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PART F

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1987 BUDGET
STATEMENTS

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BUDGET SECRET

Copy 1 of 15

PDP



FROM: P D P BARNES

DATE: 13 MARCH 1987

PS/CHANCELLOR

cc PS/Chief Secretary
 PS/Financial Secretary
 PS/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

BUDGET STATEMENT: FIFTH DRAFT

below
 The Economic Secretary has seen the Financial Secretary's minute to the Chancellor of 12 March.

which you rejected.
 2. The Economic Secretary agrees with the Financial Secretary's suggestion for a new passage in H3. The Economic Secretary suggests adding at the end of this passage "and indeed they have done so".

P D P BARNES
 Private Secretary



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

*The track is this (page 2)
Don't know about woman
on average female
comp 2P off is
with 12 over
73 a wk.*

*As for X, we do of course Law F 23.
But we do not believe
we can start
with no higher
rate of 15
any more*

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).

*is a budget
what,
So far from
cutting the
basic rate,
is actually
making
New*

X

*for the basic rate.
I am perfectly happy
for the budget 'cut
taxes to increase receipts'
argument to be used
debate (a) there is
concern of what we have done (b)
as a whole we have done
in the future. But we may do
what we can. But we are
doing this
you.*

NORMAN LAMONT

BUDGET: SECRET

*(about
marginally)
more so.
And of course the
Laffont's cost is
more which is
not planned)*

A P



FROM: A P HUDSON

DATE: 16 March 1987

PS/FINANCIAL SECRETARY

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

BUDGET STATEMENT: SIXTH DRAFT

The Chancellor has seen the Financial Secretary's 13 March minute. He does not think it is quite accurate to say that "anyone" on average earnings gains over £3 a week. For a women on average adult female earnings, the gain is considerably lower.

2. Paragraph F23 already hints at the "cut taxes to increase receipts" issue. The Chancellor does not believe we can sensibly apply the argument to the higher rates of income tax in a Budget which, so far from cutting the higher rates, is actually making them (albeit marginally) more severe. And of course the Lafferite case is most unlikely to be valid or even plausible for the basic rate. The Chancellor is quite happy for the argument to be used in the Budget Debate and thereafter

- (a) in the context of what we have done; and
- (b) as a hint of what we may do in the future.

But, to repeat, not in the context of what we are doing this year.

A handwritten signature in dark ink, appearing to be 'A P HUDSON'.

A P HUDSON



Phf

FROM: A P HUDSON
DATE: 13 March 1987

SIR T BURNS

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

BUDGET STATEMENT: PARAGRAPH D7

The Chancellor was grateful for your 12 March minute.

2. On inspection of the figures, he agrees it is safer to say "since 1950".

AH

A P HUDSON



FROM: N G FRAY
DATE: 13 MARCH 1987

CHANCELLOR

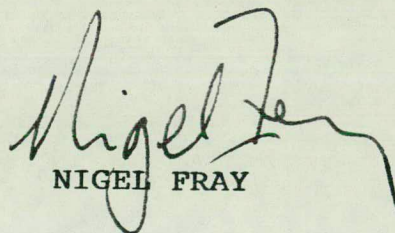
cc Mr Allan
Mr Hudson

1987 BUDGET STATEMENT: A RECORD BREAKER?

I have double checked the league table of Budget statements and have discovered a few errors. A revised table is attached at Annex A. I must emphasize that the table gives only a selection of statements delivered by well known Chancellors this century and there is no guarantee, even though all of these statements are delivered in excess of one hour, that there are no shorter statements in existence. But, should you deliver your statement in an hour or under, I think you would be on safe ground to say that you had delivered one of the shortest Budget statements since 1900.

You may also be interested to see the introduction of Sir Geoffrey Howe's Budget speech in 1983 (Annex B). Sir Geoffrey said that this statement was to be the shortest that he had delivered, though his first statement, on 12 June 1979 lasted only 1 hour 10 minutes. Sir Geoffrey might have considered that the 1979 Budget was not a fully fledged statement, indeed, his statements from 1980 onwards did get shorter.

I hope this is useful.


NIGEL FRAY

LENGTH AND DURATION OF BUDGET SPEECHES

Listed below are a selection of the longest and shortest Budget speeches since 1853:

CHANCELLOR	APPROX NO OF WORDS	DURATION
Nigel Lawson		
18 March 1986	9,918	1hr 16
19 March 1985	9,786	1hr 15
13 March 1984	(Not counted)	1hr 20*
Sir Geoffrey Howe		
15 March 1983	(Not counted)	1hr 24*
9 March 1982	18,200	1hr 45
March 1981	14,500	1hr 30
26 March 1980	19,000	2hrs
12 June 1979	11,500	1hr 10
Denis Healey		
11 April 1978	9,500	1hr 4
24 March 1974	20,500	2hrs 20
Anthony Barber		
6 March 1973	18,000	2hrs
30 March 1971	15,500	1hr 50
Roy Jenkins		
14 April 1970	17,000	1hr 55
19 March 1968	20,000	2hrs 10
James Callaghan		
3 May 1966	13,000	1hr 20
6 April 1965	22,000	2hrs 20
Reginald Maudling		
14 April 1964	13,000	1hr 30
3 April 1963	17,000	1hr 50
Selwyn Lloyd		
9 April 1962	14,000	1hr 30
17 April 1961	13,000	1hr 20
Derick Heathcoat Amory		
4 April 1960	13,000	1hr 20

* Time taken from Hansard.

CHANCELLOR

APPROX NO OF WORDS DURATION

Harold Macmillan

17 April 1956 15,000 1hr 45

R A Butler

19 April 1955 11,250 1hr 10

11 March 1952 13,850 1hr 25

Sir Stafford Cripps

18 April 1950 18,000 2hrs

W S Churchill

15 April 1929 15,500 1hr 45

28 April 1925 16,200 2hrs

D Lloyd George

2 April 1912 8,993 1hr 30

30 June 1910 8,222 1hr 25

Sir Mark Hicks Beach

5 March 1900 - 35 mins

Benjamin Disraeli

4 April 1867 6,500 45 mins

Sir William Gladstone

18 April 1853 35,000 4hrs 45

BROADCASTING OF PARLIAMENT (ANNUAL REVIEW)

Dr. Edmund Marshall accordingly presented a Bill to provide for the annual review of arrangements for the broadcasting of parliamentary proceedings: And the same was read the First time; and ordered to be read a Second time upon Friday 15 April and to be printed. [Bill 100.]

WAYS AND MEANS

Budget Statement

Mr. Deputy Speaker (Mr. Bernard Weatherill): Before I call the Chancellor of the Exchequer, it may be for the convenience of hon. Members if I remind them that, at the end of the Chancellor's speech, as in past years, copies of the Budget resolutions will not be handed around in the Chamber but will be available to hon. Members in the Vote Office.

3.38 pm

INTRODUCTION

The Chancellor of the Exchequer (Sir Geoffrey Howe): The longest Budget speech that I have been able to trace was given by Mr. Gladstone on 18 April 1953—*[Interruption.]*

Mr. Deputy Speaker: Order. Perhaps the Chancellor would like to start again.

Sir Geoffrey Howe: I am content, Mr. Deputy Speaker, to recognise that, although Liberals have long lives, they do not live that long. The date to which I refer, of course, was 1853. The speech lasted for about 4¾ hours. The then Leader of the Opposition said of the speech: "... it was so extensive that it is impossible, without consideration, to weigh its disadvantages and advantages". That could have its merits in certain circumstances. But I can assure the House that I shall not try to rival Mr. Gladstone. Instead, I shall try to follow Disraeli, who delivered a Budget speech in 1867 lasting only 45 minutes. I am afraid that I cannot quite match that; but at least this will be one of the shortest—perhaps the shortest—of my Budget speeches, or at any rate the shortest so far. And that will not be its only attractive feature.

I begin, as last year, by making it clear that I shall today be proposing further significant cuts in the taxes paid both by businesses and by individuals. These proposals will be consistent with our medium-term strategy for effective control of the money supply, for lower public borrowing, and for further progress on inflation.

The requirement we saw, and the country accepted, in 1979, was for resolve, for purpose and for continuity. My proposals in this Budget are rooted in that same resolve, and will maintain that purpose, and that continuity. They are designed to further the living standards and employment opportunities of all our people and to sustain and advance the recovery for which we have laid the foundations.

WORLD ECONOMY

In 1979 it was clear that the long-term decline of Britain's relative position in the world economy called for a fresh start, for a radical new beginning. And it soon became apparent, as the effects of the second oil price shock hit home, that that fresh start would have to be made in an international setting that was increasingly difficult.

Last year world output and trade were lower than generally expected. In the major industrial economies output fell; and more than 30 million of their people were unemployed.

Developing countries have faced similar difficulties. Weak markets for their products, high oil import costs and

PPS/CHANCELLOR

FROM: COLIN MOWL
DATE: 13 March 1987

cc Mr Scholar
Mr Sedgwick

PS/Inland Revenue
Mr Calder - IR

BUDGET STATEMENT: PARAGRAPHS F22 AND F23

Mr Sedgwick showed me paragraphs F22 and F23.

2. In the sixth line of F22 'nearly' should be deleted as the increase is almost exactly three times. I imagine the 'nearly' was consistent with the statement in earlier drafts that the expected yield of Inheritance Tax in 1987-88 was nearly £1 billion, compared with the final forecast of over £1 billion.

3. In the third line of paragraph F23 'more than' should be deleted as the increase is again almost exactly 80 per cent.

Colin Mowl

COLIN MOWL

PWH



FROM: A P HUDSON
DATE: 13 March 1987

SIR P MIDDLETON

BUDGET SPEECH

The Chancellor has seen your 12 March minute. He is still considering paragraph C5, and has drafted a compromise version for the time being.

AH

A P HUDSON



FROM: A P HUDSON
DATE: 13 March 1987

AWP

PS/FINANCIAL SECRETARY

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

BUDGET STATEMENT: FIFTH DRAFT

The Chancellor has seen the Financial Secretary's 12 March minute.

2. He has decided not to mention the three measures on employee share ownership in the Budget Speech. He thinks the Financial Secretary could refer to them in his own speech the following day. But he does not think the announcement of a review will cut much ice.

AWP

A P HUDSON

PWP



FROM: A P HUDSON
DATE: 13 March 1987

SIR T BURNS

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

BUDGET STATEMENT: PARAGRAPH B3

The Chancellor was grateful for your 12 March minute.

2. He prefers his revised formulation. But he would like your suggestion to appear in addition in the Budget Brief.

A P HUDSON

A P HUDSON

J. CONCLUSION

Mr Deputy Speaker, in this Budget I have reaffirmed the prudent policies which, despite a year-long coal strike ~~and a~~ ^{followed by a} collapse in the oil price, have given us the strongest economy we have known since the war.

~~Following an Autumn Statement which allows an increase in public expenditure I have once again cut the basic rate of income tax, a cut which the Party opposite are pledged to reverse. And I have done so after increasing public ~~expenditure~~ spending ~~on~~ in very ~~partly~~ ^{areas}~~

~~Following~~ ^{After} an Autumn Statement which increases public spending in priority areas, I have once again cut the basic rate of income tax; a cut which the Party opposite ~~are~~ are pledged to reverse, if they are given the chance - which they will not be.

And I have done ~~at~~ this
while ~~sharply~~ sharply reducing
public borrowing; a combination
that has allowed successive
Governments to thrive.

This is a Budget first of all,
and a Budget for success.
I commend it to the House.



delete 'like'
substitute 'to be'
almost

C.

SPEECH

Final comments on paras

instr ✓ 'Stating'
~~in~~
October!

~~B2~~, ~~B12~~, D2, ~~D11~~, ~~E 20 (x2)~~,
~~E 35~~, ~~E 39~~, ~~F 3~~, F 10, ~~F 15~~,
~~G 7~~, and ~~J 2~~.

Most of these are very minor,
The only one of substance is
Michael Scholar on D11.

Once you have decided on these,
can we take this as the final
text? YES

Re E 20,

I accept both ~~AMH~~

Changes, ~~amh~~ ✓ ~~no just.~~

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FROM: A C S ALLAN
DATE: 16 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 F15
- ✓ 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 - *No comments*
- Mr Bone - C&E

Mr
(No.10)

Norgrove

BUDGET STATEMENT: FINAL DRAFT

I attach the final draft of the Budget Statement.

2. Please could copy recipients check this very carefully, and let me have any comments by 1.00 pm.

ACSA

A C S ALLAN

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*Typist
Green overrides blue.*

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A. INTRODUCTION

A1. The setting for this year's Budget is more favourable than it has been for very many years. We are now entering our seventh successive year of steady growth, and the fifth in which this 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. I shall begin, as usual, by reviewing the economic background to the Budget. I shall then turn to monetary policy and to the fiscal outlook 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.

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B. THE ECONOMIC BACKGROUND

B1. I start with the economic background.

Am B2. ¹⁹⁸⁶ Nineteen eighty-six³ 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 during 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 been accompanied by falling inflation, which at $3\frac{1}{2}$ per cent in 1986 reached the lowest figure for almost 20 years. Over the lifetime of this

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Parliament, inflation has averaged less than 5 per cent, while growth has averaged over 3 per cent.

Agreed ✓

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 July 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 Restart

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programme for the long-term unemployed. There will also be more places on the Enterprise Allowance Scheme, and the number of Jobclubs is to be quadrupled. The new Job Training Scheme will eventually 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 is in 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. During 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

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account surplus of some £20 billion between 1979 and 1985. Some deterioration in our current account was inevitable in the face of a ~~£5~~^{£4} 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 will provide a continuing support to the current account in the years ahead. At well over £100 billion our net overseas assets are now greater than at any time since the War, and second only to those of Japan.

B10. Looking ahead, I expect 1987 to be another year of balanced growth with low inflation. Total output is forecast to rise by 3 per cent, with exports and investment up by 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

See my previous note. MCS feels strongly we should be consistent with FSR.

Agreed X

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in the performance of business and industry. That sustained improvement in economic performance is now well under way.

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 exceeding 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 underlying downward 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

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MOM
(small letter)

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exacerbated by renewed turmoil in the foreign exchange markets, whose tendency to overshoot is as notorious as it is damaging.

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.

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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 ^{gradually} ~~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, it is probably wiser in current circumstances to eschew an explicit target altogether. But broad money will

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continue to be taken into account in assessing monetary conditions, as of course will the exchange rate.

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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 ~~£6~~ £7 billion of North Sea oil revenue, I nonetheless decided to hold the PSBR for this year, 1986-87, to £7 billion, or 1¾ 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 in general and of the Corporation Tax paid by an increasingly profitable business sector in particular.

D5. Looking ahead, there is still a degree of uncertainty surrounding oil prices, and I have

BUDGET

to
almost

MCS:
FSBR says £11½
down to £4¾ bn
could say "almost £7 billion"

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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 a very strong position.

D6. I intend to keep it that way. Last year's MTFS indicated a PSBR for 1987-88 of £7 billion, or 1½ 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 £4½ 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. My aim will be to keep it there over the years ahead. This will maintain a degree of fiscal prudence that, until this year, had been achieved on only two occasions since 1950.

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

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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

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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~~ ^{their} advice, of our so-called expansionist critics, the British economy would never have been in the unprecedentedly favourable position it is in today.

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Our so-called expansionist critics said that this combination could never be. They were wrong. It has.

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~~X.~~ X. EXCHANGE CONTROL

X1. Before I turn to my proposals for changes in taxation, I have one other 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 the Exchange Control Act remains on the Statute book. The time has come to repeal it. The necessary legislation will be contained in this year's Finance Bill.

X4. 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".

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

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F 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.

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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. Hitherto, companies have not been 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 dividends, the gains are in effect taxed twice, once in the hands of the company and once in the hands of the shareholder. I propose that, under the new system, companies should be able to set ACT payments against tax on capital gains.

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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.

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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.

E16. While business and industry as a whole are 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

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themselves have repeatedly stressed their desire for stability.

E17. However, in the light of the immediate problems, I introduced legislation last autumn 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.

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

E20. Last year I put the Business Expansion Scheme onto a permanent footing. However, ~~there is still~~ ^{still} ~~evidence that~~ ^{too much} the present rules produce end-year

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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. I have to set the 1988-89 car and 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 fuel scales which, as already announced, will also be used for VAT purposes from 6 April.

E22. Training and retraining are vital to a flexible and competitive economy. At present, training financed by an employer that is related to the employee'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 for future employment elsewhere may find that the cost of this is not allowable against tax, and the employee may find that he has received a taxable benefit. I propose to remove both these obstacles. This should help more workers to acquire new skills for new jobs.

*M. Haigh (FP)
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E23. ~~The past few years have~~ seen a remarkable and 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.

E24. 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.

E25. 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.

E26. My first and most important proposal, therefore, is that, as from 1 October, businesses whose annual turnover is under £1 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

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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.

E27. 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.

E28. 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.

E29. Third, the period within which businesses must apply to be registered for VAT will be extended from ten to thirty days.

E30. Fourth, there will be changes to the rules for the special VAT schemes for retailers, and more

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small and medium-sized businesses will be able to make use of the simpler schemes.

E31. 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.

E32. In addition, I propose to increase the VAT threshold to £21,300, to keep it at the maximum permitted under existing European Community law.

E33. 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.

E34. 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.

E35. In any ongoing programme of tax reduction and reform, where much still remains to be done, an essential element must always be the elimination of

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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 that end.

E36. 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 proposed 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 will be some £300 million in 1987-88 and £400 million in 1988-89.

E37. 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

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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.

E38. 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.

E39. 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

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legislation. The new rules will first apply to premiums payable for the Lloyds account which closes on 31 December this year.

E40 Fifth, I 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.

E41. I have one further proposal to make in the broad field of the taxation of business and enterprise.

E42. In my Budget last year I suggested the possibility of introducing a measure of tax relief for profit-related pay.

E43. 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

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nation, we are to defeat the scourge of unemployment.

E44. 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.

E45. 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, as take-up grows, and as the proportion of an employee's pay which is profit-related rises.

E46. 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

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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.

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~~G~~ 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.

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, ^{a number} many of them first-time investors, as I had hoped.

F4. We know that 63 per cent of households now own their own homes, 2½ million more than in 1979. However, there have been no official figures for the

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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 at the beginning of next year, three months earlier than planned.

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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 published in a consultative document 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.

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F10. Finally, I have decided to go beyond the proposals set out in the consultative document in one important respect. ^{From} I propose ^{to allow members} ~~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 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.

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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 tax-exempt life assurance 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.

F16. The tax-exempt limits governing sickness and accident benefits which trade unions provide for their members have not been changed since 1982.

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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.

F19. I also propose to make two minor changes affecting business assets. First, holdings in companies quoted on the unlisted securities market 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

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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 principal 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. 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 three times the yield of Capital Transfer Tax in 1978-79, an increase in real terms of almost 50 per cent.

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F23. It is the same story with the other capital taxes. Since we first entered office, their severity has been significantly eased. And over the same period the yield of Capital Gains Tax has risen in real terms by 80 per cent and that of Stamp Duty by 140 per cent.

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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.

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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 am sure that this measure will be welcomed by 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 undertook to introduce a tax differential in favour of unleaded petrol, to offset its higher production cost. I can now announce that the differential will be fivepence 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. In my 1985 Budget I announced the first stage in the process of increasing the rates of Vehicle Excise Duty on farmers' heavy lorries to bring them into line with the use they make of the public roads. I introduced the second stage in last year's Budget and propose to complete the process this

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year. 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.

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3. 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 better economic performance. And 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. And we have increased the main

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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

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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

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taxpayer in the land, will be worth more than £3 a week to a 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 important for future growth and jobs.

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

H14. The total cost of all the measures in this year's Budget, again on an indexed basis, is a little over £2½ billion.

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K J. CONCLUSION

J1. Mr Deputy Speaker, in this Budget I have reaffirmed the prudent policies which, despite a year-long coal strike followed by a collapse in the oil price, have given us the strongest economy we have known since the War.

A. Turnbull
[He says most of increase was not in priority areas. Also I think it's OK as it is.]

J2. After an Autumn Statement which ^{permitted} increased ^{5% in} public spending in priority areas, I have once again cut the basic rate of income tax; a cut which the Party opposite are pledged to reverse, if they are given the chance - which they will not be. And I have done this while sharply reducing public borrowing; a combination that has eluded successive Governments for decades. This is a Budget built on success, and a Budget for success. I commend it to the House.

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÷ 135 = 56½

÷ 130 = 58½

Copy No 1 of 41



FROM: A C S ALLAN

DATE: 16 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
Mr Norgrove
(No.10)

BUDGET STATEMENT: FINAL DRAFT

I attach the final draft of the Budget Statement.

2. Please could copy recipients check this very carefully, and let me have any comments by 1.00 pm.

ACSA
A C S ALLAN

A. INTRODUCTION

A1. The setting for this year's Budget is more favourable than it has been for very many years. We are now entering our seventh successive year of steady growth, and the fifth in which this 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. I shall begin, as usual, by reviewing the economic background to the Budget. I shall then turn to monetary policy and to the fiscal outlook 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

(X) 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 during 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 been accompanied by falling inflation, which at $3\frac{1}{2}$ per cent in 1986 reached the lowest figure for almost 20 years. Over the lifetime of this

Parliament, inflation has averaged less than 5 per cent, while growth has averaged over 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 July 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 Restart

programme for the long-term unemployed. There will also be more places on the Enterprise Allowance Scheme, and the number of Jobclubs is to be quadrupled. The new Job Training Scheme will eventually 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 is in 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. During 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 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 will provide a continuing support to the current account in the years ahead. At well over £100 billion our net overseas assets are now greater than at any time since the War, and second only to those of Japan.

B10. Looking ahead, I expect 1987 to be another year of balanced growth with low inflation. Total output is forecast to rise by 3 per cent, with exports and investment up by 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 $3\frac{1}{2}$ 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 is now well under way.

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 exceeding 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 underlying downward 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.

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.

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, it is probably wiser in current circumstances 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.

COMPTROLLER

III

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

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 a very 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. My aim will be to keep it there over the years ahead. This will maintain a degree of fiscal prudence that, until this year, had been achieved on only two occasions since 1950.

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 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 the Exchange Control Act remains on the Statute book. The time has come to repeal it. The necessary legislation will be contained in this year's Finance Bill.

X4. 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.

20

E. BUSINESS AND ENTERPRISE

X 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. Hitherto, companies have not been 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 dividends, the gains are in effect taxed twice, once in the hands of the company and once in the hands of the shareholder. I propose that, under the new system, companies should be able to set ACT payments against 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. 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.

E16. While business and industry as a whole are 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.

E17. However, in the light of the immediate problems, I introduced legislation last autumn 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.

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

E20. Last year I put the Business Expansion Scheme onto a permanent footing. However, there is still 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.

E21. I have to set the 1988-89 car and 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 fuel scales which, as already announced, will also be used for VAT purposes from 6 April.

E22. Training and retraining are vital to a flexible and competitive economy. At present, training financed by an employer that is related to the employee'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 for future employment elsewhere may find that the cost of this is not allowable against tax, and the employee may find that he has received a taxable benefit. I propose to remove both these obstacles. This should help more workers to acquire new skills for new jobs.

E23. The past few years have seen a remarkable and 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.

E24. 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.

E25. 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.

E26. 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.

E27. 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 £ $\frac{1}{4}$ million is considerably greater than the £100,000 suggested in the consultative document.

E28. 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.

E29. Third, the period within which businesses must apply to be registered for VAT will be extended from ten to thirty days.

E30. 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.

E31. 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.

E32. In addition, I propose to increase the VAT threshold to £21,300, to keep it at the maximum permitted under existing European Community law.

E33. 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.

E34. 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.

E35. In any ongoing programme of tax reduction and reform, where much still remains to be done, an essential element 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 that end.

E36. 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 proposed 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 will be some £300 million in 1987-88 and £400 million in 1988-89.

E37. 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.

E38. 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.

E39. 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.

E40 Fifth, I 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.

E41. I have one further proposal to make in the broad field of the taxation of business and enterprise.

E42. In my Budget last year I suggested the possibility of introducing a measure of tax relief for profit-related pay.

E43. 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.

E44. 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.

E45. 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, as take-up grows, and as the proportion of an employee's pay which is profit-related rises.

E46. 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.

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, ⁵⁰ 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, ¹⁰⁰ 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 ¹⁵⁰ of households now own their own homes, 2½ million more than in 1979. However, there have been 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 ⁵⁰ 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 ¹⁰⁰ 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 ¹⁵⁰ 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 at the beginning of next year, three months earlier than planned.

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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 present⁵⁰ 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.¹⁰⁰ These were duly published in a consultative document 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 be¹⁵⁰ 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.

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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, being¹⁰⁰ restricted to plans within their employer's schemes. They will be able to top their pensions 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 contributions¹⁵⁰ 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 freedom²⁰⁰ 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.

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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 ⁵⁰ 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 ¹⁰⁰ 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 tax-exempt life assurance limit based on the sum assured with a new limit based on annual premiums. I propose to ¹⁵⁰ 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.

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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, which⁵⁰ 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 benefit¹⁰⁰ to family businesses and to heritage properties, both of which are often held in trust.

F19. I also propose to make two minor changes affecting business assets. First, holdings in companies quoted on the unlisted securities market will henceforth be treated for Inheritance Tax purposes in precisely the same way¹⁵⁰ 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

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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 remain⁵⁰ conscious that it did little to help the smallest taxable estates, where the family home is often the principal 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. 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 three times the yield of Capital Transfer Tax in 1978-79, an increase in real terms of almost 50 per cent.

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F23. It is the same story with the other capital taxes. Since we first entered office, their severity has been significantly eased. And over the same period the yield of Capital Gains Tax has risen in real terms by 80 per cent and that of Stamp Duty by 140 per cent.

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CONQUEROR

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 am sure that this measure will be welcomed by 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 undertook to introduce a tax differential in favour of unleaded petrol, to offset its higher production cost. I can now announce that the differential will be fivepence 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. In my 1985 Budget I announced the first stage in the process of increasing the rates of Vehicle Excise Duty on farmers' heavy lorries to bring them into line with the use they make of the public roads. I introduced the second stage in last year's Budget and propose to complete the process this

year. 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.

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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 better economic performance. And 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. And 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 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 important for future growth and jobs.

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

H14. The total cost of all the measures in this year's Budget, again on an indexed basis, is a little over £2½ billion.

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J. CONCLUSION

J1. Mr Deputy Speaker, in this Budget I have reaffirmed the prudent policies which, despite a year-long coal strike followed by a collapse in the oil price, have given us the strongest economy we have known since the War.

J2. After an Autumn Statement which increased public spending in priority areas, I have once again cut the basic rate of income tax; a cut which the Party opposite are pledged to reverse, if they are given the chance - which they will not be. And I have done this while sharply reducing public borrowing; a combination that has eluded successive Governments for decades. This is a Budget built on success, and a Budget for success. I commend it to the House.

SAM BRITTAN - COMMENTS ON CHANCELLOR (EXTRACT)

Manuscript from: BBC Radio 4, Today, 17 March 1987

INTERVIEWER: (Peter Day) It's Mr Lawson's fourth Budget. Four Budgets is oftenthe allotted span for a Chancellor in office. By what criteria does one assess a Chancellor - Samuel Brittan, friend of Mr Lawson and influential economic commentator on the Financial Times.

BRITTAN: How far he has stood up to the Prime Minister, how far he has stood up to the prejudices of his own Party and how far he has provided an environment in which the rest of us can get on with our affairs.

INTERVIEWER: Mr Brittan thinks the economy is in fair shape, but to what extent is that due to Mr Lawson?

BRITTAN: Government has much less to do with the performance of the economy than people realise. I think his main contribution has been his handling of a fall in the oil price which has not produced the doom which people who thought Britain was largely an oil economy thought it would bring. And his handling of interest rate and exchange rate policy has been quite subtle. But I don't think, and I don't think hethinks, that Chancellors produce miracles.

LBC: tel 353 1010:@

CHIEF SECRETARY - INTERVIEW ON BUDGET ✓

PPs Chancellor
12/12

Transcript from: BBC 1 tv, Breakfast TV, 18 March 1987

INTERVIEWER: (.....) Mr Macgregor, don't you care about the unemployed, why haven't you done more for them?

CHIEF SEC: Of course we do. And can I just make two points. I saw Peter Webber just before the news talking about employment schemes. Perh. Peter doesn't realise that employment schemes come through in the expenditure plans which we announced earlier for next year. And there we are spending another £4 3/4 billion including on infrastructure, including on housing, including on school buildings. All things that those people were asking for. And including £3 billion on employment and training measures. Now that's one point. The other point is that the Budget's about dealing with taxes and all the other things in the economy. And I think it's very interesting that the CBI have said that this Budget is just what industry wanted, just what the CBI wanted, it was good for business and good for jobs. And that's right.

INTERVIEWER: We also saw in Leicester there an unemployed man who's precisely 45pence a week better off. As he put it, not even enough for a return bus fare to the Job Centre.

CHIEF SEC: Yes but the Budget is about taxes, it's not about expenditure plans which comes at another time. And inevitably people who are not paying much tax will not gain a great deal of benefit from a reduction in taxes. But I mean Shirley Green you see, for example, was talking about not enough off as she saw it. In fact if you look at the Opposition plans both Labour and SDP, look at what they're saying about what they'd do. They'd massively put taxes up.

INTERVIEWER: They did that,

CHIEF SEC: In fact all the sort of people who I believe are still

having too much taken out of their pay packets in tax and national insurance contributions would find them massively going up under the policies of the Opposition parties.

INTERVIEWER: But you've been promising a 25 p in the £ rate of income tax for several years now. If you can't do it now when can you do it?

CHIEF SEC: We're doing pretty well. We've got it down from 33p to 27p and we made quite clear what our target is. But the important point also I think is that this is a prudent Budget because we have a strong economy now, now strong finances, we don't want to throw that away as used to be done in the past. And that's the best guarantee for jobs I may say.

INTERVIEWER: But manufacturing output in this country is lower now than it was in 1979?

CHIEF SEC: We went through a very severe recession, a world recession from 79 to 81. Since 1983, the last election, manufacturing output, manufacturing investment, manufacturing exports are all heavily up.

INTERVIEWER: They're lower now than they were in 1979?

CHIEF SEC: But that was because of the heavy world recession. and I think that is in fact why the CBI have given this Budget such a welcome. And of course the other very important point is interest rates. It affects businesses very substantially, it affects householders through their mortgage. Now I don't know what the City will do today. But so far the reactions have been very favourable. One paper described the City's reaction as admirably prudent and confidence building. That leads to reduced interest rates that undoubtedly means very good for jobs and very good for householders.

INTERVIEWER: One does also hear businessmen saying though that the strong £, and we've seen it now at a record high last night, the record for 5 years, that that actually makes exporting much much more difficult?

CHIEF SEC: But in fact the position on sterling has been very favourable for industry as the CBI themselves say. I mean the position in relation to the deutchmark gives us tremendous export opportunities which our businesses are now picking up. But I think the really important point also is that if you look at what the opposition are actually saying they will just spend more borrow more. That would put interest rates up. That's not in the interest of business. It's not in the interest of jobs nor is it in the interest of families with mortggages.

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FINANCIAL SECRETARY - INTERVIEW ON BUDGET

Transcript from: BBC Radio 4, World Tonight, 17 March 1987

INTERVIEWER: (Sally hardcastle) Economic observers in the City used another description which was reiterated by Norman Lamont, Financial Secretary to the Treasury, when he defended the Budget's financial wisdom.

FST: It's a prudent Budget. But I think in a way it is spectacular. Because what the Chancellor has done is to deliver a hat-trick of the kind we haven't had in this country for many years. We've reduced taxes, we've reduced borrowing in a spectacular way and we have also put up public spending by £4 3/4 billion in the Autumn Statement. That was a far bigger figure than the cuts in income tax. So that's a remarkable triple achievement.

INTERVIEWER: There does seem to be some feeling that the Chancellor could have responded rather more to Back Bench pressure for more action to produce jobs?

FST: We've made it clear for a long time that we don't think public spending is the way to create jobs. That just gives a short-lived boost to employment and then the problems come later. The real way to create jobs is to have a fast-growing economy. That's what we've had for the last few years. We've had the fastest growing economy in Europe. Something that is quite new for this country. What the Chancellor has tried to create is the conditions in which that can continue. And I think it will continue. The forecast is that the economy will grow by about 3% this year. That should mean that we will continue to see something of the favourable trend in unemployment that there's been in the recent past.

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Andrew
PWP

Summary of Revenue Points

Col942 Mr Roy Hattersley (La)

Nothing for pensioners without second income, poor families or unemployed.

943 Mr Eric Forth (C)

Low interest rates help business and create employment.

Mr Hattersley

Tax cuts do not. Paying for unemployment not prudent.

944

Income tax cuts not sustainable. Bad for balance of payments, credit boom. VAT will go up.

945

False accounting for privatisation.

946

Corporation tax revenues a result of tax disincentive to investment.Stamp duty receipts a result of house prices and merger mania. VAT receipts on imports. Household debt. Balance of payments. Oil revenues.

947

Welcomed - unleaded petrol
- concessions for charities
- over 80s allowance
- blind allowance
- tax relief for training

948

Exchange controls. Welcomed dropping M3.
Welcomed - VAT admin changes
- Labour proposed them last year.
Growth rate. Inflation rate.

949

Tax on low paid increased. Should have reduced rate band increased allowances or NIC cut. Only richest 5% have gained. Nurses prefer spending on health. Stirling research on incentives.

950

City salaries. BIM prefers public spending.

- 951 Labour's employment strategy.
- 952 Labour's fiscal plans.
Private borrowing, public borrowing and interest rates.
- 953 Compared 2p cut with help for pensioners.
Criticised IHT cut. Raise Child Benefit.
- 954 Labour's plans on Child Benefit, pensions, supplementary benefit.
- 955 Mr John MacGregor (CST) Hat trick on spending, tax and PSBR. Steady growth.
- 956 Mr Jack Straw (La) Manufacturing output and investment down.
- Mr MacGregor Corporation tax revenues. US emulating low CT rate.
Productivity up. Investment rising. Evidence on exports from CBI, ABCC, EEF.
Overseas assets.
- 957
- 958 Mr Kenneth Carlisle (C) Tax cuts sustainable.
Labour's income tax plans
- 959 Mr MacGregor Public expenditure - health, training, law and order.
PSBR prudent.
- 960 Tax cuts good for incentives.
Allowances vs rates. Allowances up 22%. Marginal rate crucial, also for self-employed. Higher rate taxpayers get limited benefit.
Top rates must come down.
Reduced rate band no good.
- 961 Take-home pay up. Wage increases also bad for imports.
PRP good for efficiency.
- 962 Small business package:
- small business CT rate.
- BES improvements.
- VAT admin changes not as Opposition suggested.
- 963 Home ownership, share ownership
IHT changes help transfer of family home.
Pensions package increases choice

- 964 and mobility. Abolition of IIS and tax cuts help pensioners on savings income. Labour's spending pledges.
- 965 Mr Roy Jenkins (SDP) Criticised - 2p off basic rate
- PSBR cut
- 966 Investment would be better for jobs.
- 967 SDP will not reverse 2p cut.
- 968 Cut interest rates by joining EMS.
Tax cuts have widened gap between rich and poor.
- 969 Sir Peter Hordern (C)
Mr Jenkins How would SDP repatriate assets?
It is automatic.
- 970 Sir Peter Hordern SDP incomes policy?
- 971 Welcomed - PSBR cut.
- Freeze in limit for mortgage interest relief.
City contributes to rising invisible earnings.
Welcomed low CT rate.
- 972 Tax structure must reflect social
973 trends. Reduce top rates.
Abolish relief for pensions contributions and mortgage interest to widen tax base.
- 974 Mr Sean Hughes (La) Nothing for unemployment.
- 976 Mr John Butterfill (C) Welcomed - VAT on foreign tours.
- CT reforms.
- BES reforms.
- Tax relief for training.
PRT reliefs also welcome in Dorset.
- 977 Welcomed - VAT admin changes.
- Personal pension tax reliefs.
- IHT changes.
VAT reliefs for drugs should extend to veterinary medicine.
Welcomed - non-indexation of higher rate thresholds

- 978 - over 80s allowance,
- blind allowance.
- 979 Dr Oonagh McDonald (La) UK share of world exports,
deficit on invisible earnings.
- 980 Mr Butterfill Export patterns change in
response to developing countries.
Look at overall trade including
invisibles.
PSBR important.
- 981 Mr Willie Hamilton (La) U-turn in public expenditure
inadequate.
- 982 Government statistics selective.
Unemployment, low wage
exploitation.
- 983 Attacked privatisation.
Tax and PSBR cuts a wasted
opportunity to create jobs,
repair schools.
- 984 Attacked rise in prescription
charges.
- 985 Mr James Hill (C) PRT reliefs will create oil jobs
on South coast.
- 986 Welcomed - VAT admin changes
- blind allowance
- unleaded petrol
- IHT threshold changes
- tax relief for
training.
Criticised effect of VAT on free
ports.
Welcomed likely cut in interest
rates - good for home owners.
- 988 Mr Terry Fields (La) Budget for rich, not for poor or
989 unemployed. Criticised state of
health service.
VAT receipts financed by credit
boom and bogus mortgages.
- 990 Disagreed with Labour front bench
about tax cuts and the low paid.
- 991 Decline in investment and
manufacturing output.
- 993 Mr Charles Morrison (C) Tax and expenditure mix about
right.
Welcomed over 80s allowance

Wanted - blind allowance
 - cut in NIC
 - low earnings benefit to encourage part-time work.

Welcomed - VAT changes.
 - CGT retirement relief increase.
 - IHT business relief.

All good for small business.
 Disappointed no 100% capital allowances on plant/machinery for unincorporated businesses.
 Welcomed likely cut in interest rates.
 More action needed to stimulate manufacturing industry - infrastructure schemes.

995 PSBR could be higher.
 Welcomed betting tax changes.

996 Mr Richard Caborn (La) Budget welcomed by City, not by industrialists.

999 Government hindering schemes for loans to small business.
Mr Graham Bright (C) Welcomed cut in PSBR - good for business.

1000 Investment in small firms better for jobs than investment in large firms.
 Welcomed - VAT admin changes.
 - cut in small firms CT rate

Wanted - CT rollover arrangements for small firms.
 - Cut in 10% special car tax.

Welcomed - PRP
 - simplified pension schemes for small firms
 - IHT threshold increase good for family business
 - IHT business relief

1001 Mr Conal Gregory (C) Welcomed - PRP

1002 - 2p off basic rate
 - over 80s allowance
 - blind allowance

Wanted - abolition of double mortgage relief for unmarried couples
 - mortgage relief limited to standard rate

- rise in NIC thresholds
 - integration of NIC and income tax administration
 - CGT tax credits for art treasures.
- 1003
- lower excise for low-alcohol drinks.
- Low exchange rate good for exports. Good record on infrastructure.
- Dr Oonagh McDonald (La)
- 1006
- PSBR cut unnecessary. Government will have to curb consumer credit.
- More investment in manufacturing industry needed.
- Tax burden on low-paid not reduced.
- Higher allowances would be better than cut in basic rate. Benefits only to rich.
- 1007
- Nothing for part-time workers, mostly women.
- No mention of independent taxation for women.
- Tiny increase in Child Benefit. Wanted age allowance for women aged 60-64.
- Welcomed over 80s allowance but pensioners still paying more tax.
- 1008
- Mr Norman Lamont (FST)
- Domestic rates increase due to cuts in Government grant.
- VAT will go up.
- Opposition ignored judgement of CBI and City. Accusations of bribes and over-prudent PSBR inconsistent.
- 1009
- Alliance tax-based incomes policy bureaucratic and unworkable.
- Alliance fudge on income tax cuts.
- 1010
- Public expenditure increased.
- CT revenues come from increased productivity and profitability.
- 1011
- Increased share ownership, more privatisation plans. Sell off BP stake.

1012

BES and ship chartering - IR consulting GCBS.
Transferable allowances - insufficient support, looking for halfway house.
Distribution of tax cuts.
All taxpayers have gained.

1013 Mr Buchan (La)
Dr McDonald
Mr Lamont

What about VAT?
Use of average figures misleading.
Pension measures good for job mobility.

1014

PRT: cross-field allowance and research relief helpful additions to accelerated APRT repayment.
Budget will continue favourable employment trend. Labour ignores service sector.

Debate adjourned



Given the long agenda, I don't think you need do more than run through Table 1 to confirm that these are the presumptions.

NB The positive total depends on - 25% increase in car sales
- raising car tax for gas guzzlers

The main discussion would then focus on excise duties etc on the specific papers below.