenue and an appeal from the company. Under Pay and File companies will estimate their tax liabilities themselves, and pay on the normal due date. Tax liabilities will be finalised once companies submit their returns and accounts. Where it turns out that the initial payment was too low, the company will pay interest to the Revenue; where the initial payment was too high, the Revenue will pay interest to the company.

E15. This new approach was set out in last December's consultative document on the recommendations in the Keith Committee Report, and was generally welcomed by the business community and their tax advisers.

E16. As this change is part of a wider programme of streamlining tax collection, including major developments in the Inland Revenue's computer systems, it will not come into force until the early 1990s. But by legislating now I am giving taxpayers



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



and their advisers a firm basis on which to prepare for the new scheme.

E17. While business and industry as a whole is doing well, the North Sea oil sector has inevitably been hard hit by last year's oil price collapse. My Rt Hon Friend the Secretary of State for Energy and I have followed closely the effects on North Sea producers and their suppliers. The industry itself is generally confident about the longer-term prospects; while as for the tax system, not only is it inherently price-sensitive, but the companies themselves have repeatedly stressed their desire for stability.

E18. However, in the light of the immediate problems, I introduced last autumn legislation to bring forward the repayment of over £300 million of Advance Petroleum Revenue Tax. This has already helped many of the smaller and medium-sized companies faced with cash flow difficulties.

E19. I now propose two further Petroleum Revenue Tax reliefs. First, as from today companies may elect to have up to 10 per cent of the costs of developing certain new fields set against their Petroleum Revenue Tax liabilities in existing fields, until such time as the income of those new fields exceeds



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



BUDGET

the costs incurred. Second, there will be a new relief against PRT for spending on research into UK oil extraction that is not related to any particular field.

E20. I hope that these carefully targeted changes will give a worthwhile measure of help to the North Sea oil sector.

E21. I have to set the 1988-89 car and <sup>fuel</sup> ~~car fuel~~ benefit scales for those with company cars. The car scale charges still fall well short of the true value of the benefit, and as last year I propose to increase them by 10 per cent. There will be no change in the ~~car~~ fuel scales which, as already announced, will also be used for VAT purposes from 6 April.

E22. Last year I put the Business Expansion Scheme onto a permanent footing. However, there is evidence that the present rules produce end-year bunching of BES investments, and hence may crowd out some projects and lead to bad decisions on others. I propose therefore to permit the investor to claim part of the relief against his previous year's income. This will make it easier for companies to raise BES finance throughout the year.



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



E23. Training and retraining are vital to a flexible and competitive economy. Some employers may be willing to help with the retraining of workers who wish to move on to a different job. At present if employers finance training unrelated to an employee's existing job, the employee will generally be liable to tax on the cost. I propose to exempt from tax the cost of training in this kind of case, to encourage more companies to help employees to acquire new skills for new jobs.

E24. The past few years have seen a remarkable and most welcome growth in the number of small businesses and the self-employed. The Government has done a great deal to lighten the burdens on this vitally important sector of the economy. But I am well aware that problems remain, not least in the field of VAT.

E25. Accordingly, I asked Customs and Excise to issue a consultative document last autumn canvassing a number of changes. In the light of the responses to that document, I have four proposals to make.

E26. Perhaps the biggest problem faced by the small businessman today is the trade customer who is late in paying his bills: so late, sometimes, that VAT



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



BUDGET

becomes due before the bill has been paid. I can do nothing about late payment; but I can, I hope, do something about the VAT problem.

E27. My first and most important proposal, therefore, is that, as from 1 October, businesses whose annual turnover is under £½ million, which means more than half of all traders registered for VAT, will be able to choose to account for VAT on the basis of cash paid and received. In other words, they will have no liability to pay VAT until they themselves have received the money from their customers. In addition to easing the cash flow problems caused by late payers, this system will of course provide automatic VAT relief for bad debts.

E28. I have to warn the House, however, that I cannot legally introduce this change without first obtaining a derogation from the European Community's Sixth VAT Directive. I am applying for the necessary derogation today. The House will note that the upper limit of £½ million is considerably greater than the £100,000 suggested in the consultative document.

E29. Second, I propose to give these businesses the option of accounting for VAT on an annual basis. Instead of making quarterly returns, they would make



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



regular payments on account, and then file a single return at the end of the year. This option, which offers considerable streamlining, will be available next year.

E30. Third, the period within which businesses must apply to be registered for VAT will be extended from ten to thirty days.

E31. Fourth, there will be changes to the rules for the special VAT schemes for retailers, and more small and medium-sized businesses will be able to make use of the simpler schemes.

E32. I believe that the changes I have outlined, and in particular the option to move to cash accounting, will be widely welcomed by the small business community. The cost will be £115 million in 1987-88 and £60 million in 1988-89.

E33. In addition, I propose to increase the VAT threshold to £21,300, to keep it at the maximum permitted under existing European Community law.

E34. In the light of the responses to the consultative document, I shall not be going ahead either with the withdrawal of the so-called standard method by which retailers calculate their gross



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



takings for VAT, or with the compulsory deregistration of traders below the VAT threshold.

E35. I have one further measure to help the small businessman, unrelated to VAT. I propose to increase the limit for Capital Gains Tax retirement relief by 25 per cent, from £100,000 to £125,000. As usual, the annual Capital Gains Tax exempt amount will be increased, in line with statutory indexation, to £6,600.

E36. An essential element in any ongoing programme of tax reduction and reform must always be the elimination of unintended or unjustified tax breaks, which cause rates of tax generally to be higher than they need to be. Accordingly, I have five proposals to make today to this end.

E37. The first concerns VAT, and has already been the subject of extensive consultation. The House will be aware that a business that provides a service that is exempt from VAT cannot in turn deduct input tax on its purchases. But where the activities of a business are in part liable to VAT and in part exempt, the existing rules are excessively generous as to the amount of input tax that can be deducted; and this generosity is being exploited on a growing scale. The rules must



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



therefore be changed, and the changes, which I announced to the House last December, will come into effect on 1 April. There will be special arrangements to deal with the problem of brewers' tied houses. I am also taking this opportunity to exclude a significant number of small businesses from the scope of this provision. The yield from this change, which in effect is a measure of the potential revenue loss, will be some £300 million in 1987-88 and £400 million in 1988-89.

E38. Second, I propose to change the law so that companies in multinational groups which enjoy dual residence will no longer be able to secure tax relief twice on one and the same interest payment. Genuine trading companies will not be affected. This change, which will take effect on 1 April, follows the similar action recently taken by the United States. The change will yield £125 million in 1988-89.

E39. Third, I propose to end the present excessively generous treatment of tax credit relief for foreign withholding tax paid on interest on bank loans. In future, banks will be able to offset this tax credit only against tax on the profit on the relevant loan, and not more widely. This will bring our rules broadly into line with those in most other



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



BUDGET

countries. The change will apply from 1 April this year for new loans and from 1 April next year for existing loans. It will yield some £20 million in 1988-89.

E40. Fourth, the tax treatment of Lloyd's syndicates as it applies to the Reinsurance to Close system is clearly unsatisfactory. I therefore propose to bring it into line with that of provisions for outstanding liabilities made by ordinary insurance companies and, indeed, of comparable provisions made by other financial traders. I have asked the Inland Revenue to consult urgently with Lloyd's about the details of the legislation. The new rules will first apply to premiums payable for the Lloyds account which closes on 31 December this year.

E41 Fifth, I also propose to implement the Keith Committee's recommendation that interest should be charged in the limited number of cases where an employer does not apply PAYE properly and a formal assessment has to be made to recover the tax. The change will take effect from April next year, and the yield in 1988-89 is estimated at £45 million.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



E42. I have one further proposal to make in the broad field of the taxation of business and enterprise.

E43. In my Budget last year I suggested the possibility of introducing a measure of tax relief for profit-related pay.

E44. I pointed then to two considerable advantages that might be expected to flow from arrangements which relate pay to profits. First, the workforce would have a more direct personal interest in the profits earned by the firm in which they work; and, second, there would be a greater degree of pay flexibility in the face of changing market conditions. Such flexibility is vital if, as a nation, we are to defeat the scourge of unemployment.

E45. Last July I presented a Green Paper on Profit-Related Pay in conjunction with my Rt Hon and Noble Friend the Secretary of State for Employment and my Rt Hon Friend the Secretary of State for Trade and Industry. I now propose to introduce a scheme of tax relief broadly along the lines floated in the Green Paper.



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



E46. My proposals depart from those in the Green Paper in one important respect. I am doubling the proportion of an employee's profit-related pay that is eligible for tax relief from a quarter to a half, up to a maximum of £3,000. So for someone on average earnings receiving 5 per cent of their pay in profit-related form, the tax relief will be equivalent to a penny off the basic rate of income tax. The cost will inevitably depend on take-up: it could be £50 million in 1988-89, building up to substantially more than that, as take-up grows, and the proportion of an employee's pay which is profit-related rises.

E47. Profit-related pay is no panacea. But then there are no panaceas. What it is is a tool to help British business gradually to overcome one of our biggest national handicaps: the nature and behaviour of our labour market. I am today challenging British management to take advantage of that tool and to make good use of it, for the good of their firm, their workforce and their country.



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**F. TAXES ON SAVING**

F1. I turn now to the taxation of savings.

F2. A central theme and purpose of the Government's policies is the creation of a genuine popular capitalism: what used to be called, when ambitions were more limited and language more inhibited, a property-owning democracy.

F3. That means wider home ownership, wider share ownership, and wider pension ownership. Over the past eight years, the Government has actively promoted the first two, and has now embarked on the third. Home ownership, above all through the council tenant's right to buy. And share ownership, through the rapid growth of employee share schemes; through the massively successful privatisation programme, where Britain has led the world; and most recently through the new Personal Equity Plans, which I announced in last year's Budget and which started up on 1 January this year. In the first month of the scheme, more than 2,000 people a day took out Personal Equity Plans, many of them first-time investors, as I had hoped.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



F4. We know that 63 per cent of households now own their own homes, compared with 55 per cent in 1979. There have been, however, no official figures for the more explosive growth of share ownership in Britain over the past eight years. The Treasury and the Stock Exchange therefore jointly commissioned a major independent survey of individual shareholding in Britain. The results are now available. They show that there are now some 8½ million individual shareholders in this country - amounting to one fifth of the total adult population, and roughly three times the number there were in 1979.

F5. And then there is wider pension ownership. Two years ago, the Government embarked on a major strategy to extend the coverage of private pension provision and to give individuals far more flexibility and choice in the way they provide for their retirement. We have already introduced a number of important new measures to that end, and the tax changes I am announcing today will complete the picture.

F6. The cornerstone of the Government's pensions strategy is the introduction of an entirely new means of provision for retirement, developed by my Rt Hon Friend the Secretary of State for Social



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



Services. This is the personal pension, which will be launched on 1 January next year.

F7. Personal pensions are an important new dimension of ownership. They will enable employees - if they so wish - to opt out of their employers' schemes and make their own arrangements, tailored to fit their own circumstances. And they will provide a new opportunity for the 10 million employees who at present do not belong to an occupational scheme to make provision of their own and, if they so wish, to contract out of SERPS.

F8. In my Budget last year I undertook to bring forward proposals to give personal pensions the same favourable tax treatment as is currently enjoyed by retirement annuities. These were duly contained in a consultative document published last November, and the necessary legislation will be contained in this year's Finance Bill.

F9. In addition, to encourage a wider spread of occupational schemes, employers will be able to set up simplified schemes with the minimum of red tape. This will be particularly welcome to many small employers who have been discouraged by the complexity and open-ended commitment of a full-blown final salary scheme. And there will be



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



much greater scope for transferring between different types of pension scheme. Again, the Finance Bill will contain the necessary tax provisions.

F10. Finally, I have decided to go beyond the proposals set out in the consultative document in one important respect. I propose to allow members of occupational pension schemes to make additional voluntary contributions, with full tax relief, to a separate plan of their own choice instead of, as now, being restricted to plans within their employer's schemes. They will be able to top their pensions right up to the present tax approval limits.

F11. The proposals I have outlined - along with the measures my Rt Hon Friend has already taken - will make it easier for people to take their pensions with them when they change jobs, which will be good both for labour mobility and for independence. They will widen the range of choices people can make about their pensions; and will mean that in future individuals will have much more control over the way in which their own pension contributions are invested.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



F12. Taken as a whole, the changes we have made in the last two years have brought about a radical transformation in the ways people can provide for their retirement. There are new options for employers, and much greater freedom for individuals to plan their own pensions. This will lead to a further major extension of ownership, as people start to take advantage of the new opportunities.

F13. But the generous tax treatment of pensions can be justified only if it is not abused. I propose, therefore, to introduce some limited changes to the present rules to restrict the excessive relief which can be obtained in some circumstances, particularly by a few very highly paid people. These will include a stricter definition of final salary and, for all arrangements entered into from today, an upper limit of £150,000 on the maximum permissible tax-free lump sum, coupled with more rigorous rules on how pension and lump-sum benefits can be calculated.

F14. The cost of the overall pensions package will inevitably depend on take up, but with that proviso is estimated at £65 million in 1988-89.

F15. In my 1984 Budget I reformed the limits that apply to tax exempt life assurance issued by



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



friendly societies. I did so because the movement's tax privileges were being increasingly exploited by certain new Friendly Societies which had been set up simply as tax-efficient investment vehicles.

F16. However, I am anxious that the traditional Friendly Societies, which have played a valuable part in mutual self-help for many generations, should be able to plan for the future with confidence. I have therefore decided to replace the existing limit based on the sum assured with a new limit based on annual premiums. I propose to set this at £100 a year, which will greatly increase the scope of the traditional societies to offer life policies to their members.

F17. The tax-exempt limits governing sickness and accident benefits which trade unions provide for their members have not been changed since 1982. With effect from today, I propose to increase them to £3,000 for lump sums and £625 for annuities.

F18. Finally, in this section, I turn to Inheritance Tax.

F19. In my Budget last year I abolished the pernicious Capital Transfer Tax on lifetime gifts between individuals, which was particularly



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



damaging to the ownership and health of family business. This year I propose to extend the same exemption from tax, on similar terms, to gifts involving settled property where there is an interest in possession. This will not, however, apply to discretionary trusts. These changes will be of particular benefit to family businesses and to heritage properties, both of which are often held in trust.

F20. I also propose to make two minor changes affecting business assets. First, in what is perhaps an unwanted tribute to the unlisted securities market, holdings in USM companies will henceforth be treated for Inheritance Tax purposes in precisely the same way as holdings in companies with a full Stock Exchange listing. Second, business relief for minority holdings in excess of 25 per cent in unquoted companies will be increased from 30 per cent to 50 per cent. The purpose of both these changes is to concentrate business relief more accurately on those assets which could provide funds to pay the tax only at the risk of damaging the business.

F21. Thanks to the efforts of this Government, the tax regime for the nation's heritage has been much improved. Today, I have two further changes to



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



propose. First, I am exempting from Inheritance Tax settled property that is put into a heritage maintenance fund within two years of the death of a life tenant. And second, I propose to improve the arrangements for acceptance of property in lieu of tax. In future, owners will have the choice of either the present system, or an arrangement under which no interest would be charged between the offer and acceptance, but the tax would be based on the market value at the date of the offer and not, as now, at the date of acceptance.

F22. The abolition of the tax on lifetime giving was of the first importance to family businesses. But I remain conscious that it did little to help the smallest taxable estates, where the family home is often the main asset.

F23. I therefore propose to make a substantial increase in the threshold for Inheritance Tax, from £71,000 to £90,000, coupled with a simplification of the rate structure from seven rates to four. As a result of this change, the number of estates liable to Inheritance Tax will be cut by roughly a third. The cost will be £75 million in 1987-88 and £170 million in 1988-89.



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



F24. Despite this substantial relief, however, and all the other much-needed reliefs that my predecessor and I have introduced since 1979, the House may be interested to learn that the expected yield of Inheritance Tax in 1987-88, at almost £1 billion, is nearly three times the yield of Capital Transfer Tax in 1978-79, an increase in real terms of almost 50 per cent.

F25. As for the other Capital Taxes, over the same period the yield of Capital Gains Tax has risen in real terms by over 80 per cent and of Stamp Duty by more than 140 per cent. These increased yields are not unconnected with the fact that, since we first took office, the severity of these taxes has been significantly eased.

B.L.O.

SECRET

BUDGET

SECRET



BUDGET SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**G. TAXES ON SPENDING**

G1. I now turn to the taxation of spending.

G2. I have already announced some important changes in value added tax to prevent avoidance and to help the small businessman. I have no other proposals for major changes in VAT this year.

G3. However, in the light of representations I have received, I have decided to extend slightly the VAT reliefs I introduced last year for certain aspects of charitable work.

G4. I propose to relieve charities from VAT on certain welfare vehicles used by hospices to transport the terminally ill; on installing or adapting lavatory or bathroom facilities in charity homes for the disabled; on drugs and chemicals used by a charity in medical research; and on specialised location and identification equipment employed by mountain rescue and first aid services.

G5. While on the subject of charitable giving, I should remind the House that this year's Finance Bill will increase the limit on donations to charity under the new payroll giving scheme, which starts next month, from £100 to £120 a year.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



G6. Next, the excise duties. I propose to maintain the revenue from the taxation of gambling, but to make some readjustment within the total. I therefore propose to increase the gaming machine licence duty by about a quarter, which will restore it in real terms to its 1982 level, when it was last increased; and to offset this by abolishing, from 29 March, the tax on on-course betting. I hope this measure will be of some assistance to the racing and bloodstock industry, as well as consoling those hon Members who have complained to me about the clash this year between Budget Day and the Champion Hurdle.

G7. In my Budget Statement last year, I gave advance notice of my intention to introduce a tax differential in favour of unleaded petrol so as to offset its higher production cost. I can now announce that the differential will be 5 pence a gallon. This means that the pump price of unleaded petrol should be no higher than that of 4-star leaded petrol. The change will take effect from 6 o'clock this evening.

G8. Following on from the action I took last year, I propose to increase the rates of Vehicle Excise Duty on farmers' lorries, to bring them into line with the use they make of the public roads. This change will take effect from midnight tonight. I



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**

also propose to increase the rates of duty on trade licences and to rationalise the taxation of recovery vehicles.

G9. I have no further changes to propose this year in the rates of excise duty.

BUDGET

SECRET

B.L.O.

SECRET

**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**H. INCOME TAX**

H1. Finally, I turn to income tax.

H2. There is now a worldwide consensus on the economic desirability of tax reform and tax reduction, and in particular the reduction of income tax. This was demonstrated most recently by the various national policy declarations that emerged from last month's meeting of Finance Ministers from the major industrial nations.

H3. Lower rates of tax sharpen up incentives and stimulate enterprise, which in turn is the only route to improved economic performance. It is only by improving our economic performance that we will be able to afford to spend more on public services; only by improving our economic performance that we will be able to create jobs on the scale that we all want to see.

H4. That is why, ever since we first took office in 1979, we have consistently sought to reduce the burden of income tax. We have cut the basic rate of tax from 33 per cent to 29 per cent and sharply reduced the punitive higher rates we inherited from the Party opposite. We have increased the main tax



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



allowances by 22 per cent more than inflation, taking almost 1½ million people out of income tax altogether.

H5. For 1987-88 I propose to raise all the main thresholds and allowances by the statutory indexation factor of 3.7 per cent, rounded up. Thus the single person's allowance will rise by £90 to £2,425 and the married man's allowance by £140 to £3,795. The single age allowance will rise by £110 to £2,960 and the married age allowance by £170 to £4,675. The age allowance income limit becomes £9,800. I propose to raise the first, 40 per cent, higher rate threshold by £700 to £17,900, in line with statutory indexation; but the threshold for the 45 per cent rate will go up by only £200 to £20,400. The other higher rate thresholds will remain unchanged.

H6. I have two other changes in allowances to announce. First, I propose to give an additional increase in the age allowance for those aged 80 or over. For them, the increase will be double the amount due under statutory indexation, so that, for the very elderly, the single age allowance will rise by £220 to £3,070 and the married age allowance by £340 to £4,845. Around 400,000 taxpayers will



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



benefit from this new measure, and up to 25,000 of them will be taken out of income tax altogether.

H7. Second, the blind person's allowance has remained unchanged since 1981, when it was increased by £180 to its present level of £360. For 1987-88 I propose to increase it by a further £180, to £540.

H8. Finally, I turn to the basic rate of income tax. This is the starting rate of income tax for everyone and the marginal rate for the overwhelming majority of taxpayers.

H9. In my Budget speech last year I reaffirmed the aim set out by my predecessor in 1979, to reduce the basic rate of income tax to no more than 25 per cent. That remains my firm objective.

H10. However, given my decision to use the greater part of the fiscal scope I now have to reduce the Public Sector Borrowing Requirement, that goal cannot be achieved in this Budget.

H11. I can, however, take a further step towards it, as I did last year. I am therefore reducing the basic rate of income tax by twopence, to 27 per cent. This reduction, which will benefit every



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



taxpayer in the land, will be worth more than £3 a week to a married man on average earnings.

H12. There will, of course, be a consequential reduction in the rate of Advance Corporation Tax, and - as last year - I also propose a corresponding cut in the small companies' rate of Corporation Tax from 29 per cent to 27 per cent. Taken together with the income tax change, this will mean a significant reduction in the tax burden on small businesses, which are so crucial for future growth and employment.

H13. The income tax changes I have announced today will take effect under PAYE on the first pay day after 17 May. They will cost a little over £2 billion in 1987-88 over and above the cost of statutory indexation.

H14. The overall cost of all the measures in this year's Budget, again on an indexed basis, is a little over £2½ billion. And I have been able to make this worthwhile reduction in tax while still achieving my objective of a PSBR of £4 billion.



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



FROM: A P HUDSON

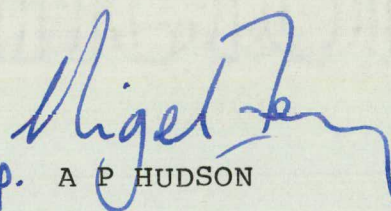
DATE: 12 March 1987

CHANCELLOR

cc Mr A C S Allan

**BUDGET STATEMENT**

I attach the present draft, incorporating the amendments you made yesterday evening.

  
pp. A P HUDSON



**A. INTRODUCTION**

A1. The setting for this year's Budget is more favourable than it has been for very many years. We are entering our seventh successive year of steady growth, at the top of the international league table. We are entering the fifth year in which this steady growth has been combined with low inflation. The public finances are sound and strong, and unemployment is falling.

A2. These are the fruits of the Government's determination, in bad times as well as good, to hold firmly to our policies of sound money and free markets. Once again, I reaffirm those policies.

A3. So the Budget I present today is a Budget built on success, and a Budget for success.

A4. I shall begin, as usual, by reviewing the economic background to the Budget. I shall then turn to monetary policy and to the fiscal prospect this year and next. Finally, I shall propose some changes in taxation designed to improve still further the prospects that lie before us. A number of press releases, filling out the details of my proposals, will be available from the Vote Office as soon as I have sat down.



**B. THE ECONOMIC BACKGROUND**

B1. I start with the economic background.

B2. Nineteen eighty-six was dominated by the sudden collapse of the oil price. Our own economy was affected not only directly, as a major oil producer and exporter, but also by the pause in world growth as the world economy adjusted to what has been described as the third oil shock. Despite this dislocation, however, the economy has developed in most respects as I foreshadowed a year ago.

B3. In 1986 as a whole output grew by a further  $2\frac{1}{2}$  per cent or so, which compares well with the experience of other industrialised countries. Indeed, we have now enjoyed the longest period of steady growth, at a rate approaching 3 per cent, that the UK economy has known since the War. It is also worth recalling that in the 1960s, and again in the 1970s, Britain's growth rate was the lowest of all the major European economies. By contrast, during the 1980s, our growth rate has been the highest of all the major European economies.

<sup>6</sup>B3A. And this greatly improved growth performance has coincided with falling inflation, which at



3½ per cent in 1986 recorded the lowest figure for almost 20 years. Over the lifetime of this Parliament, inflation has averaged less than 5 per cent.

<sup>5</sup>B4. During the first half of last year exports and hence output were affected by the pause in world growth to which I have already referred. But since the middle of the year exports have grown strongly. Indeed, over the last three months the volume of non-oil visible exports was almost 10 per cent higher than a year earlier - a better performance than that of any other major economy. This pattern was reflected in the rapid growth of manufacturing output in the second half of last year.

<sup>6</sup>B5. This resurgence of economic growth, coupled with the special measures we have taken, has brought about a welcome fall in the number of people out of work. Since August unemployment has fallen by more than 100,000; the largest six-monthly fall since 1973. Though the numbers out of work are still far too high, both youth unemployment and long-term unemployment are now lower than they were a year ago.

<sup>7</sup>B6. I announced a number of specific employment measures in my last Budget, and since then, my Rt Hon and Noble Friend the Secretary of State for



Employment has further extended the successful Restart programme for the long-term unemployed. Starting next month, all those who have been unemployed for more than six months will be offered Restart interviews twice a year, to give them individual advice and help. There will also be more places on the successful Enterprise Allowance Scheme, helping unemployed people to set up their own businesses. Again, the number of Jobclubs is to be quadrupled, with room for 150,000 people a year. And once fully under way, the new Job Training Scheme will give a quarter of a million others, most of them young people, work experience and vocational training. Together with the Youth Training Scheme and other programmes, what this means is that this Government has developed its employment and training measures on a scale which no other country can match. But the best hope of all for the unemployed lies in the continuing vigour of the economy.

<sup>8</sup>  
B7. Since the early months of last year, there has been a further surge in manufacturing productivity. This continues the remarkable improvement in productivity growth achieved by British industry throughout the 1980s. In the 1960s, and again in the 1970s, growth in manufacturing productivity in the UK was the lowest of all the seven major industrial countries in the world. During the



1980s, our annual rate of growth of output per head in manufacturing has been the highest of all the seven major industrial countries.

<sup>9</sup>  
B8. The recorded current account of the balance of payments went into deficit in 1986 by around £1 billion. This followed a cumulative current account surplus of some £20 billion between 1979 and 1985. Some deterioration in our current account was inevitable in the face of a £5 billion loss of earnings on oil trade virtually overnight. But the significance of this should not be exaggerated. The exchange rate adjustment that followed the fall in the oil price is already contributing to an improved non-oil trade performance. And earnings from the massive stock of net overseas assets we have acquired since 1979, which at well over £100 billion is second only to that of Japan, will provide a continuing support to the current account in the years ahead.

<sup>10</sup>  
B9. Looking ahead, I expect 1987 to be another year of steady, balanced growth with low inflation. Total output is forecast to rise by 3 per cent, with exports and investment up rather more than that. Manufacturing industry, in particular, should do well. And with the non-oil economy set to grow at  $3\frac{1}{2}$  per cent, there is every prospect of unemployment continuing to fall throughout 1987. In last year's



Budget Speech I said that the outlook for jobs depended on a sustained improvement in the performance of business and industry. That sustained improvement in economic performance has occurred and is continuing.

<sup>1</sup>Bl0. Despite the strong growth in exports, it will inevitably take time for the full effect of the exchange rate adjustment to work through. The current account is thus likely to remain in deficit this year, by some £2½ billion, around half of one per cent of GDP.

<sup>2</sup>Bl1. As I foreshadowed in the Autumn Statement, inflation may continue to edge up for a time, perhaps to a little over 4½ per cent by the Summer, before falling back to 4 per cent by the end of the year. While short-term fluctuations are inescapable, it remains the Government's prime objective to keep inflation on an unambiguously downward underlying trend.

<sup>3</sup>Bl2. Given the continuation of present policies in this country, the biggest risk to the excellent prospect I have outlined is that of a downturn in the world economy as a whole. There are still serious imbalances afflicting the three major economies - the United States on the one hand and Japan and Germany on the other - which, if not



handled properly, could lead to a simultaneous downturn in all three. And this in turn could be exacerbated by renewed turmoil in the foreign exchange markets, whose tendency to overshoot is as notorious as it is damaging.

<sup>4</sup>Bl3. It was to address these dangers that the Finance Ministers and Central Bank Governors of six major nations met in Paris last month, and agreed among other things to co-operate closely in fostering a period of exchange rate stability. In my Budget Speech last year, I said:

"Provided we are not over-ambitious, I believe that the Plaza accord is something we can usefully build on."

That is what we have now done, with Plaza II. But it would be idle to deny that the wider risks still remain.

<sup>5</sup>Bl4. Short of a world downturn, which can and must be avoided, British industry now has an outstanding opportunity, with growing markets at home and overseas, low inflation, rapidly growing productivity and greatly improved profitability. Provided it can control its costs and maintain its present competitive advantage, and assuming the continuation of present policies, we can look forward to many more years of strong growth combined with low inflation.



### C. MONETARY POLICY

C1. For its part, the Government will keep in place a sound and prudent financial framework. That means, as it has done since 1980, the medium-term financial strategy.

C2. The central objective of the MTFS is steadily to reduce the growth of money GDP over the medium term, so as to squeeze inflation out of the system and ultimately to achieve price stability.

C3. This requires monetary discipline buttressed by low public sector borrowing. The essential instrument of monetary policy must remain short term interest rates. These will continue to be set in the light of monetary conditions as indicated principally by the growth of narrow and broad money and the behaviour of the exchange rate.

C4. For narrow money, MO, the target range for next year will be 2 to 6 per cent, as foreshadowed in last year's MTFS. For broad money, however, as the Governor of the Bank of England cogently argued in his Loughborough lecture last October, in current circumstances it is probably wiser to eschew an explicit target altogether. But broad money will continue to be taken into account in assessing



monetary conditions, as of course will the exchange rate.

C5. In my Lombard Association speech last April, I set out at considerable length precisely how in practice monetary policy is operated. While I note that in some quarters this was felt to be unclear or in some other way unsatisfactory, I am struck by the fact that Mr Paul Volcker, Chairman of the United States Federal Reserve Board, in his written testimony to the Senate last month, explained how the Fed operates monetary policy in remarkably similar terms.



**D. PUBLIC SECTOR BORROWING**

D1. I mentioned a moment ago the need to keep public sector borrowing low.

D2. The final outturn for the public sector borrowing requirement last year, 1985-86, was just under £6 billion, equivalent to  $1\frac{1}{2}$  per cent of GDP, the lowest level since 1970-71. In my Budget last year, faced with a massive loss of what now looks like £7 billion of North Sea oil revenue, I nonetheless decided to hold the PSBR for this year, 1986-87, to £7 billion, or  $1\frac{3}{4}$  per cent of GDP.

D3. In the event, this year's PSBR looks like turning out at only £4 billion, or 1 per cent of GDP: the second successive year of significant undershoot.

D4. This successful outcome is chiefly attributable to the remarkable buoyancy of non-oil tax revenues. And this in turn is due not to some short-term surge in consumer spending, but in particular to an increase over last year of no less than a third in the yield of Corporation Tax from an increasingly profitable business and industry.



D5. Looking ahead, there is still a degree of uncertainty surrounding oil prices, and I have therefore stuck to the assumption I made last year that the North Sea price will average \$15 a barrel. But it is clear that the increased flow of non-oil tax revenues, coupled with the prospective further growth of the economy in excess of the growth of public expenditure, puts the public finances in an exceptionally strong position.

D6. I intend to keep it that way. Last year's MTF5 indicated a PSBR for 1987-88 of £7 billion, or  $1\frac{3}{4}$  per cent of GDP; and, as the House will recall, I gave an assurance at the time of the Autumn Statement, when I announced a £4 $\frac{3}{4}$  billion increase in planned public spending in 1987-88, that on no account would I exceed that figure.

D7. Indeed, I believe it is right to go below it. Since its inception in 1980, the MTF5 has indicated a steadily declining path for the PSBR expressed as a percentage of GDP. We have now reached what I judge to be its appropriate destination: a PSBR of 1 per cent of GDP. I intend to stick to that figure. This will maintain a degree of fiscal prudence that, until this year, had been recorded on only two occasions since the War.



D8. Accordingly, I have decided to provide for a PSBR in 1987-88 of £4 billion.

D9. Inevitably, this greatly diminishes the scope I have this year for reducing the burden of taxation, which of course remains a major objective of Government policy. But I am sure it is right to err on the side of prudence and caution, and to build a still firmer base for the future. That is the principle on which both I and my predecessor have consistently conducted economic policy these past eight years, and I see no reason to depart from it now.

D10. Meanwhile, I would make one further observation, of a different nature. Economic arguments are seldom concluded, one way or another. This is chiefly because it is unusual for economic policies to be held in place long enough to provide sufficient evidence. But the 1980s have been different; and, as a result, one critically important economic argument has now been concluded, finally and decisively.

D11. Throughout our period of office, our critics have consistently maintained not only that a fiscal stimulus would produce real economic growth, but that without an expansionary fiscal policy



sustained growth was impossible. They were wrong, and have been proved wrong. The British economy is now embarking on its seventh successive year of steady growth, at an average rate of getting on for 3 per cent a year. And during that time the PSBR, even if privatisation proceeds are added back, has been deliberately and steadily reduced from a shade under 6 per cent of GDP to a little over 2 per cent. Indeed, had I or my predecessor at any time heeded the advice of our so-called expansionist critics, the British economy would never have been in the unprecedentedly favourable position it is in today.



**X. EXCHANGE CONTROL**

X1. Before I turn to my proposals for changes in taxation, I have one other important change of a specific nature to announce.

X2. In 1979, a few months after the present Government had first taken office, my predecessor announced the abolition of exchange controls, which had been in continuous operation ever since the outbreak of war in 1939. That bold action has, over the past 7½ years, proved wholly beneficial to the British economy; and I am glad to note that other European countries are now moving in the same direction.

X3. But although the operation of exchange control has ceased, the Exchange Control Act itself remains on the Statute book. So long as it does, there is likely to persist a nagging fear that, in certain circumstances, exchange control might be reimposed; and such uncertainty could be damaging.

X4. I have therefore concluded that the time has come to repeal the Act. The necessary legislation will be contained in this year's Finance Bill.



X5. I note that, in what was clearly intended to be a major speech in New York in September, the Deputy-Leader of the Labour Party declared that, and I quote:

"The Labour Party has no intention of reintroducing statutory exchange controls".

I am confident, therefore, that the proposal I have just made will be welcomed on all sides of the House.



Draft of 12 March

**E. BUSINESS AND ENTERPRISE**

E1. I now turn to taxation. First, taxes on business.

E2. The fundamental reform of the Corporation Tax system which I introduced in 1984 came fully into effect last April. The new system has undoubtedly improved the quality of business investment decisions in Britain, and is also encouraging more overseas companies to set up here.

E3. During the transition to the new system, companies were given advance notice of the main rate of Corporation Tax for the year ahead. This helped them in their forward planning, and I intend as far as possible to continue the practice of setting the rate in advance. Accordingly, I can announce now that the main rate of Corporation Tax in 1987-88 will be unchanged at 35 per cent - lower than in any other major industrial nation, though the United States is now set to emulate us.

E4. The low rate of Corporation Tax enables me to introduced a further simplification into the system.



E5. At present, while companies' capital gains are liable to Corporation Tax, the amount of such gains is first adjusted by a certain fraction so that the effective rate of tax is the same as that on capital gains made by individuals. This dates back to the time when the two rates of tax were far apart.

E6. This is no longer the case: indeed, the Corporation Tax rate for small companies is now below the Capital Gains Tax rate.

E7. I therefore propose that, from today, companies' capital gains be charged at the appropriate Corporation Tax rate, without adjustment, save for the indexation which applies to all post-1982 gains.

E8. It has, however, been argued that it is wrong that, where companies distribute capital gains as dividends, the gains are taxed twice, once in the hands of the company and once in the hands of the shareholder. I believe there is some justice in this complaint. Accordingly, I propose to remedy it by allowing companies to set payments of Advance Corporation Tax against their liability to tax on capital gains.



E9. Taken together, these changes should yield £60 million in 1988-89.

E10. I also have some further simplification and rationalisation of the Corporation Tax system to announce.

E11. At present, some companies established before 1965 do not have to pay their Corporation Tax until up to 21 months after the end of the period for which it is due, whereas companies established since 1965 have to pay their tax after 9 months - and some building societies have to pay sooner still.

E12. This difference in treatment cannot be justified. Moreover, it is open to an abuse which could put the timing of a substantial proportion of the total Corporation Tax yield at risk.

E13. I therefore propose that all companies and building societies should be treated the same way, with all liable to pay Corporation Tax nine months after the end of the accounting period on which the tax is due. The change will be phased in, but I would expect it to yield around £100 million in 1988-89.



E14. I also propose to legislate now to pave the way for a new method of collecting Corporation Tax, to be known as Pay and File. At present, many company accounts are not received in time to agree the tax liability before payment is due. So there is a laborious process of an estimated assessment from the Inland Revenue and an appeal from the company. Under Pay and File companies will estimate their tax liabilities themselves, and pay on the normal due date. Tax liabilities will be finalised once companies submit their returns and accounts. Where it turns out that the initial payment was too low, the company will pay interest to the Revenue; where the initial payment was too high, the Revenue will pay interest to the company.

E15. This new approach was set out in last December's consultative document on the recommendations in the Keith Committee Report, and was generally welcomed by the business community and their tax advisers.

E16. As this change is part of a wider programme of streamlining tax collection, including major developments in the Inland Revenue's computer systems, it will not come into force until the early 1990s. But by legislating now I am giving taxpayers



and their advisers a firm basis on which to prepare for the new scheme.

E17. While business and industry as a whole is doing well, the North Sea oil sector has inevitably been hard hit by last year's oil price collapse. My Rt Hon Friend the Secretary of State for Energy and I have followed closely the effects on North Sea producers and their suppliers. The industry itself is generally confident about the longer-term prospects; while as for the tax system, not only is it inherently price-sensitive, but the companies themselves have repeatedly stressed their desire for stability.

E18. However, in the light of the immediate problems, I introduced last autumn legislation to bring forward the repayment of over £300 million of Advance Petroleum Revenue Tax. This has already helped many of the smaller and medium-sized companies faced with cash flow difficulties.

E19. I now propose two further Petroleum Revenue Tax reliefs. First, as from today companies may elect to have up to 10 per cent of the costs of developing certain new fields set against their Petroleum Revenue Tax liabilities in existing fields, until such time as the income of those new fields exceeds



the costs incurred. Second, there will be a new relief against PRT for spending on research into UK oil extraction that is not related to any particular field.

E20. I hope that these carefully targeted changes will give a worthwhile measure of help to the North Sea oil sector.

E21. I have to set the 1988-89 car and car fuel benefit scales for those with company cars. The car scale charges still fall well short of the true value of the benefit, and as last year I propose to increase them by 10 per cent. There will be no change in the car fuel scales which, as already announced, will also be used for VAT purposes from 6 April.

E22. Last year I put the Business Expansion Scheme onto a permanent footing. However, there is evidence that the present rules produce end-year bunching of BES investments, and hence may crowd out some projects and lead to bad decisions on others. I propose therefore to permit the investor to claim part of the relief against his previous year's income. This will make it easier for companies to raise BES finance throughout the year.



E23. Training and retraining are vital to a flexible and competitive economy. Some employers may be willing to help with the retraining of workers who wish to move on to a different job. At present if employers finance training unrelated to an employee's existing job, the employee will generally be liable to tax on the cost. I propose to exempt from tax the cost of training in this kind of case, to encourage more companies to help employees to acquire new skills for new jobs.

E24. The past few years have seen a remarkable and most welcome growth in the number of small businesses and the self-employed. The Government has done a great deal to lighten the burdens on this vitally important sector of the economy. But I am well aware that problems remain, not least in the field of VAT.

E25. Accordingly, I asked Customs and Excise to issue a consultative document last autumn canvassing a number of changes. In the light of the responses to that document, I have four proposals to make.

E26. Perhaps the biggest problem faced by the small businessman today is the trade customer who is late in paying his bills: so late, sometimes, that VAT



becomes due before the bill has been paid. I can do nothing about late payment; but I can, I hope, do something about the VAT problem.

E27. My first and most important proposal, therefore, is that, as from 1 October, businesses whose annual turnover is under £¼ million, which means more than half of all traders registered for VAT, will be able to choose to account for VAT on the basis of cash paid and received. In other words, they will have no liability to pay VAT until they themselves have received the money from their customers. In addition to easing the cash flow problems caused by late payers, this system will of course provide automatic VAT relief for bad debts.

E28. I have to warn the House, however, that I cannot legally introduce this change without first obtaining a derogation from the European Community's Sixth VAT Directive. I am applying for the necessary derogation today. The House will note that the upper limit of £¼ million is considerably greater than the £100,000 suggested in the consultative document.

E29. Second, I propose to give these businesses the option of accounting for VAT on an annual basis. Instead of making quarterly returns, they would make



regular payments on account, and then file a single return at the end of the year. This option, which offers considerable streamlining, will be available next year.

E30. Third, the period within which businesses must apply to be registered for VAT will be extended from ten to thirty days.

E31. Fourth, there will be changes to the rules for the special VAT schemes for retailers, and more small and medium-sized businesses will be able to make use of the simpler schemes.

E32. I believe that the changes I have outlined, and in particular the option to move to cash accounting, will be widely welcomed by the small business community. The cost will be £115 million in 1987-88 and £60 million in 1988-89.

E33. In addition, I propose to increase the VAT threshold to £21,300, to keep it at the maximum permitted under existing European Community law.

E34. In the light of the responses to the consultative document, I shall not be going ahead either with the withdrawal of the so-called standard method by which retailers calculate their gross



takings for VAT, or with the compulsory deregistration of traders below the VAT threshold.

E35. I have one further measure to help the small businessman, unrelated to VAT. I propose to increase the limit for Capital Gains Tax retirement relief by 25 per cent, from £100,000 to £125,000. As usual, the annual Capital Gains Tax exempt amount will be increased, in line with statutory indexation, to £6,600.

E36. An essential element in any ongoing programme of tax reduction and reform must always be the elimination of unintended or unjustified tax breaks, which cause rates of tax generally to be higher than they need to be. Accordingly, I have five proposals to make today to this end.

E37. The first concerns VAT, and has already been the subject of extensive consultation. The House will be aware that a business that provides a service that is exempt from VAT cannot in turn deduct input tax on its purchases. But where the activities of a business are in part liable to VAT and in part exempt, the existing rules are excessively generous as to the amount of input tax that can be deducted; and this generosity is being exploited on a growing scale. The rules must



therefore be changed, and the changes, which I announced to the House last December, will come into effect on 1 April. There will be special arrangements to deal with the problem of brewers' tied houses. I am also taking this opportunity to exclude a significant number of small businesses from the scope of this provision. The yield from this change, which in effect is a measure of the potential revenue loss, will be some £300 million in 1987-88 and £400 million in 1988-89.

E38. Second, I propose to change the law so that companies in multinational groups which enjoy dual residence will no longer be able to secure tax relief twice on one and the same interest payment. Genuine trading companies will not be affected. This change, which will take effect on 1 April, follows the similar action recently taken by the United States. The change will yield £125 million in 1988-89.

E39. Third, I propose to end the present excessively generous treatment of tax credit relief for foreign withholding tax paid on interest on bank loans. In future, banks will be able to offset this tax credit only against tax on the profit on the relevant loan, and not more widely. This will bring our rules broadly into line with those in most other



countries. The change will apply from 1 April this year for new loans and from 1 April next year for existing loans. It will yield some £20 million in 1988-89.

E40. Fourth, the tax treatment of Lloyd's syndicates as it applies to the Reinsurance to Close system is clearly unsatisfactory. I therefore propose to bring it into line with that of provisions for outstanding liabilities made by ordinary insurance companies and, indeed, of comparable provisions made by other financial traders. I have asked the Inland Revenue to consult urgently with Lloyd's about the details of the legislation. The new rules will first apply to premiums payable for the Lloyds account which closes on 31 December this year.

E41 Fifth, I also propose to implement the Keith Committee's recommendation that interest should be charged in the limited number of cases where an employer does not apply PAYE properly and a formal assessment has to be made to recover the tax. The change will take effect from April next year, and the yield in 1988-89 is estimated at £45 million.



E42. I have one further proposal to make in the broad field of the taxation of business and enterprise.

E43. In my Budget last year I suggested the possibility of introducing a measure of tax relief for profit-related pay.

E44. I pointed then to two considerable advantages that might be expected to flow from arrangements which relate pay to profits. First, the workforce would have a more direct personal interest in the profits earned by the firm in which they work; and, second, there would be a greater degree of pay flexibility in the face of changing market conditions. Such flexibility is vital if, as a nation, we are to defeat the scourge of unemployment.

E45. Last July I presented a Green Paper on Profit-Related Pay in conjunction with my Rt Hon and Noble Friend the Secretary of State for Employment and my Rt Hon Friend the Secretary of State for Trade and Industry. I now propose to introduce a scheme of tax relief broadly along the lines floated in the Green Paper.



E46. My proposals depart from those in the Green Paper in one important respect. I am doubling the proportion of an employee's profit-related pay that is eligible for tax relief from a quarter to a half, up to a maximum of £3,000. So for someone on average earnings receiving 5 per cent of their pay in profit-related form, the tax relief will be equivalent to a penny off the basic rate of income tax. The cost will inevitably depend on take-up: it could be £50 million in 1988-89, building up to substantially more than that, as take-up grows, and the proportion of an employee's pay which is profit-related rises.

E47. Profit-related pay is no panacea. But then there are no panaceas. What it is is a tool to help British business gradually to overcome one of our biggest national handicaps: the nature and behaviour of our labour market. I am today challenging British management to take advantage of that tool and to make good use of it, for the good of their firm, their workforce and their country.



## F. TAXES ON SAVING

F1. I turn now to the taxation of savings.

F2. A central theme and purpose of the Government's policies is the creation of a genuine popular capitalism: what used to be called, when ambitions were more limited and language more inhibited, a property-owning democracy.

F3. That means wider home ownership, wider share ownership, and wider pension ownership. Over the past eight years, the Government has actively promoted the first two, and has now embarked on the third. Home ownership, above all through the council tenant's right to buy. And share ownership, through the rapid growth of employee share schemes; through the massively successful privatisation programme, where Britain has led the world; and most recently through the new Personal Equity Plans, which I announced in last year's Budget and which started up on 1 January this year. In the first month of the scheme, more than 2,000 people a day took out Personal Equity Plans, many of them first-time investors, as I had hoped.



F4. We know that 63 per cent of households now own their own homes, compared with 55 per cent in 1979. There have been, however, no official figures for the more explosive growth of share ownership in Britain over the past eight years. The Treasury and the Stock Exchange therefore jointly commissioned a major independent survey of individual shareholding in Britain. The results are now available. They show that there are now some 8½ million individual shareholders in this country - amounting to one fifth of the total adult population, and roughly three times the number there were in 1979.

F5. And then there is wider pension ownership. Two years ago, the Government embarked on a major strategy to extend the coverage of private pension provision and to give individuals far more flexibility and choice in the way they provide for their retirement. We have already introduced a number of important new measures to that end, and the tax changes I am announcing today will complete the picture.

F6. The cornerstone of the Government's pensions strategy is the introduction of an entirely new means of provision for retirement, developed by my Rt Hon Friend the Secretary of State for Social



Services. This is the personal pension, which will be launched on 1 January next year.

F7. Personal pensions are an important new dimension of ownership. They will enable employees - if they so wish - to opt out of their employers' schemes and make their own arrangements, tailored to fit their own circumstances. And they will provide a new opportunity for the 10 million employees who at present do not belong to an occupational scheme to make provision of their own and, if they so wish, to contract out of SERPS.

F8. In my Budget last year I undertook to bring forward proposals to give personal pensions the same favourable tax treatment as is currently enjoyed by retirement annuities. These were duly contained in a consultative document published last November, and the necessary legislation will be contained in this year's Finance Bill.

F9. In addition, to encourage a wider spread of occupational schemes, employers will be able to set up simplified schemes with the minimum of red tape. This will be particularly welcome to many small employers who have been discouraged by the complexity and open-ended commitment of a full-blown final salary scheme. And there will be



much greater scope for transferring between different types of pension scheme. Again, the Finance Bill will contain the necessary tax provisions.

F10. Finally, I have decided to go beyond the proposals set out in the consultative document in one important respect. I propose to allow members of occupational pension schemes to make additional voluntary contributions, with full tax relief, to a separate plan of their own choice instead of, as now, being restricted to plans within their employer's schemes. They will be able to top their pensions right up to the present tax approval limits.

F11. The proposals I have outlined - along with the measures my Rt Hon Friend has already taken - will make it easier for people to take their pensions with them when they change jobs, which will be good both for labour mobility and for independence. They will widen the range of choices people can make about their pensions; and will mean that in future individuals will have much more control over the way in which their own pension contributions are invested.



F12. Taken as a whole, the changes we have made in the last two years have brought about a radical transformation in the ways people can provide for their retirement. There are new options for employers, and much greater freedom for individuals to plan their own pensions. This will lead to a further major extension of ownership, as people start to take advantage of the new opportunities.

F13. But the generous tax treatment of pensions can be justified only if it is not abused. I propose, therefore, to introduce some limited changes to the present rules to restrict the excessive relief which can be obtained in some circumstances, particularly by a few very highly paid people. These will include a stricter definition of final salary and, for all arrangements entered into from today, an upper limit of £150,000 on the maximum permissible tax-free lump sum, coupled with more rigorous rules on how pension and lump-sum benefits can be calculated.

F14. The cost of the overall pensions package will inevitably depend on take up, but with that proviso is estimated at £65 million in 1988-89.

F15. In my 1984 Budget I reformed the limits that apply to tax exempt life assurance issued by



friendly societies. I did so because the movement's tax privileges were being increasingly exploited by certain new Friendly Societies which had been set up simply as tax-efficient investment vehicles.

F16. However, I am anxious that the traditional Friendly Societies, which have played a valuable part in mutual self-help for many generations, should be able to plan for the future with confidence. I have therefore decided to replace the existing limit based on the sum assured with a new limit based on annual premiums. I propose to set this at £100 a year, which will greatly increase the scope of the traditional societies to offer life policies to their members.

F17. The tax-exempt limits governing sickness and accident benefits which trade unions provide for their members have not been changed since 1982. With effect from today, I propose to increase them to £3,000 for lump sums and £625 for annuities.

F18. Finally, in this section, I turn to Inheritance Tax.

F19. In my Budget last year I abolished the pernicious Capital Transfer Tax on lifetime gifts between individuals, which was particularly



damaging to the ownership and health of family business. This year I propose to extend the same exemption from tax, on similar terms, to gifts involving settled property where there is an interest in possession. This will not, however, apply to discretionary trusts. These changes will be of particular benefit to family businesses and to heritage properties, both of which are often held in trust.

F20. I also propose to make two minor changes affecting business assets. First, in what is perhaps an unwanted tribute to the unlisted securities market, holdings in USM companies will henceforth be treated for Inheritance Tax purposes in precisely the same way as holdings in companies with a full Stock Exchange listing. Second, business relief for minority holdings in excess of 25 per cent in unquoted companies will be increased from 30 per cent to 50 per cent. The purpose of both these changes is to concentrate business relief more accurately on those assets which could provide funds to pay the tax only at the risk of damaging the business.

F21. Thanks to the efforts of this Government, the tax regime for the nation's heritage has been much improved. Today, I have two further changes to



propose. First, I am exempting from Inheritance Tax settled property that is put into a heritage maintenance fund within two years of the death of a life tenant. And second, I propose to improve the arrangements for acceptance of property in lieu of tax. In future, owners will have the choice of either the present system, or an arrangement under which no interest would be charged between the offer and acceptance, but the tax would be based on the market value at the date of the offer and not, as now, at the date of acceptance.

F22. The abolition of the tax on lifetime giving was of the first importance to family businesses. But I remain conscious that it did little to help the smallest taxable estates, where the family home is often the main asset.

F23. I therefore propose to make a substantial increase in the threshold for Inheritance Tax, from £71,000 to £90,000, coupled with a simplification of the rate structure from seven rates to four. As a result of this change, the number of estates liable to Inheritance Tax will be cut by roughly a third. The cost will be £75 million in 1987-88 and £170 million in 1988-89.



F24. Despite this substantial relief, however, and all the other much-needed reliefs that my predecessor and I have introduced since 1979, the House may be interested to learn that the expected yield of Inheritance Tax in 1987-88, at almost £1 billion, is nearly three times the yield of Capital Transfer Tax in 1978-79, an increase in real terms of almost 50 per cent.

F25. As for the other Capital Taxes, over the same period the yield of Capital Gains Tax has risen in real terms by over 80 per cent and of Stamp Duty by more than 140 per cent. These increased yields are not unconnected with the fact that, since we first took office, the severity of these taxes has been significantly eased.



**G. TAXES ON SPENDING**

G1. I now turn to the taxation of spending.

G2. I have already announced some important changes in value added tax to prevent avoidance and to help the small businessman. I have no other proposals for major changes in VAT this year.

G3. However, in the light of representations I have received, I have decided to extend slightly the VAT reliefs I introduced last year for certain aspects of charitable work.

G4. I propose to relieve charities from VAT on certain welfare vehicles used by hospices to transport the terminally ill; on installing or adapting lavatory or bathroom facilities in charity homes for the disabled; on drugs and chemicals used by a charity in medical research; and on specialised location and identification equipment employed by mountain rescue and first aid services.

G5. While on the subject of charitable giving, I should remind the House that this year's Finance Bill will increase the limit on donations to charity under the new payroll giving scheme, which starts next month, from £100 to £120 a year.



G6. Next, the excise duties. I propose to maintain the revenue from the taxation of gambling, but to make some readjustment within the total. I therefore propose to increase the gaming machine licence duty by about a quarter, which will restore it in real terms to its 1982 level, when it was last increased; and to offset this by abolishing, from 29 March, the tax on on-course betting. I hope this measure will be of some assistance to the racing and bloodstock industry, as well as consoling those hon Members who have complained to me about the clash this year between Budget Day and the Champion Hurdle.

G7. In my Budget Statement last year, I gave advance notice of my intention to introduce a tax differential in favour of unleaded petrol so as to offset its higher production cost. I can now announce that the differential will be 5 pence a gallon. This means that the pump price of unleaded petrol should be no higher than that of 4-star leaded petrol. The change will take effect from 6 o'clock this evening.

G8. Following on from the action I took last year, I propose to increase the rates of Vehicle Excise Duty on farmers' lorries, to bring them into line with the use they make of the public roads. This change will take effect from midnight tonight. I



also propose to increase the rates of duty on trade licences and to rationalise the taxation of recovery vehicles.

G9. I have no further changes to propose this year in the rates of excise duty.



Draft of 12 March

## H. INCOME TAX

H1. Finally, I turn to income tax.

H2. There is now a worldwide consensus on the economic desirability of tax reform and tax reduction, and in particular the reduction of income tax. This was demonstrated most recently by the various national policy declarations that emerged from last month's meeting of Finance Ministers from the major industrial nations.

H3. Lower rates of tax sharpen up incentives and stimulate enterprise, which in turn is the only route to improved economic performance. It is only by improving our economic performance that we will be able to afford to spend more on public services; only by improving our economic performance that we will be able to create jobs on the scale that we all want to see.

H4. That is why, ever since we first took office in 1979, we have consistently sought to reduce the burden of income tax. We have cut the basic rate of tax from 33 per cent to 29 per cent and sharply reduced the punitive higher rates we inherited from the Party opposite. We have increased the main tax



allowances by 22 per cent more than inflation, taking almost 1½ million people out of income tax altogether.

H5. For 1987-88 I propose to raise all the main thresholds and allowances by the statutory indexation factor of 3.7 per cent, rounded up. Thus the single person's allowance will rise by £90 to £2,425 and the married man's allowance by £140 to £3,795. The single age allowance will rise by £110 to £2,960 and the married age allowance by £170 to £4,675. The age allowance income limit becomes £9,800. I propose to raise the first, 40 per cent, higher rate threshold by £700 to £17,900, in line with statutory indexation; but the threshold for the 45 per cent rate will go up by only £200 to £20,400. The other higher rate thresholds will remain unchanged.

H6. I have two other changes in allowances to announce. First, I propose to give an additional increase in the age allowance for those aged 80 or over. For them, the increase will be double the amount due under statutory indexation, so that, for the very elderly, the single age allowance will rise by £220 to £3,070 and the married age allowance by £340 to £4,845. Around 400,000 taxpayers will



benefit from this new measure, and up to 25,000 of them will be taken out of income tax altogether.

H7. Second, the blind person's allowance has remained unchanged since 1981, when it was increased by £180 to its present level of £360. For 1987-88 I propose to increase it by a further £180, to £540.

H8. Finally, I turn to the basic rate of income tax. This is the starting rate of income tax for everyone and the marginal rate for the overwhelming majority of taxpayers.

H9. In my Budget speech last year I reaffirmed the aim set out by my predecessor in 1979, to reduce the basic rate of income tax to no more than 25 per cent. That remains my firm objective.

H10. However, given my decision to use the greater part of the fiscal scope I now have to reduce the Public Sector Borrowing Requirement, that goal cannot be achieved in this Budget.

H11. I can, however, take a further step towards it, as I did last year. I am therefore reducing the basic rate of income tax by twopence, to 27 per cent. This reduction, which will benefit every



taxpayer in the land, will be worth more than £3 a week to a married man on average earnings.

H12. There will, of course, be a consequential reduction in the rate of Advance Corporation Tax, and - as last year - I also propose a corresponding cut in the small companies' rate of Corporation Tax from 29 per cent to 27 per cent. Taken together with the income tax change, this will mean a significant reduction in the tax burden on small businesses, which are so crucial for future growth and employment.

H13. The income tax changes I have announced today will take effect under PAYE on the first pay day after 17 May. They will cost a little over £2 billion in 1987-88 over and above the cost of statutory indexation.

H14. The overall cost of all the measures in this year's Budget, again on an indexed basis, is a little over £2½ billion. And I have been able to make this worthwhile reduction in tax while still achieving my objective of a PSBR of £4 billion.



**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**



FROM: A C S ALLAN

*Final draft.*

DATE: 13 March 1987

MR SCHOLAR

- cc: Chief Secretary
- Financial Secretary
- Economic Secretary
- Minister of State
- Sir P Middleton
- Sir T Burns
- Sir G Littler
- Mr F E R Butler
- Mr Wilson
- Mr Cassell
- Mr Monck
- Mr Sedgwick
- Mr Odling-Smee
- Mr Culpin
- Miss O'Mara
- Miss Sinclair
- Miss Evans
- Mr Cropper
- Mr Tyrie
- Mr Ross Goobey
- Mr Battishill - IR
- Mr Isaac - IR
- Mr Painter - IR
- Mr Beighton - IR
- Mr McManus - IR
- Sir Angus Fraser - C&E
- Mr Knox - C&E
- Mr Wilmott - C&E
- Mr Bone - C&E

**BUDGET SECRET**

*MASTER COPY*

*Some changes + annotation*

*plan for a new fund comm. with other comm.*

*This is the final draft*

**B.L.O.**

**BUDGET STATEMENT: SIXTH DRAFT**

I attach the sixth draft of the Budget Statement.

2. This may be the last full draft that is circulated, so please could copy recipients check their sections carefully and let me have any comments by close tonight.

*ACSA*

A C S ALLAN

**SECRET**

**BUDGET SECRET**

**NOT TO BE COPIED**



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**A. INTRODUCTION**

A1. The setting for this year's Budget is more favourable than it has been for very many years. We are <sup>now</sup> entering our seventh successive year of steady growth, <sup>and</sup> ~~at the top of the international league table.~~ We are entering the fifth year in which this ~~steady growth~~ has been combined with low inflation. The public finances are sound and strong, and unemployment is falling.

A2. These are the fruits of the Government's determination, in bad times as well as good, to hold firmly to our policies of sound money and free markets. Once again, I reaffirm those policies.

~~A3. So the Budget I present today is a Budget built on success, and a Budget for success.~~

~~A3~~ A4. I shall begin, as usual, by reviewing the economic background to the Budget. I shall then turn to monetary policy and to the fiscal <sup>outlook</sup> ~~prospect~~ this year and next. Finally, I shall propose some changes in taxation designed to improve still further the prospects that lie before us. A number of press releases, filling out the details of my proposals, will be available from the Vote Office as soon as I have sat down.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**

FINAL

**B. THE ECONOMIC BACKGROUND**

B1. I start with the economic background.

B2. Nineteen eighty-six was dominated by the sudden collapse of the oil price. Our own economy was affected not only directly, as a major oil producer and exporter, but also by the pause in world growth as the world economy adjusted to what has been described as the third oil shock. Despite this dislocation, however, the economy has developed in most respects as I foreshadowed a year ago.

B3. In 1986 as a whole output grew by a further  $2\frac{1}{2}$  per cent or so, which compares well with the experience of other industrialised countries. It is worth recalling that ~~in~~ <sup>during</sup> the 1960s, and again in the 1970s, Britain's growth rate was the lowest of all the major European economies. By contrast, during the 1980s, our growth rate has been the highest of all the major European economies.

B4. And this greatly improved growth performance has ~~coincided~~ <sup>been accompanied by</sup> with falling inflation, which at  $3\frac{1}{2}$  per cent in 1986 ~~recorded~~ <sup>reached</sup> the lowest figure for

**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



almost 20 years. Over the lifetime of this Parliament, inflation has averaged less than 5 per cent, ~~whole~~ <sup>whole</sup> growth <sup>has averaged</sup> (almost) 3 per cent.

B5. During the first half of last year exports and hence output were affected by the pause in world growth to which I have already referred. But since the middle of the year exports have grown strongly. Indeed, over the last three months the volume of exports of manufactures was 6 per cent higher than a year earlier - a better performance than that of any other major economy. This pattern was reflected in the rapid growth of manufacturing output in the second half of last year.

B6. This resurgence of economic growth, coupled with the special measures we have taken, has brought about a welcome fall in the number of people out of work. Since ~~August~~ <sup>July</sup> unemployment has fallen by more than 100,000; the largest six-monthly fall since 1973. Though the numbers out of work are still far too high, both youth unemployment and long-term unemployment are now lower than they were a year ago.

B7. I announced a number of specific employment measures in my last Budget, and since then, my Rt Hon and Noble Friend the Secretary of State for Employment has further extended the ~~successful~~

\* What is the present (annual) growth rate? @ 2.7% 1983

SECRET

SECRET



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



Restart programme for the long-term unemployed. There will also be more places on the ~~successful~~ Enterprise Allowance Scheme, and the number of Jobclubs is to be quadrupled. The new Job Training Scheme will ~~give~~ <sup>eventually</sup> give a quarter of a million people, most of them youngsters, vocational training leading to recognised qualifications. With these and other measures, this Government has developed its employment and training programmes on a scale which no other country can match. But the best hope of all for the unemployed ~~lies in~~ <sup>is</sup> the continuing vigour of the economy.

B8. Since the early months of last year, there has been a further surge in manufacturing productivity. This continues the remarkable improvement in productivity growth achieved by British industry throughout the 1980s. <sup>During</sup> In the 1960s, and again in the 1970s, growth in manufacturing productivity in the UK was the lowest of all the seven major industrial countries in the world. During the 1980s, our annual rate of growth of output per head in manufacturing has been the highest of all the seven major industrial countries.

B9. The recorded current account of the balance of payments went into deficit in 1986 by around £1 billion. This followed a cumulative current account surplus of some £20 billion between 1979 and



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



BUDGET

1985. Some deterioration in our current account was inevitable in the face of a £5 billion loss of earnings on oil trade virtually overnight. But the significance of this should not be exaggerated. The exchange rate adjustment that followed the fall in the oil price is already contributing to an improved non-oil trade performance. And earnings from the massive stock of net overseas assets we have acquired since 1979, ~~which at well over £100 billion is second only to that of Japan,~~ will provide a continuing support to the current account in the years ahead.

At well over £100 billion our net overseas assets are ~~higher~~ now greater than at any time since the war, and stand only 5% short of Japan.

B10. Looking ahead, I expect 1987 to be another year of ~~steady~~ balanced growth with low inflation. Total output is forecast to rise by 3 per cent, with exports and investment <sup>by</sup> rather more than that. By then we will have registered the longest period of steady growth, at a rate approaching 3 per cent a year, that the British economy has known since the War. Manufacturing industry, in particular, should do well in 1987. And with the non-oil economy set to grow at 3½ per cent, there is every prospect of unemployment continuing to fall throughout the year. In last year's Budget Speech I said that the outlook for jobs depended on a sustained improvement in the performance of business and industry. That sustained improvement in economic performance ~~has occurred and is continuing.~~ <sup>is now well under way.</sup>



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



B11. Despite the strong growth in exports, it will inevitably take time for the full effect of the exchange rate adjustment to work through. The current account is thus likely to remain in deficit this year, by some £2½ billion, around half of one per cent of GDP.

B12. As I foreshadowed in the Autumn Statement, inflation may continue to edge up for a time, perhaps ~~to a little over~~ <sup>exceeding</sup> 4½ per cent by the Summer, before falling back to 4 per cent by the end of the year. While short-term fluctuations are inescapable, it remains the Government's prime objective to keep inflation on an ~~unambiguously~~ downward underlying trend.

B13. Given the continuation of present policies in this country, the biggest risk to the excellent prospect I have outlined is that of a downturn in the world economy as a whole. There are still serious imbalances afflicting the three major economies - the United States on the one hand and Japan and Germany on the other - which, if not handled properly, could lead to a simultaneous downturn in all three. And this in turn could be exacerbated by renewed turmoil in the foreign exchange markets, whose tendency to overshoot is as notorious as it is damaging.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



B14. It was to address these dangers that the Finance Ministers and Central Bank Governors of six major nations met in Paris last month, and agreed among other things to co-operate closely in fostering a period of exchange rate stability. In my Budget Speech last year, I said:

"Provided we are not over-ambitious, I believe that the Plaza accord is something we can usefully build on."

That is what we have now done, with Plaza II. But it would be idle to deny that the wider risks still remain.

B15. Short of a world downturn, which can and must be avoided, British industry now has an outstanding opportunity, with growing markets at home and overseas, low inflation, rapidly growing productivity and greatly improved profitability. Provided it can control its costs and maintain its present competitive advantage, and assuming the continuation of present policies, we can look forward to many more years of strong growth combined with low inflation.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**

FINAL

**C. MONETARY POLICY**

C1. For its part, the Government will keep in place a sound and prudent financial framework. That means, as it has done since 1980, the medium-term financial strategy.

C2. The central objective of the MTFS is <sup>gradually</sup> (steadily) to reduce the growth of money GDP over the medium term, so as to squeeze inflation out of the system and ultimately to achieve price stability.

C3. This requires monetary discipline buttressed by low public sector borrowing. The essential instrument of monetary policy must remain short term interest rates. These will continue to be set in the light of monetary conditions as indicated principally by the growth of narrow and broad money and the behaviour of the exchange rate.

C4. For narrow money, M0, the target range for next year will be 2 to 6 per cent, as foreshadowed in last year's MTFS. For broad money, however, as the Governor of the Bank of England cogently argued in his Loughborough lecture last October, in current circumstances it is probably wiser to eschew an explicit target altogether. But broad money will continue to be taken into account in assessing

**BUDGET SECRET<sub>1</sub>  
BUDGET LIST ONLY**

**NOT TO BE COPIED**



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



monetary conditions, as of course will the exchange rate.

[ C5. In my Lombard Association speech last April, I set out at considerable length precisely how in practice monetary policy is operated. Rt Hon and Hon Members who are interested in such matters will no doubt have observed that Mr Paul Volcker, Chairman of the United States Federal Reserve Board, in his written testimony to the Senate last month, explained how the Fed operates monetary policy in remarkably similar terms. ]

**B.L.O.**

**SECRET**



BUDGET SECRET  
BUDGET LIST ONLY

11a  
NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



FINAL

**D. PUBLIC SECTOR BORROWING**

D1. I mentioned a moment ago the need to keep public sector borrowing low.

D2. The final outturn for the public sector borrowing requirement last year, 1985-86, was just under £6 billion, equivalent to 1½ per cent of GDP, the lowest level since 1970-71. In my Budget last year, faced with a massive loss of what now looks like £7 billion of North Sea oil revenue, I nonetheless decided to hold the PSBR for this year, 1986-87, to £7 billion, or 1½ per cent of GDP.

D3. In the event, this year's PSBR looks like turning out at only £4 billion, or 1 per cent of GDP: the second successive year of significant undershoot.

D4. This successful outcome is chiefly attributable to the remarkable buoyancy of non-oil tax revenues. And this in turn is due not to some short-term surge in consumer spending, but in particular to an increase over last year of no less than a third in the yield of Corporation Tax from an increasingly profitable business and industry.

*in general  
and of the  
Corporation Tax paid by  
an increasingly profitable  
business sector  
in particular.*



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



BUDGET

D5. Looking ahead, there is still a degree of uncertainty surrounding oil prices, and I have therefore stuck to the assumption I made last year that the North Sea price will average \$15 a barrel. But it is clear that the increased flow of non-oil tax revenues, coupled with the prospective further growth of the economy in excess of the growth of public expenditure, puts the public finances in ~~an~~ <sup>a</sup> ~~exceptionally~~ <sup>very</sup> strong position.

D6. I intend to keep it that way. Last year's MTFIS indicated a PSBR for 1987-88 of £7 billion, or 1 3/4 per cent of GDP; and, as the House will recall, I gave an assurance at the time of the Autumn Statement, when I announced a £4 3/4 billion increase in planned public spending in 1987-88, that on no account would I exceed that figure.

D7. Indeed, I believe it is right to go below it. Since its inception in 1980, the MTFIS has indicated a steadily declining path for the PSBR expressed as a percentage of GDP. We have now reached what I judge to be its appropriate destination: a PSBR of 1 per cent of GDP. ~~I intend to stick to that figure.~~ <sup>(My aim will be to keep it there over the years ahead.)</sup> This will maintain a degree of PSBR <sup>fiscal</sup>

prudence that, until this year, had been achieved on only two occasions since 1950.

SECRET

B.L.

SECRET



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



D8. Accordingly, I have decided to provide for a PSBR in 1987-88 of £4 billion.

D9. Inevitably, this greatly diminishes the scope I have this year for reducing the burden of taxation, which of course remains a major objective of Government policy. But I am sure it is right to err on the side of prudence and caution, and to build a still firmer base for the future. That is the principle on which both I and my predecessor have consistently conducted economic policy these past eight years, and I see no reason to depart from it now.

D10. Meanwhile, I would make one further observation, of a different nature. Economic arguments are seldom concluded, one way or another. This is chiefly because it is unusual for economic policies to be held in place long enough to provide sufficient evidence. But the 1980s have been different; and, as a result, one critically important economic argument has now been concluded, finally and decisively.

D11. Throughout our period of office, our critics have consistently maintained not only that a fiscal stimulus would produce real economic growth, but that without an expansionary fiscal policy



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



sustained growth was impossible. They were wrong, and have been proved wrong. The British economy is now embarking on its seventh successive year of steady growth, at an average rate of getting on for 3 per cent a year. And during that time the PSBR, even if privatisation proceeds are added back, has been deliberately and steadily reduced from a shade under 6 per cent of GDP to a little over 2 per cent. Indeed, had I or my predecessor at any time heeded the advice of our so-called expansionist critics, the British economy would never have been in the unprecedentedly favourable position it is in today.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



Final draft

~~E~~ X. EXCHANGE CONTROL

~~E~~ X1. Before I turn to my proposals for changes in taxation, I have one other ~~important~~ change of a specific nature to announce.

~~E~~ X2. In 1979, a few months after the present Government had first taken office, my predecessor announced the abolition of exchange controls, which had been in continuous operation ever since the outbreak of war in 1939. That bold action has, over the past 7½ years, proved wholly beneficial to the British economy; and I am glad to note that other European countries are now moving in the same direction.

~~E~~ X3. But ~~although the operation of exchange control has ceased,~~ the Exchange Control Act ~~itself~~ remains on the Statute book. So long as it does, there is likely to persist a nagging fear that, in certain circumstances, exchange control might be reimposed; and such uncertainty could be damaging.

~~X4. I have therefore concluded that the time has come to repeal the Act, it.~~ The necessary legislation will be contained in this year's Finance Bill.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**

~~X4.~~  
~~X5.~~

I note that, in what was clearly intended to be a major speech in New York in September, the Deputy-Leader of the Labour Party declared that, and I quote:

"The Labour Party has no intention of reintroducing statutory exchange controls".

I am confident, therefore, that the proposal I have just made will be welcomed on all sides of the House.

BUDGET

SECRET

B.L.O.

SECRET

**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**E. BUSINESS AND ENTERPRISE**

- Pat  
Remains E,  
as we said.*
- B* E1. I now turn to taxation. First, taxes on business.
- B* E2. The fundamental reform of the Corporation Tax system which I introduced in 1984 came fully into effect last April. The new system has undoubtedly improved the quality of business investment decisions in Britain, and is also encouraging more overseas companies to set up here.
- B* E3. During the transition to the new system, companies were given advance notice of the main rate of Corporation Tax for the year ahead. This helped them in their forward planning, and I intend as far as possible to continue the practice of setting the rate in advance. Accordingly, I can announce now that the main rate of Corporation Tax in 1987-88 will be unchanged at 35 per cent - lower than in any other major industrial nation, though the United States is now set to emulate us.
- B* E4. The low rate of Corporation Tax enables me to introduced a further simplification into the system.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



*BUDGET*  
E5. At present, while companies' capital gains are liable to Corporation Tax, the amount of such gains is first adjusted by a certain fraction so that the effective rate of tax is the same as that on capital gains made by individuals. This dates back to the time when the two rates of tax were far apart.

E6. This is no longer the case: indeed, the Corporation Tax rate for small companies is now below the Capital Gains Tax rate.

E7. I therefore propose that, from today, companies' capital gains be charged at the appropriate Corporation Tax rate, without adjustment, save for the indexation which applies to all post-1982 gains.

*Hitherto, companies have not been*

E8. It has, however, been argued that it is wrong that, where companies distribute capital gains as dividends, the gains are taxed twice, once in the hands of the company and once in the hands of the shareholder. I believe there is some justice in this complaint. Accordingly, I propose to remedy it by allowing companies to set payments of Advance Corporation Tax against their liability to tax on capital gains.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



~~At the same time, I am conscious that~~

ES. At present, companies are not allowed to set payments of Advance Corporation Tax against their liability to tax on capital gains. This means that, where companies distribute capital gains as dividend, the gains are in effect taxed twice, once in the hands of the company and once in the hands of the shareholder. This gives rise to complaints, which, I believe, have some justification. I therefore propose to allow companies to set payments of Advance Corporation Tax against tax on capital gains.

I propose that, under the new system, companies should be able to set ACT payments against tax on capital gains.



*B* E9. Taken together, these changes should yield £60 million in 1988-89.

*R* E10. I also have some further simplification and rationalisation of the Corporation Tax system to announce.

*V* E11. At present, some companies established before 1965 do not have to pay their Corporation Tax until up to 21 months after the end of the period for which it is due, whereas companies established since 1965 have to pay their tax after 9 months - and some building societies have to pay sooner still.

*R* E12. This difference in treatment cannot be justified. Moreover, it is open to an abuse which could put the timing of a substantial proportion of the total Corporation Tax yield at risk.

*A* E13. I therefore propose that all companies and building societies should be treated the same way, with all liable to pay Corporation Tax nine months after the end of the accounting period on which the tax is due. The change will be phased in, but I would expect it to yield around £100 million in 1988-89.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



~~E14.~~ I also propose to legislate now to pave the way for a new method of collecting Corporation Tax, to be known as Pay and File. Under this system companies will estimate their tax liabilities themselves, and pay on the normal due date. Where it turns out that the initial payment was too low, the company will pay interest to the Revenue; where the initial payment was too high, the Revenue will pay interest to the company.

~~E15.~~ This new approach, which has already been generally welcomed by the business community, is part of a wider programme of streamlining tax collection, and will not come into force until the early 1990s. But by legislating now I am giving taxpayers and their advisers a firm basis on which to prepare for the new scheme.

X ~~E16.~~ While business and industry as a whole <sup>are</sup> ~~is~~ doing well, the North Sea oil sector has inevitably been hard hit by last year's oil price collapse. My Rt Hon Friend the Secretary of State for Energy and I have followed closely the effects on North Sea producers and their suppliers. The industry itself is generally confident about the longer-term prospects; while as for the tax system, not only is it inherently price-sensitive, but the companies



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



themselves have repeatedly stressed their desire for stability.

E17. However, in the light of the immediate problems, I introduced last autumn legislation to bring forward the repayment of over £300 million of Advance Petroleum Revenue Tax. This has already helped many of the smaller and medium-sized companies faced with cash flow difficulties.

E18. I now propose two further Petroleum Revenue Tax reliefs. First, as from today companies may elect to have up to 10 per cent of the costs of developing certain new fields set against their Petroleum Revenue Tax liabilities in existing fields, until such time as the income of those new fields exceeds the costs incurred. Second, there will be a new relief against PRT for spending on research into UK oil extraction that is not related to any particular field.

*believe*  
E19. I ~~hope~~ that these carefully targeted changes will give a worthwhile measure of help to the North Sea oil sector.

*Pat*  
*This is E21 on present version.*  
E20. Last year I put the Business Expansion Scheme onto a permanent footing. However, there is evidence that the present rules produce end-year



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



§ 21A. Training and retraining are vital to a flexible  
 and competitive economy. At present training  
~~financed~~ <sup>financed</sup> by an employer ~~is not~~ that is  
 related to the employer's current job is  
 allowable against tax for the employer and  
 imposes no tax burden on the employee.  
 But an employer who is willing to finance  
 the retraining of workers ~~desires~~ for future  
 employment elsewhere may find that the cost of  
 this is not allowable against tax, as the  
 employer may find that he has ~~received~~ <sup>received</sup> a  
 taxable benefit. I propose to remove some  
 these obstacles. This should ~~remove~~ <sup>help</sup> ~~remove~~ <sup>help</sup> ~~remove~~ <sup>help</sup> ~~remove~~ <sup>help</sup> ~~remove~~ <sup>help</sup>  
 workers to ~~acquire~~ acquire new skills for  
 new jobs.



bunching of BES investments, and hence may crowd out some projects and lead to bad decisions on others. I propose therefore to permit the investor to claim part of the relief against his previous year's income. This will make it easier for companies to raise BES finance throughout the year.

~~E21. Training and retraining are vital to a flexible and competitive economy. Some employers may be willing to help with the retraining of workers who are leaving their current employment. At present the tax system can be an obstacle to this. I propose that both employers and employees should be exempt from tax in this kind of case, which should encourage workers to acquire new skills for new jobs.~~

*22*  
**INSERT E21A (below) HERE (α check)**

~~E22.~~ <sup>E23</sup> E22. The past few years have seen a remarkable and ~~most~~ welcome growth in the number of small businesses and the self-employed. The Government has done a great deal to lighten the burdens on this vitally important sector of the economy. But I am well aware that problems remain, not least in the field of VAT.

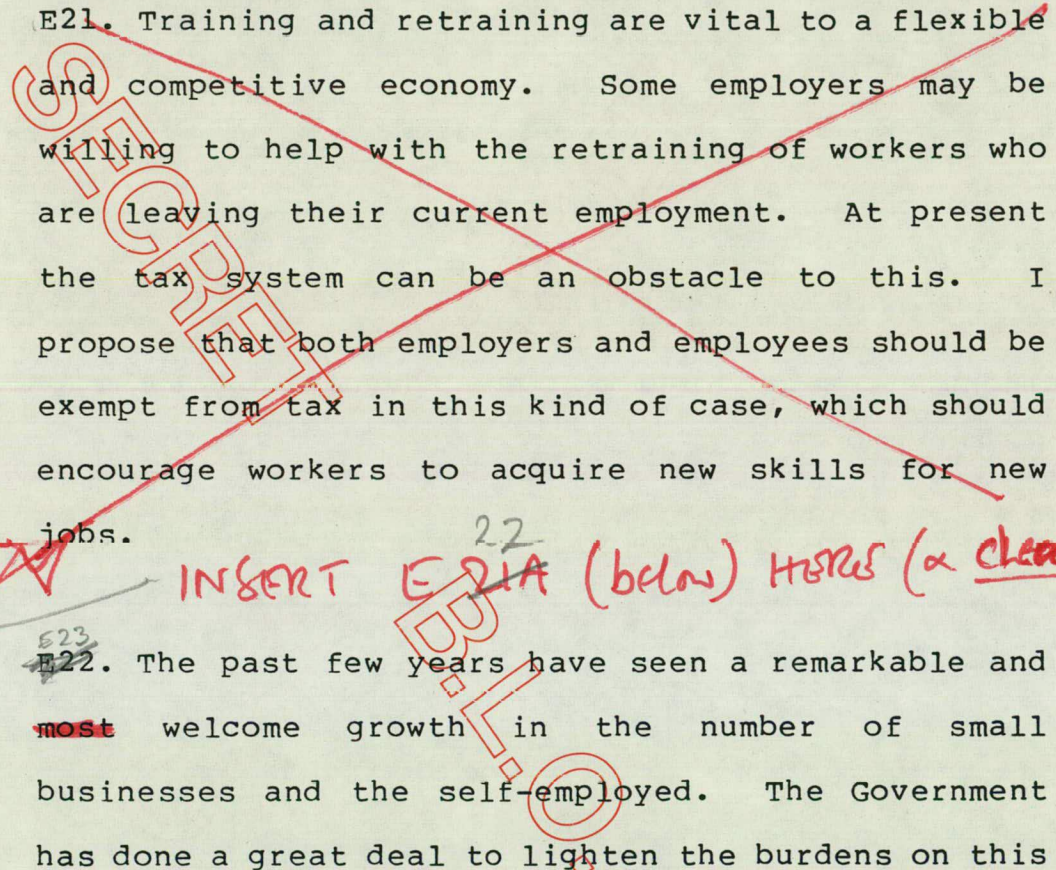
~~E23.~~ <sup>E24</sup> E23. Accordingly, I asked Customs and Excise to issue a consultative document last autumn canvassing a number of changes. In the light of the

*Pat*  
*This is E20 on present version.*

*Riskov*  
*form E 21\**  
*(can & can just*  
*split scales)*  
*here - though*  
*delete "car" from*  
*lms 1 & 6.*

*\* in draft of 12/3*

*Pat*  
*Delete*  
*present E22 & take*  
*in C's version.*





BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



responses to that document, I have four proposals to make.

<sup>5</sup>  
E24. Perhaps the biggest problem faced by the small businessman today is the trade customer who is late in paying his bills: so late, sometimes, that VAT becomes due before the bill has been paid. I can do nothing about late payment; but I can, I hope, do something about the VAT problem.

<sup>6</sup>  
E25. My first and most important proposal, therefore, is that, as from 1 October, businesses whose annual turnover is under £½ million, which means more than half of all traders registered for VAT, will be able to choose to account for VAT on the basis of cash paid and received. In other words, they will have no liability to pay VAT until they themselves have received the money from their customers. In addition to easing the cash flow problems caused by late payers, this system will of course provide automatic VAT relief for bad debts.

<sup>7</sup>  
E26. I have to warn the House, however, that I cannot legally introduce this change without first obtaining a derogation from the European Community's Sixth VAT Directive. I am applying for the necessary derogation today. The House will note that the upper limit of £½ million is considerably



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



greater than the £100,000 suggested in the consultative document.

<sup>8</sup>  
E27. Second, I propose to give these businesses the option of accounting for VAT on an annual basis. Instead of making quarterly returns, they would make regular payments on account, and then file a single return at the end of the year. This option, which offers considerable streamlining, will be available next year.

<sup>9</sup>  
E28. Third, the period within which businesses must apply to be registered for VAT will be extended from ten to thirty days.

<sup>30</sup>  
E29. Fourth, there will be changes to the rules for the special VAT schemes for retailers, and more small and medium-sized businesses will be able to make use of the simpler schemes.

<sup>31</sup>  
E30. I believe that the changes I have outlined, and in particular the option to move to cash accounting, will be widely welcomed by the small business community. The cost will be £115 million in 1987-88 and £60 million in 1988-89.

<sup>2</sup>  
E31. In addition, I propose to increase the VAT



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



threshold to £21,300, to keep it at the maximum permitted under existing European Community law.

<sup>3</sup>  
~~E32.~~ In the light of the responses to the consultative document, I shall not be going ahead either with the withdrawal of the so-called standard method by which retailers calculate their gross takings for VAT, or with the compulsory deregistration of traders below the VAT threshold.

<sup>4</sup>  
~~E33.~~ I have one further measure to help the small businessman, unrelated to VAT. I propose to increase the limit for Capital Gains Tax retirement relief by 25 per cent, from £100,000 to £125,000. ~~As usual, the annual Capital Gains Tax exempt amount will be increased, in line with statutory indexation, to £6,600.~~

*Pat  
Already deleted.*

<sup>5</sup>  
~~E34.~~ An essential element in any ongoing programme of tax reduction and reform <sup>where much still remains to be done,</sup> ~~must always be the~~ <sup>an essential element must always be the</sup> elimination of unintended or unjustified tax breaks, which cause rates of tax generally to be higher than they need to be. Accordingly, I have five proposals to make today to <sup>that</sup> ~~this~~ end.

~~E35.~~ The first concerns VAT, and has already been the subject of extensive consultation. The House will be aware that a business that provides a



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



service that is exempt from VAT cannot in turn deduct input tax on its purchases. But where the activities of a business are in part liable to VAT and in part exempt, the existing rules are excessively generous as to the amount of input tax that can be deducted; and this generosity is being exploited on a growing scale. The rules must therefore be changed, and the changes, which I <sup>(proposed)</sup> announced to the House last December, will come into effect on 1 April. There will be special arrangements to deal with the problem of brewers' tied houses. I am also taking this opportunity to exclude a significant number of small businesses from the scope of this provision. The yield from this change, ~~which in effect is a measure of the potential revenue loss,~~ will be some £300 million in 1987-88 and £400 million in 1988-89.

<sup>7</sup> E36. Second, I propose to change the law so that companies in multinational groups which enjoy dual residence will no longer be able to secure tax relief twice on one and the same interest payment. Genuine trading companies will not be affected. This change, which will take effect on 1 April, follows the similar action recently taken by the United States. It will yield £125 million in 1988-89.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



<sup>37</sup>  
E37. Third, I propose to end the present excessively generous treatment of tax credit relief for foreign withholding tax paid on interest on bank loans. In future, banks will be able to offset this tax credit only against tax on the profit on the relevant loan, and not more widely. This will bring our rules broadly into line with those in most other countries. The change will apply from 1 April this year for new loans and from 1 April next year for existing loans. It will yield some £20 million in 1988-89.

<sup>38</sup>  
E38. Fourth, the tax treatment of Lloyd's syndicates as it applies to the Reinsurance to Close system is clearly unsatisfactory. I therefore propose to bring it into line with that of provisions for outstanding liabilities made by ordinary insurance companies and, indeed, of comparable provisions made by other financial traders. I have asked the Inland Revenue to consult urgently with Lloyd's about the details of the legislation. The new rules will first apply to premiums payable for the Lloyds account which closes on 31 December this year.

<sup>40</sup>  
E39 Fifth, I ~~also~~ propose to implement the Keith Committee's recommendation that interest should be charged in the limited number of cases where an



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



employer does not apply PAYE properly and a formal assessment has to be made to recover the tax. The change will take effect from April next year, and the yield in 1988-89 is estimated at £45 million.

<sup>1</sup>  
E40. I have one further proposal to make in the broad field of the taxation of business and enterprise.

<sup>2</sup>  
E41. In my Budget last year I suggested the possibility of introducing a measure of tax relief for profit-related pay.

<sup>3</sup>  
E42. I pointed then to two considerable advantages that might be expected to flow from arrangements which relate pay to profits. First, the workforce would have a more direct personal interest in the profits earned by the firm in which they work; and, second, there would be a greater degree of pay flexibility in the face of changing market conditions. Such flexibility is vital if, as a nation, we are to defeat the scourge of unemployment.

<sup>4</sup>  
E43. Last July I presented a Green Paper on Profit-Related Pay in conjunction with my Rt Hon and Noble Friend the Secretary of State for Employment and my Rt Hon Friend the Secretary of State for



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



Trade and Industry. I now propose to introduce a scheme of tax relief broadly along the lines floated in the Green Paper.

<sup>5</sup>  
E44. My proposals depart from those in the Green Paper in one important respect. I am doubling the proportion of an employee's profit-related pay that will be tax free from a quarter to a half, and I am also increasing the upper limits on the relief. So for a married man on average earnings receiving 5 per cent of his pay in profit-related form, the tax relief will be equivalent to a penny off the basic rate of income tax. The cost will inevitably depend on take-up: it could be £50 million in 1988-89, building up to substantially more than that, <sup>as</sup> take-up grows, and <sup>the</sup> the proportion of an employee's pay which is profitrelated rises.

<sup>6</sup>  
E45. Profit-related pay is no panacea. But then there are no panaceas. What it is is a tool to help British business gradually to overcome one of our biggest national handicaps: the nature and behaviour of our labour market. I am today challenging British management to take advantage of that tool and to make good use of it, for the good of their firm, their workforce and their country.



BUDGET SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**F. TAXES ON SAVING**

F1. I turn now to the taxation of savings.

F2. A central theme and purpose of the Government's policies is the creation of a genuine popular capitalism. ~~what used to be called, when ambitions were more limited and language more inhibited, a property-owning democracy.~~

F3. That means wider home ownership, wider share ownership, and wider pension ownership. Over the past eight years, the Government has actively promoted the first two, and has now embarked on the third. Home ownership, above all through the council tenant's right to buy. And share ownership, through the rapid growth of employee share schemes; through the massively successful privatisation programme, where Britain has led the world; and most recently through the new Personal Equity Plans, which I announced in last year's Budget and which started up on 1 January this year. In the first month of the scheme, more than 2,000 people a day took out Personal Equity Plans, many of them first-time investors, as I had hoped.



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



F4. We know that 63 per cent of households now own their own homes, <sup>2½ million more than in</sup> ~~compared with 55 per cent in 1979.~~

→ There have been, ~~However,~~ no official figures for the more explosive growth of share ownership in Britain over the past eight years. The Treasury and the Stock Exchange therefore jointly commissioned a major independent survey of individual shareholding in Britain. The results are now available. They show that there are now some 8½ million individual shareholders in this country - amounting to one fifth of the total adult population, and roughly three times the number there were in 1979.

F5. And then there is wider pension ownership. Two years ago, the Government embarked on a major strategy to extend the coverage of private pension provision and to give individuals far more flexibility and choice in the way they provide for their retirement. We have already introduced a number of important new measures to that end, and the tax changes I am announcing today will complete the picture.

F6. The cornerstone of the Government's pensions strategy is the introduction of an entirely new means of provision for retirement, developed by my Rt Hon Friend the Secretary of State for Social



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



Services. This is the personal pension, which will be launched at the beginning of next year, three months earlier than planned.

F7. Personal pensions are an important new dimension of ownership. They will enable employees - if they so wish - to opt out of their employers' schemes and make their own arrangements, tailored to fit their own circumstances. And they will provide a new opportunity for the 10 million employees who at present do not belong to an occupational scheme to make provision of their own and, if they so wish, to contract out of SERPS.

F8. In my Budget last year I undertook to bring forward proposals to give personal pensions the same favourable tax treatment as is currently enjoyed by retirement annuities. These were duly ~~contained~~ <sup>published</sup> in a consultative document ~~published~~ last November, and the necessary legislation will be contained in this year's Finance Bill.

F9. In addition, to encourage a wider spread of occupational schemes, employers will be able to set up simplified schemes with the minimum of red tape. This will be particularly welcome to many small employers who have been discouraged by the complexity and open-ended commitment of a full-blown final salary scheme. And there will be



BUDGET SECRET  
BUDGET LIST ONLY

BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



much greater scope for transferring between different types of pension scheme. Again, the Finance Bill will contain the necessary tax provisions.

F10. Finally, I have decided to go beyond the proposals set out in the consultative document in one important respect. I propose to allow members of occupational pension schemes to make additional voluntary contributions, with full tax relief, to a separate plan of their own choice instead of, as now, being restricted to plans within their employer's schemes. They will be able to top their pensions ~~right~~ up to the present tax approval limits.

F11. The proposals I have outlined - along with the measures my Rt Hon Friend has already taken - will make it easier for people to take their pensions with them when they change jobs, which will be good both for labour mobility and for independence. They will widen the range of choices people can make about their pensions; and will mean that in future individuals will have much more control over the way in which their own pension contributions are invested.



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



F12. Taken as a whole, the changes we have made in the last two years have brought about a radical transformation in the ways people can provide for their retirement. There are new options for employers, and much greater freedom for individuals to plan their own pensions. This will lead to a further major extension of ownership, as people start to take advantage of the new opportunities.

F13. But the generous tax treatment of pensions can be justified only if it is not abused. I propose, therefore, to introduce some limited changes to the present rules to restrict the excessive relief which can be obtained in some circumstances, particularly by a few very highly paid people. These will include a stricter definition of final salary and, for all arrangements entered into from today, an upper limit of £150,000 on the maximum permissible tax-free lump sum, coupled with more rigorous rules on how pension and lump-sum benefits can be calculated.

F14. The cost of the overall pensions package will inevitably depend on take up, but with that proviso is estimated at £65 million in 1988-89.

F.15 For Friendly Societies, I have decided to replace the existing limit based on the sum assured



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



with a new limit based on annual premiums. I propose to set this at £100 a year, which will greatly increase the scope of the traditional societies to offer life policies to their members.

F16. The tax-exempt limits governing sickness and accident benefits which trade unions provide for their members have not been changed since 1982. With effect from today, I propose to increase them to £3,000 for lump sums and £625 for annuities.

F17. Finally, in this section, I turn to Inheritance Tax.

F18. In my Budget last year I abolished the pernicious Capital Transfer Tax on lifetime gifts between individuals, which was particularly damaging to the ownership and health of family business. This year I propose to extend the same exemption from tax, on similar terms, to gifts involving settled property where there is an interest in possession. This will not, however, apply to discretionary trusts. These changes will be of particular benefit to family businesses and to heritage properties, both of which are often held in trust.



BUDGET SECRET  
BUDGET LIST ONLY

BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



F19. I also propose to make two minor changes affecting business assets. First, <sup>holdings in</sup> ~~in what is~~ <sup>companies quoted on the unlisted securities market</sup> perhaps an unwanted tribute to the unlisted

~~securities market, holdings in USM companies will~~ henceforth be treated for Inheritance Tax purposes in precisely the same way as holdings in companies with a full Stock Exchange listing. Second, business relief for minority holdings in excess of 25 per cent in unquoted companies will be increased from 30 per cent to 50 per cent. The purpose of both these changes is to concentrate business relief more accurately on those assets which could provide funds to pay the tax only at the risk of damaging the business.

F20. The abolition of the tax on lifetime giving was of the first importance to family businesses. But I remain conscious that it did little to help the smallest taxable estates, where the family home is often the <sup>Principal</sup> ~~main~~ asset.

F21. I therefore propose to make a substantial increase in the threshold for Inheritance Tax, from £71,000 to £90,000, coupled with a simplification of the rate structure from seven rates to four. As a result of this change, the number of estates liable to Inheritance Tax will be cut by roughly a third.



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**BUDGET SECRET  
BUDGET LIST ONLY**

**NOT TO BE COPIED**

The cost will be £75 million in 1987-88 and £170 million in 1988-89.

F22. Despite this substantial relief, however, and all the other much-needed reliefs that my predecessor and I have introduced since 1979, the House may be interested to learn that the expected yield of Inheritance Tax in 1987-88, at over £1 billion, is ~~nearly~~ three times the yield of Capital Transfer Tax in 1978-79, an increase in real terms of almost 50 per cent.

F 23 Below



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET



(It is the same story with)

~~the~~

F23. As for the other Capital Taxes, over the same period the yield of Capital Gains Tax has risen in real terms by more than 80 per cent and of Stamp Duty by 140 per cent. These increased yields are not unconnected with the fact that, since we first took office, the severity of these taxes has been significantly eased.

I have started to keep the bank - maybe with higher rate - too - for wind-up.

Since we first entered office, their severity has been significantly ~~just~~ eased. And the yield of Capital Gains Tax has risen in real terms by 80 per cent and that of Stamp Duty by 140 per cent.

Other the same power

The London Market may also be back for wind-up



SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**G. TAXES ON SPENDING**

G1. I now turn to the taxation of spending.

G2. I have already announced some important changes in value added tax to prevent avoidance and to help the small businessman. I have no other proposals for major changes in VAT this year.

G3. However, in the light of representations I have received, I have decided to extend slightly the VAT reliefs I introduced last year for certain aspects of charitable work.

G4. I propose to relieve charities from VAT on certain welfare vehicles used by hospices to transport the terminally ill; on installing or adapting lavatory or bathroom facilities in charity homes for the disabled; on drugs and chemicals used by a charity in medical research; and on specialised location and identification equipment employed by mountain rescue and first aid services.

G5. While on the subject of charitable giving, I should remind the House that this year's Finance Bill will increase the limit on donations to charity under the new payroll giving scheme, which starts next month, from £100 to £120 a year.



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



Q8. In my 1985 Budget I announced the first stage in the process of increasing the rate of Vehicle Excise duty on farmers' heavy lorries & only now we will be able to make good the public roads. I introduced the second stage in last year's Budget & propose to complete the process this year. →



G6. Next, the excise duties. I propose to maintain the revenue from the taxation of gambling, but to make some readjustment within the total. I therefore propose to increase the gaming machine licence duty by about a quarter, which will restore it in real terms to its 1982 level, when it was last increased; and to offset this by abolishing, from 29 March, the tax on on-course betting. <sup>I am sure</sup> ~~I hope this measure will be of some assistance to~~ the racing and bloodstock industry, as well as consoling those hon Members who have complained to me about the clash this year between Budget Day and the Champion Hurdle.

G7. In my Budget Statement last year, I <sup>under took</sup> ~~gave~~ ~~advance notice of my intention~~ to introduce a tax differential in favour of unleaded petrol, ~~so as~~ to offset its higher production cost. I can now announce that the differential will be <sup>(five pence)</sup> ~~5 pence~~ a gallon. This means that the pump price of unleaded petrol should be no higher than that of 4-star leaded petrol. The change will take effect from 6 o'clock this evening.

G8. Following on from the action I took last year, I propose to increase the rates of Vehicle Excise Duty on farmers' lorries, to bring them into line with the use they make of the public roads. This change will take effect from midnight tonight. I

BUDGET

SECRET

SECRET

~~G8. In my 1985 Budget I announced a first stage in the process of~~



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



I also propose to increase the rates of duty on trade licences and to rationalise the taxation of recovery vehicles.

G9. I have no further changes to propose this year in the rates of excise duty.

**SECRET**

**B.L.O.**

**SECRET**



BUDGET SECRET  
BUDGET LIST ONLY

BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



**H. INCOME TAX**

H1. Finally, I turn to income tax.

H2. There is now a worldwide consensus on the economic desirability of tax reform and tax reduction, and in particular the reduction of income tax. This was demonstrated most recently by the various national policy declarations that emerged from last month's meeting of Finance Ministers from the major industrial nations.

H3. Lower rates of tax sharpen up incentives and stimulate enterprise, which in turn is the only route to ~~improved~~ <sup>better</sup> economic performance. ~~It~~ <sup>And</sup> is only by improving our economic performance that we will be able to afford to spend more on public services; only by improving our economic performance that we will be able to create jobs on the scale that we all want to see.

H4. That is why, ever since we first took office in 1979, we have consistently sought to reduce the burden of income tax. We have cut the basic rate of tax from 33 per cent to 29 per cent and sharply reduced the punitive higher rates we inherited from the Party opposite. ~~We~~ <sup>And</sup> have increased the main tax



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



allowances by 22 per cent more than inflation, taking almost 1½ million people out of income tax altogether.

H5. For 1987-88 I propose to raise all the main thresholds and allowances by the statutory indexation factor of 3.7 per cent, rounded up. Thus the single person's allowance will rise by £90 to £2,425 and the married man's allowance by £140 to £3,795. The single age allowance will rise by £110 to £2,960 and the married age allowance by £170 to £4,675. The age allowance income limit becomes £9,800. I propose to raise the first, 40 per cent, higher rate threshold by £700 to £17,900, in line with statutory indexation; but the threshold for the 45 per cent rate will go up by only £200 to £20,400. The other higher rate thresholds will remain unchanged.

H6. I have two other changes in allowances to announce. First, I propose to give an additional increase in the age allowance for those aged 80 or over. For them, the increase will be double the amount due under statutory indexation, so that, for the very elderly, the single age allowance will rise by £220 to £3,070 and the married age allowance by £340 to £4,845. Around 400,000 taxpayers will



BUDGET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



benefit from this new measure, and up to 25,000 of them will be taken out of income tax altogether.

H7. Second, the blind person's allowance has remained unchanged since 1981, when it was increased by £180 to its present level of £360. For 1987-88 I propose to increase it by a further £180, to £540.

H8. Finally, I turn to the basic rate of income tax. This is the starting rate of income tax for everyone and the marginal rate for the overwhelming majority of taxpayers.

H9. In my Budget speech last year I reaffirmed the aim set out by my predecessor in 1979, to reduce the basic rate of income tax to no more than 25 per cent. That remains my firm objective.

H10. However, given my decision to use the greater part of the fiscal scope I now have to reduce the Public Sector Borrowing Requirement, that goal cannot be achieved in this Budget.

H11. I can, however, take a further step towards it, as I did last year. I am therefore reducing the basic rate of income tax by twopence, to 27 per cent. This reduction, which will benefit every



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



taxpayer in the land, will be worth more than £3 a week to a ~~married man~~ <sup>a man</sup> on average earnings.

H12. There will, of course, be a consequential reduction in the rate of Advance Corporation Tax, and - as last year - I also propose a corresponding cut in the small companies' rate of Corporation Tax from 29 per cent to 27 per cent. Taken together with the income tax change, this will mean a significant reduction in the tax burden on small businesses, which are so ~~crucial~~ <sup>important</sup> for future growth and employment. <sup>jobs.</sup>

H13. The income tax changes I have <sup>just</sup> ~~announced today~~ will take effect under PAYE on the first pay day after 17 May. They will cost a little <sup>more than</sup> ~~over~~ £2 billion in 1987-88 over and above the cost of statutory indexation.

H14. The <sup>total</sup> ~~overall~~ cost of ~~all~~ the measures in this year's Budget, again on an indexed basis, is a little over £2½ billion. ~~And I have been able to make this worthwhile reduction in tax while still achieving my objective of a PSBR of £4 billion.~~



BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET  
BUDGET LIST ONLY

NOT TO BE COPIED



PUT



PS / Chancellor

Budget Speech 6" Draft.

A few more small  
prints.

PJR



BUDGET SECRET

- A3 If for success is underlined, then should not on success be underline for emphasis in delivery?
- D4 On re-reading this, I find it very complex. "And this in turn is due not ....., but in particular .... of no less ....".  
Maybe: "This buoyancy, in turn, is due not to some short-term surge in consumer spending: it is due, in particular, to an increase ....".
- E8 First sentence difficult to deliver? You could start: "Meanwhile it has been argued that, where companies distribute capital gains as dividends, the gains are being taxed twice, once ..... shareholder.".
- E16 "While business and industry as a whole is doing well ....". I think are would be more natural.
- E35 Line 12. It occurs to me to wonder whether "announced" is the right word. "Proposed"?
- H13-  
14 over.....over....overall.....over

PJC





FWP

CHANCELLOR

SPEECH: LOOSE ENDS

1. Cockshy peroration and section X enclosed.
2. You wanted to were thinking of including a piece on the Growth League Tables. I attach a suggestion.
3. The statement in B3 on growth is OK, though 82 H2 on 81 H1 is only gives growth of 1.2 per cent. But
  - as you said, the 1976-79 growth has minuses either side;
  - we know '87 H1 is going well;
  - growth picked up very rapidly in 1982 Q4 (up from 100.1 to 101).
4. The announcement about the start date for personal pensions was omitted from F6 by mistake in the redrafting. Apologies. I shall reinsert it next time round.
5. The MST <sup>has proposed a slight redraft of</sup> ~~is looking at~~ your wording on E37. See his minute.

AH



PHW

**B. THE ECONOMIC BACKGROUND**

B1. I start with the economic background.

B2. Nineteen eighty-six was dominated by the sudden collapse of the oil price. Our own economy was affected not only directly, as a major oil producer and exporter, but also by the pause in world growth as the world economy adjusted to what has been described as the third oil shock. Despite this dislocation, however, the economy has developed in most respects as I foreshadowed a year ago.

B3. In 1986 as a whole output grew by a further 2½ per cent or so, which compares well with the experience of other industrialised countries. Indeed, we have now enjoyed the longest period of steady growth, at a rate approaching 3 per cent, that the UK economy has known since the War.) ~~and~~

Moreover, in both the 1960s and the 1970s, our growth rate was the slowest among the major European economies. But since 1980, we have grown faster than any of these rivals. //

B3A. This <sup>improved growth</sup> has coincided with falling inflation, which at 3½ per cent in 1986 recorded the lowest figure for almost 20 years. Over the lifetime of this Parliament, inflation has averaged less than 5 per cent.

B4. During the first half of last year exports were affected by the pause in world growth to which I



Thinker: PWP  
WR speaker:

D7. Indeed, I believe it is right to go below it. I propose to hold the PSBR to 1% of GDP [ , which I judge to be the appropriate and sustainable level for the medium-term ]. This will maintain a degree of fiscal prudence that, until this year, had been recorded on only two occasions since the War.

Ch

Robert & I thought something along these lines would avoid "reaching destination by accident" nuances.

AA