

PO-CH / NL / 0279

PART A

Part A

CONFIDENTIAL
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MANAGEMENT - IN - CONFIDENCE

Begins: 1/5/87
Ends: 8/10/87


PO -CH /NL/0279

PART A

Chancellor's (Lawson) Papers:

INLAND REVENUE AND
CUSTOMS AND EXCISE 1987
- 1988 PUBLIC
EXPENDITURE SURVEY BIDS

PO -CH /NL/0279
PART A

Disposal Directions: 25 Years

D. Anderson

11/10/95

CONFIDENTIAL



FROM: A W KUCZYS
DATE: 1 MAY 1987

CHANCELLOR

INLAND REVENUE: 1987-88 RUNNING COST PROVISION

I am sorry you have been landed with this discussion with the Chief Secretary and the Financial Secretary at 8.30 on Tuesday morning. You will remember the problem: this was set out in Tony Battishill's minute of 6 April. You commented at the time:

"Something will have to be done. After Financial Secretary has thoroughly gone through this with Mr Battishill, he will wish to discuss with Chief Secretary."

The Financial Secretary has now gone through the first part of this process: there is a note of his meeting with Tony Battishill on the folder below. But it is unlikely that he and the Chief Secretary will be able to reach agreement without your getting involved. Apart from anything else, they are getting conflicting advice: ~~GE~~ advising the Chief Secretary to take a very hard line; FP and the Financial Secretary being more sympathetic to the Revenue.

All this is summarised in Michael Scholar's note below.* Michael felt very strongly that a discussion between you, the Chief Secretary and the Financial Secretary was needed. Although I have not invited Treasury or Revenue officials, they will have had a meeting immediately beforehand with the Financial Secretary and will be available if you want to call them in.

The urgency of all this is that Tony Battishill appears before PAC on Wednesday. The Financial Secretary is seeing him again mid-morning on Tuesday, to convey Treasury Ministers' decision. We really need to have this settled by then.

AWK
A W KUCZYS

*and now FERB's comments too



Chancellor.

I am sending this to the
Chief Secretary now: to
the FST on his return:
the other copies to wait
until after the holidays

[Signature]

4.8.87

*AA
Psr
file
for classification*



Alex.

IR P.B.

I had a word with JKR - it
emerged that our "problem" about
handling had ceased to exist.
Hence no note to Ch. However
he may like to have a word
with CST nonetheless (see
my pencilled ms. note, below)

[Signature]

*(it pairs)
with the CST
minutes*

*I did not
think this
was worth
back for
a post, & have
discussed
with CST.
I think,*

*constr. to next
stop
for
discuss
that
proposed*

From A M W BATTISHILL



THE BOARD ROOM
INLAND REVENUE
SOMERSET HOUSE

*1. See to
renew grant
No provision chry...
No realisation of the...
low of the...
costs to IR low
put in for 1988-89
in the last PDS
check (PDR)*

29 June 1987

1. FINANCIAL SECRETARY TO THE TREASURY

2. CHIEF SECRETARY TO THE TREASURY

*They have now gone
to the other side - if you
may wish to (with a
small radical
change to the way
the system of
work...)*

PUBLIC EXPENDITURE : INLAND REVENUE BIDS

I enclose a memorandum in support of the additional bids I need to ask you to consider for the Inland Revenue. It includes the usual summary tables and a separate note on manpower.

Size of bids

2. Altogether I must ask for an additional £m82.3 for 1988/89. This represents £m85.6 for running costs, £m3 for capital; offset by an increase of £m6.3 in forecast appropriations in aid. This represents an increase of

cc Chancellor of the Exchequer
Paymaster General
Economic Secretary
Sir Peter Middleton
Mr Butler
Mr Scholar

Chairman
Mr Isaac
Mr Painter
Mr Rogers
Mr Crawley
Mr Cherry
Mr Matheson
Mr Beighton

BATTISHILL
TO
CST
29/6

10.7 per cent on our 1987/88 provision, with substantially smaller increases for the two later years of the survey period.

3. There is also a bid of £m40 for 1988/89 for the public expenditure element of mortgage interest relief at source (MIRAS) and life- assurance premium relief (LAPR) for recipients not liable to income tax: this is a separate vote for which we are responsible, but which is wholly outside the Revenue's control.

4. The formally recorded increase in our running costs next year is just over 12 per cent. But that is on the basis of comparison with the current year's provision which is inadequate to meet our known pay costs for the year, even after interim measures agreed with the Financial Secretary before the Election. Ministers recognised earlier this year that we were facing real difficulties on the basis of our current 1987/88 provision, but authorised us to issue internal budgets consistent with existing plans. We are due to consider the funding problem again with Ministers in the autumn.

5. On the basis of a realistic provision for the current year, the increase in next year's running costs comes to under 11 per cent if our additional bids are met in full.

6. This would come down to a little over 10 per cent if one excludes the bid we have been obliged to make for the Government Data Network project. This project, if it goes forward, will be to the general benefit of Government Departments in the medium term. But, at least in the short term, it may prove more expensive for the Revenue than continuing to develop our own network.

7. Nevertheless, I recognise that these are substantial figures for one of the Chancellor's own Departments. They have been arrived at only after the most careful scrutiny by the Board who have already cut back on bids made within the Department by a very substantial amount. Over much of the field the pressures on our financial needs are externally generated and beyond our direct control.

Reasons for bids

8. There are four main reasons why, on present policies, running costs will exceed our baseline next year.

9. First, and predominantly, pay. The allowance for pay next year is demonstrably not enough to cover our agreed numbers on any conceivable central pay settlement even before Ministers consider whether those numbers should be increased. Partly, this reflects the identified shortfall in our pay provision this year and last. If left uncorrected, this shortfall will carry through into next year and beyond. And it will be aggravated by the phased nature of this year's settlements which are expected to cost us a full 1 per cent more next year than this. Partly, it reflects our best assessment of how next year's pay round will go - both the level for Civil Service pay generally, and the special pay consequences for the Revenue from the various understanding reached with the IRSF in the negotiations on this year's pay round. We have assumed that the basic offers for the Civil Service next year will be 4.5 per cent, a shade above the forecast RPI.

10. Second, we need more manpower to keep up with the relentless increase in work beyond any conceivable improvements in productivity, and to deal with acknowledged

levels of inexperience from consistently high turnover (particularly in London and the South East) and with inadequate supervision in local offices. These were both identified by the work measurement exercise completed last year; some aspects of this have already been discussed with the Treasury. And our Departmental unions have given notice of an intensive campaign to increase manpower.

11. I believe we are in danger of a vicious circle here - and one which the unions will try to exploit. Staff shortages and high turnover depress staff morale, people leave in large numbers, the level of experience drops, and those left behind find it even more difficult to cope. Our manpower bids are intended to keep up with rising work and do something to break into this inexperience factor.

12. Third, accommodation. We are not planning for any volume increase. On the contrary, we have set ourselves a 1 per cent space reduction target. This is recognised to be ambitious on top of the major local office rationalisation programme of the last three years. And we have recently taken decisions to move some hundreds of key staff out of London to save money. Our bids are almost wholly due to our best estimates of increases in rents, rates and PSA charges over which we have no effective control.

13. Fourth, implementation of our computer plans. These plans are at the heart both of our improving efficiency and major staff savings over the next few years. But the short-term, costs of installation, maintenance and staff preparation and training are always going to be high. For various reasons, including some change in the phased delivery of savings, we need to devote more money to this

over the survey period if the savings are to mature on schedule.

Independent taxation

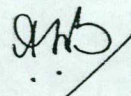
14. The bids contain nothing for the costs of introducing independent taxation of husband and wife on which we shall be letting Ministers have a paper shortly. One of the options it will discuss is a 1990 start date. If Ministers decide to go ahead on that basis, it will be necessary to seek additional funds and manpower for this purpose in 1988/89 and later years. But it will also reinforce our bids for extra resources to deal with the existing work of the Department and its projected growth, particularly for 1988/89. The workstate at the beginning of 1989/90 will be a critical factor in ensuring the successful introduction of a new scheme for married couples on such a very tight timetable. If we are to be in a satisfactory position to take on the work, we must have adequate funding throughout next year.

Conclusions

15. Despite these bids, I believe the Revenue gives good value for money. Since 1979 we have reduced our staff by 16,000. Our local office networks are achieving very real improvements in productivity. We are within sight of installing the largest clerical computer system of its kind in Western Europe on time and without the major cost overrun some people had predicted would occur. And we seem on published figures to be the Department with the lowest running costs per head in Whitehall - and below, by a significant margin, other large Departments which operate through local office networks.

16. What we cannot do is control the external environment. Staff must be paid the rates they have been awarded - whether or not the budget allows for that. Numbers of taxpayers, the levels of thresholds, frequency of assessments, growth in stamp duty transactions, and so on rightly depend on political decisions. And we must always be ready to cope with changes arising from the Budget each year. Finally, there are economic and social changes, like the growth in self-employment and employment, and a greater readiness by some taxpayers to leave tax unpaid, which also increase the Revenue's work. We need adequate resources if we are to cope.

18. No doubt you will want us to work through the figures with Treasury officials. When that has been done, I am at your or the Financial Secretary's disposal if you would like to discuss.



(A M W BATTISHILL)

CUSTOMS
PES

CONFIDENTIAL



Board Room
H M Customs and Excise
King's Beam House
Mark Lane London EC3R 7HE

FROM: A M FRASER
DATE: 2 JULY 1987

CHIEF SECRETARY

cc: Chancellor of
the Exchequer
Paymaster
General
Sir P Middleton
Mr F E R Butler
Mr Anson
Mr Scholar
Miss Sinclair

(Some of the PLS, (some) are given)

PES 87 : CUSTOMS AND EXCISE ADDITIONAL BIDS

1. In accordance with the PES guidelines, I send details of the Customs and Excise additional bids for the period 1988-89 to 1990-91. They are summarised in a series of tables at the end of this minute:

Annex A sets out the additional cash bids

Annex B shows the additions we are seeking to manpower numbers

Annex C sets out the efficiency savings which we have built into our manpower bid

Annex D comprises a series of graphs relating outputs to inputs over time for each of our priority areas, comparing the baseline position with the bid-for resources.

Detailed supporting material is being sent to official Treasury.

2. **Background.** It may be helpful to give you the briefest resume of our chief aims and of our approach to achieving them efficiently and effectively. The Department's forward strategy is set out in Section 2 of our Management Plan for the current year, which was agreed with Treasury Ministers (copy attached). Our top priorities for the period are:

to maintain and enhance the effective collection of VAT and the very high yielding excise duties; and to increase our effectiveness in investigating and preventing drug smuggling.

3. On VAT control, we have demonstrated in recent years that by careful targeting of resources we can reap a revenue benefit quite disproportionate to the cost of those resources, thereby increasing the yield of the tax with no change to either rate or coverage. The average direct cost/yield ratio of control visits, now improved to about 1:8, is undoubtedly good value for money - and is at least doubled when the preventive effect is taken into account. We aim to do still better.
4. On drugs, the Department is, by virtue of our role at points of entry into the UK, in the front line of the Government's fight against drug trafficking; over 90% of drugs seizures are normally made by Customs and Excise. We are pursuing a six-point strategy approved by Ministers and we have devised some useful indicators of our effectiveness. The workload in this politically sensitive area is increasing in both amount and complexity, and it is resource-intensive.
5. We shall continue to carry out work on these priorities, as on all our tasks, setting challenging targets for improving both efficiency and value for money. Since staff costs account for over two-thirds of our total expenditure, we pay particular attention to staff numbers. Our manpower bid for

the PES period takes account of stringent productivity savings in all areas of the Department's work : as a result it is some 1200 less than it otherwise would have been. Together with nearly 600 savings already counted in the baseline, efficiency improvement amounts to the equivalent of about 7% of our present complement. We also pay close attention to value for money across the board : all our targets are set with this precept in mind. Earlier this year the Paymaster General and I gave a seminar on the subject for the Prime Minister, at which I reported both our considerable progress and achievement to date and our commitment to the future. You may be interested to see the attached copy of the note of the seminar.

6. In the light of this commitment we welcome the Survey's increasing emphasis on relating inputs to outputs. As far as inputs are concerned, the resource position of the Department continues to be influenced by long-term environmental factors : first, the continuing growth in VAT and customs work : and secondly, the increasing complexity of the work with, in particular, the increasingly sophisticated methods used in drugs smuggling and tax evasion and avoidance. In Annex D to this submission you will find output tables and efficiency indicators in graph form for our main functions, showing that the investment of additional resources would provide more than commensurate outputs. On the other hand, a restriction to the baseline would undoubtedly set the advances we have made in recent years into reverse and result in lower targets for both drugs seizures and VAT yield. More detailed tables have been sent to official Treasury.
7. I will illustrate these points later on, but it might be helpful if I present our bids in three parts : those needed to keep our main controls at their existing standards and levels of effectiveness; those needed to deal with new functions or activities laid on the Department; and those required to support particularly cost-effective measures to enhance drugs preventive work and VAT control work in the light of the trends mentioned above.

8. **Maintaining existing standards.** This accounts for the great bulk of the additional running costs bid - approximately £30 million out of £32.5 million in 1988-89. There are five main elements : sharpening VAT control skills, pay, accommodation, extra manpower at ports and airports for essential controls primarily against drugs smuggling, and certain legal and other expenses associated directly with the investigation and prosecution of drugs smuggling and VAT fraud cases.
9. **VAT control skills.** Our thinking has been greatly influenced by the report of an efficiency scrutiny on the effectiveness of VAT control work, which we have just published with the approval of the Paymaster General and Sir Robin Ibbs, and by the emerging findings of a scrutiny on the problems of attracting the right quality of staff to work in London. We had considered whether to log this bid under 'enhancements', but in our view it is central to the question of maintaining existing standards : the fact that there would also be substantial additional revenue in later years is a bonus.
10. We have successively set and achieved very stretching value for money targets for our VAT control effort. We have a good deal further to go but we now consider that a marked increase in the skill and experience of our VAT control staff will be necessary not only to achieve extra potential revenue but, more immediately, to secure all the revenue which we are currently getting in. Figures 3.1 and 3.2 of Annex D illustrate the point : you will see that the cost yield ratio from VAT control work has increased steadily over the years but we now see it flattening out in the later PES years unless we invest in training and make efforts to retain experienced staff. If we hold to the baseline the very best we could do would be to maintain the cost yield ratio.
11. In fact we see considerable danger of a decline, perversely because of the success of the Keith 'package' of enforcement measures to improve compliance. These have had, and should continue to have, a markedly beneficial effect on the cash-flow to the Exchequer, amounting to hundreds of

£ millions. But there has been a commensurate heightening of the VAT profile among the traders which we have to control, amounting to a greatly changed climate in which we must operate. This is exemplified by the increase in professional skills and advice offered by the accountancy profession, which carries with it the real threat of increased sophistication in tax accounting and the falling away of compliance as the 1990s approach. I have little doubt that, if we were unable to respond to this threat, we should actually start to lose revenue : we estimate of the order of £40 million per annum in the first instance in 1990-91 but potentially very much more in subsequent years. We therefore regard it as imperative that we take the sort of steps identified by the scrutineer to safeguard this revenue. But more immediately we would expect that the illustrative package which he proposes would bring in direct extra revenue of £50 million - at least seven times the initial investment - in the first year, arising from more effectiveness, and increasing in subsequent years.

12. **Pay.** We estimate that in 1988-89 the actual cost of salaries and overtime to cover the numbers and grading of staff and the amount of overtime assumed in the baseline will be £17 million more than has been allowed for in the baseline. In last year's PES it was in the end assumed that the total cost of this year's pay agreement would be 4.5 per cent, despite a higher opening assumption. In fact, the effect of the current offer made by the Treasury is more likely to be at least 6.5 per cent in 1988-89. No realistic estimate of next year's pay settlement was made in our PES last year and the standard Treasury inflator of 2.5 per cent was used. I believe that a credible assumption cannot be less than a full year on year additional cost of 6 per cent.

13. I make two observations on these pay figures. First, I recognise that there will be arguments for absorbing the impact of this year's pay settlement not covered in the baseline in future years. That would amount to our finding savings worth some £6 million. I can give you an absolute

assurance that not only shall we be absorbing that sum by offsetting efficiency improvements but we shall be going even further. Annex C to this submission sets out our (ambitious) efficiency savings for the PES period : at the most conservative estimate we calculate that these represent for 1988-89 a saving of £9 million in salaries. We have reduced our bid accordingly to take account of these savings. If you found it presentationally preferable, we could make our manpower bid gross and subsequently offset the necessary savings against the costs incurred by the pay award. The key point however is that I do not believe that there is any scope for further absorption of the totality of the bids I am now presenting by yet more efficiency gains.

14. Second, I believe that a pay assumption for next year of 6 per cent is the best assessment we can make at this stage. In PES 85 we originally proposed a pay assumption of 7 per cent and accepted 5 per cent : the outcome was a full year on year cost of about 7 per cent. In PES 86, we originally proposed 6 per cent and eventually accepted 4 1/2 per cent : as I have mentioned, the final outcome for this Department will be at the very least a year on year increase of 6 1/2 per cent. Given the competitive pressures which are becoming more acute, especially for our experienced staff in priority areas, I think it most unlikely that, whatever the level of the basic pay settlement in 1988, the total cost will be less than 6 per cent, taking into account special allowances and any restructuring.
15. **Accommodation.** In accordance with the recommendations of the multi-departmental review on accommodation, we have been setting ourselves challenging targets on the more efficient use of our accommodation. We have reduced the average amount of space per member of staff from 16.3 sq metres in 1983-84 to 15.6 sq metres in 1986-87 and we have a target to reduce it to 15 sq metres by 1990. Although comparisons are difficult, it would appear from PSA information that our space standards are more tightly drawn than for other departments with networks of offices; and it is interesting to note that the PSA's own advisory standard for accommodation is 18.6 sq metres per person.

16. The reason for the additional bid for accommodation does not therefore arise from any relaxation in our efforts to use space as efficiently as possible - the target of 15 sq metres by 1990 is exerting a tremendous downward pressure. It results from the combined effect of three factors - the move under PRS to charging on the basis of current market rental for individual buildings; the particularly rapid increase in market rentals in the London area; and our sharp increase in operational work in the London area, especially on VAT and on drugs investigation. We have sent our detailed analysis of these trends, supported by information from PSA, to official Treasury, but two examples may help to illustrate the situation. The VAT office in the City of London which is expanding to deal with the rapid increase in VAT control work has had to be transferred to larger premises. The current PRS charges are £480k per annum : next year they will be £1.2 million. The lease on the main building used by our Investigation Division runs out in 1988 and new, larger premises will be needed to cope with increased manpower mainly to deal with drugs work. The current PRS charges are £1.95 million per annum : in 1989-90 they will be £4.1 million.
17. Controls at ports and airports. In last year's PES round, at the Chancellor's request, we withdrew a bid for additional staff to handle controls over both passenger and freight at ports and airports in 1988-89 and in 1989-90 on the basis that the requirements could be looked at in this round in the light of up to date assessments of traffic flows and risks. The bid which we now make reflects such an assessment built on more sophisticated analyses by our operational research and investigation specialists. In making our assessment of manpower needs I underline three important points.
18. The first is that the bid is fully in line with Point 1 of the Department's six-point strategy (published in the Government's strategy "Tackling Drug Misuse"), viz that routine controls will be maintained in line with increasing

traffic. The second is that a large proportion of the bid is required quite specifically to man new controls which are firmly planned - for example, at Stansted, Gatwick and Luton. We simply have no option on these. Thirdly, we have set our bid at the level which we consider will enable us to secure the optimum level of efficiency, taking the fullest possible account of further efficiency improvements and economies of scale. But the corollary of this is that if our bids are not met, inefficiency will increase : staff will become overwhelmed; they will make more errors; backlogs will build up; or controls will have to be reduced. Examples of this "overwhelming" effect show that on the freight side it actually means that a smaller number of entries is dealt with per person. As a consequence, the outcome is either sharply to lower standards - in effect, to let through many entries without any control whatsoever - or to create extensive delays in clearance which will soon become unacceptable. A similar situation will arise on passenger control, although in this case there is no scope for backlogs to build up, because ports and airports would almost immediately become jammed : the result therefore would be reduced control. The effect can be seen in figures 2.1 and 2.2 of Annex D : purely in statistical terms the impact on drugs seizures is significant but it will be substantially worse if the result were to impact on morale and push the efforts of Customs Officers into a downward spiral.

19. Legal and other expenses of investigation and prosecution. The main reason for this bid is our underestimation in the past of the costs of our own success in increasing the number of investigations and subsequent prosecutions for both drugs offences and VAT fraud. The sharp increase in cases handled was a major factor in our supplementary estimate last year. It is now clear that the rate of increase in this work over the next few years is likely to continue to be considerably higher than that assumed in the baseline. The amount also includes £500k for witnesses' expenses which were formerly paid for by the Lord Chancellor's Department but have been transferred to this Department without any appropriate PES transfer.

20. New functions and activities laid on Department. In line with our policy of keeping a very tight grip on administration (we expect our ratio of administrative manpower to operational manpower to continue to drop throughout the PES period - see Fig 4.1 in Annex D) we have been extremely stringent in absorbing a good number of additional pressures. These are illustrated in Annex C in the efficiency savings we have targeted for ourselves. In the VAT area the resources needed to handle cash accounting and annual accounting will be more than offset in 1988-89 by the savings from the deferment of Keith III and the consequent net saving helps to absorb some of the new initiatives in other fields. After also projecting other productivity and efficiency savings we will need provision for additional work on the Drugs Trafficking Offences Act (new work on the smaller cases not exceeding £50k which are expected to yield at least £3 million in a full year) and on the Criminal Justice Bill for dealing with extended custody of persons suspected of concealing drugs internally and for investigating the assets of offenders other than drug smugglers. 25 staff in 1988-89 are the minimum required to deal with work arising from the Data Protection Act, changes in Civil Service Pension Scheme and some untying from the PSA.

21. I should add that we are under constant threat of having to take on new work in the customs area to deal with additional restrictions on certain imports and exports. Possible countervailing measures against Japanese protectionism have been mooted, as too has the extension of restrictions on trade with countries such as Iran, Syria and Libya. There are also periodic moves to increase relatively minor controls and, in particular, to increase consumer protection, eg against imports of unsafe toys, to increase copyright restrictions and to preserve cultural heritage. If some of these proposals were to come to fruition we would have to ask for additional resources to deal with them or get transfers from other Departments.

22. Enhancement of Drugs Preventive work. This bid is to enhance our efforts in the top priority area of prevention of drugs smuggling, in ways designed to achieve highly cost-effective results. We have undertaken our annual analysis of the trends and prospects for drug smuggling. It is difficult to be confident about the immediate future. On the one hand there are some encouraging signs that the peak of heroin smuggling may have at least for the time being passed : the quality of the drug being seized is now much poorer than in recent years and the quantity of seizure has begun to turn down. This may be attributable to some extent to supply problems but we are reasonably sure that our strengthened efforts to counter heroin smuggling have had a significant impact. On the other hand, there is also evidence that if anything smuggling of cocaine, cannabis and most recently amphetamines has been increasing, and this is likely to continue in the immediate future.

23. A particular feature of the scene last year has been the enormous increase in the attempts to smuggle drugs in the body and there is no sign whatever that this trend, which imposes tremendous pressures on our resources, is likely to change in the near future. Against this background, we propose certain very selective strengthening to deal with drug smuggling as indicated in Annex B. We have obtained very good results from earlier enhancements and we would look to secure similar improvement as a direct result of this extra manpower once it is fully operational. Given the volatility of the drugs scene we would wish to await next year's PES round before considering whether any further selective enhancement of our efforts in 1989-90 and 1990-91 might be necessary. We would also want to keep the nature of our drugs target under review. For the first time we set a target for the current year (confidential and not published in our Management Plan) of a 15 per cent increase in drugs seizures, and further increases for the PES years are built in to our bid, illustrated in figures 2.1 and 2.2 of Annex D. While committed to setting stretching drugs targets, however, we may wish to change their form to reflect the nature of the

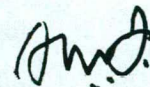
trafficking and shifts in risk areas - if, for example we needed to pay more attention to freight traffic, as seems probable, targets reflecting a range of relevant indicators may be more appropriate than numbers of seizures.

24. **Capital expenditure.** We are seeking £5 million extra in 1988-89 for Part 1 works, and larger amounts in subsequent years. A major component in all three years is for new accommodation projects in Northern Ireland, where our facilities are particularly poor and still deteriorating. The major reason for the escalation in costs arises from the recent news from PSA that their earlier estimates for the projects were more than 100 per cent out. They have now been revised from just over £9 million in total to as much as £19.2 million. We are still grappling with the detail and will provide more once the picture becomes clearer. But, despite this bombshell, we remain convinced that the time is long overdue for improving our estate in Northern Ireland. It is not simply a case of good management needing to provide an adequate working environment for maintaining staff morale; our efficiency and effectiveness are vitiated by our inability to perform some functions to the necessary level at what is the UK's only land frontier. We have substantial demands and cost escalation to cope with in 1988-89, but by deferring wherever possible we have reduced the first year requirement in order to be able to fund continuing work on Newry Custom House, work on computer halls at Southend, ingoing works for our new Investigation building, and essential works for new facilities at Luton and Stansted. With this deferment, larger bids for subsequent years become inevitable. We can provide officials with details of our programme as required.

25. **Conclusion.** I recognise that the bids are substantial, but I would emphasise that they are designed to secure commensurately larger increases in outputs in the two key priority areas of the prevention of drugs smuggling and in securing VAT revenue; in both cases we have built in substantial productivity improvements, without which our bid would be

very much higher. The bids do, however, reflect the actual pay requirements. We see this as unavoidable in an increasingly competitive climate and essential if we are to achieve the value for money targets we would want to propose and agree with Ministers. If we cannot attract and retain staff in the high tax-yielding areas of our work because the remuneration package is not appropriate, or if we are not able to recruit and train staff according to planned profiles because of shortage of cash, the impact on our outputs is likely to be disproportionately greater than the cost. Even if we concentrated purely on inputs (which would be misleading, since a large element of our bid is designed to increase the resources available either for meeting public expenditure or for reducing taxes), it is significant that our unit cost of input is, along with the Inland Revenue, the lowest of the main Government Departments. Moreover, our rate of increase of unit cost of input from 1983-84 to 1987-88 is the second lowest of the main Departments and well below the average for all Departments - this despite the fact that we have a much higher ratio of executive officers to clericals than most Departments.

26. For these reasons I am convinced that the bids are the minimum needed if the Department is to fulfil the Government's publicly declared objectives, especially in the revenue and drugs field in the face of continuing increased pressures. We stand ready to discuss.



A M FRASER

ANNEX A

	1988/89	1989/90	£k 1990/91
1. Running Costs			
a. Extra staff (inc on-cost)	5125	13632	24112
b. Pay assumption for existing staff	16692	17300	18891
c. Overtime & t&s (Outfield)	0	1764	3244
d. Accommodation charge	2896	6730	7541
e. Minor works	0	687	795
f. Training	300	937	1124
g. Misc preventive (vehicles, radios & uniforms)	562	365	418
h. IT/CEPS	0	3513	6326
i. VAT skills	7000	8000	9000
j. Miscellaneous	0	1083	1478
Total running costs	32575	54011	72929
2. Non Running Costs			
a. EC 180 (mainly legal)	2264	2548	2728
b. CCC Fee	0	0	6
3. Capital			
a. IT	0	-1534	-1204
b. Part 1 Works	5000	8500	11800
c. Other	1354	946	1140
Total	6354	7912	11736
4. A-in-A	(522)✓	(250)✓	(170)✓
Total bid	40671	64221	87229

✓ ie increased yield

ADDITIONAL CASH BIDS: NOTES

Item 1(a) Extra staff. The reasons for the bid are set out in Annex B. The cost per head reflects our best estimate of the cost of training and equipping staff in key areas.

Item 1(b) Pay assumption. We are working on a 6% pay assumption for 1988. We see this as covering not only the basic pay settlement but also the various pay allowances, supplements and restructuring which in each of the last two years have added about 2% to our pay bill. The figures include two other items: first, the cost of carrying forward the 1987 pay award - we are content to discuss the presentation of this; and second the cost in 1990-91 of a full year's salary for those additional staff agreed for 1989-90 in last year's PES. This is a purely technical change. However, we have not felt able to make a realistic pay assumption for PES years 2 and 3; we have therefore left this at 2 1/2 per cent in each year.

Item 1(c) Overtime and t&s. We are making no additional bid in the focal year. The bids for future years reflect continuing redeployment of staff into front-line areas and the need to ensure adequate provision - consistent with that for 1988-89.

Item 1(d) Accommodation charge. We have set ourselves a demanding accommodation target for 1990 but the increases in PRS charges primarily reflect rapidly rising rents in the London area exacerbated by a continuing drift of work to the south east. A detailed case supporting this bid is being sent to Official Treasury.

Item 1(e) Minor works. There is no additional bid for 1988-89, but this is on the important assumption that PSA will be funded to fulfil their obligations under the PRS system; for the later years we are seeking adequate provision to ensure that we can cope with backlogs of maintenance etc.

Item 1(f) Training. The first year bid reflects projected expenditure on technical and development training for managers in the VAT and Customs areas. The future years involve some catching up of earlier deferments, eg on management development, under pressure from the centre (and kwhich we would like to achieve anyway).

Item 1(g) Miscellaneous preventive. This reflects a continuing need for extra spending on vehicles, radios and uniforms if the drugs effort and related priorities are to be sustained.

Item 1(h) IT. We have no bid in 1988-89; in the later years there is a significant shift from capital to current, relating mainly to rephasing of the CHIEF project, which we will explain to Official Treasury. It also arises from changes in the amounts estimated in PES 86 which can properly be reclassified from current to capital. It may be that some later adjustment will be necessary if the decision is made to go ahead with the Government Data Network.

Item 1(i) VAT skills. This is the subject of current discussions. The figures quoted represent the best estimates of what may be needed for investment training and allowances for VAT officers with a view to achieving very substantial improvements in performance.

Item 1(j) Miscellaneous. Again we have been able, despite pressures from new tasks and our increasing priority work, to contain our bid in the first year, but must bid in subsequent years so as to ensure that provision for a range of items remains adequate to support increased operations.

Item 2(a) EC 180. There are a number of items here which we feel ought to be excluded from running costs and treated as more akin to programme expenditure. The most important of these - and the one that produces most of the increase - is legal expenditure. This largely reflects our growing success in pursuing VAT and drugs

cases and the costs. It includes £500k for witnesses' expenses; responsibility for paying these has been transferred from the Lord Chancellor's Department but without a PES transfer.

Item 3. Capital. Our bid here primarily reflects an increasing realisation of our need to invest in building works if we are to be able to perform effectively. We made provision in the last PES round for some major projects but there have been new developments since then: first, the doubling of PSA's estimates for the Northern Ireland projects; secondly, the need to reorder our London estate; and thirdly, the need to ensure adequate funding for some less costly but still essential projects over which we have little control eg new customs facilities at Luton and Stansted; and finally, the need to ensure that development costs are covered. We are also bidding for some extra money in respect of items - like cars - needed for preventive work; with a possible offset in the IT area.

Item 1 A-in-A. Our latest projections suggest that income may exceed baseline figures. This produces, of course, a small saving on our overall requirement.

PES MANPOWER 1988-91: CHANGES BETWEEN PES 86 & PES 87 AND NEW BIDS FOR 1990/91

	Changes 88/89	Changes 89/90	New bids 90/91	Totals	
CUSTOMS					
Growth & Enhancement Growth in Passenger/ Freight traffic	+226	+223	+209	658	Increases for growth required to maintain current standards especially of control of drugs smuggling and to staff essential new control points. The bid is net of efficiency/productivity savings amounting to more than 250 in each year.
Enhancement of Drugs Control	+130	+2	+1	133	Increases needed to enhance mobile preventive & freight teams, dog handling units, intelligence & passenger controls, plus 21 specialist drugs investigators and support staff. The enhancements are predicted to lead to increases in the number and amount of drugs seizures and prosecutions - see graph.
Drugs Prosecutions	+16	+8 1/2	+5 1/2	30	Additional Solicitor's Office staff required to cope with a 75% increase in drugs cases in the last two years and with continuing growth in the PES period.
New legislation Drugs Trafficking Offences Act Criminal Justice Bill	+36	+12 1/2	+10 1/2	59	This bid represents new work on the smaller cases (ne £50,000) arising under the DTOA and is expected to yield £3m in a full year.
	+23			+23	Additional staff are required for extended custody of persons suspected of concealing drugs internally (stuffers & swallowers) and for investigation of the assets of offenders other than drugs smugglers who are covered by the DTOA (expected to realise £3 1/2 m in a full year).
Other					
HQ:Customs	+16	+32	-4	+44	The 88-89 increase is for further development of the CHIEF project. The 89-90 increase reflects slippage in CHIEF and deferment of some of the forecast savings [about 40 efficiency savings will still be made].
	+447	+278	+222	+947	
EXCISE					
Miscellaneous changes	+2	-3		-1	A wide variety of changes in procedures and controls are taken account of in this bid which is net of a further 164 efficiency/productivity savings in the three forecast years.
	+2	-3		-1	
VAT					
Growth & Enhancement Growth in the register			+93	+93	Resources required are for continued growth in the VAT register largely for cost effective control work.
AV Enhancement			+50	+50	New bid in line with previous years. The addition of 50 visiting staff yields £10.25m in a full year at an expected cost benefit ratio of 1:10 (HEO level).
Large trader control			+15	+15	This covers the highly cost effective control of large traders and it is forecast that the extra staff would bring in over £6m in a full year.
New legislation Keith	-151	-33	+164	-20	Postponement of implementation of Keith III to facilitate the early introduction of annual accounting means that resource requirements for 88-89 & 89-90 have been deferred to 90-91.
Cash/Annual Accounting	+90	-30	-15	+45	A once for all increase of +45 in 88-89 is needed for the introduction of cash accounting. The annual accounting arrangements give rise to a temporary requirement in 88/89 for a further 45 which will be relinquished in the following 2 years.
Other					
Miscellaneous changes	-1	+11		+10	This forecast is net of 56 new productivity/efficiency savings in HQ.
	-62	-52	+307	+193	
ADMINISTRATION					
New legislation and Central initiatives	+25	+26	+24	+75	These figures assume large continuing savings and a declining ratio of administration to operational staff but resources are needed in 88/89 for Data Protection Act and changes in Civil Service Pensions Scheme and for untying from PSA of Major and Minor works and maintenance in all 3 years.
Other bids					
Miscellaneous changes	-2	-6	-23	-31	Reflects a variety of minor organisational changes. The bid includes an extra 30 efficiency savings in 88/89 and 20 new savings in 90/91.
	+23	+20	+1	+44	
GRAND TOTAL	+410	+243	+530	1183	

PRODUCTIVITY/EFFICIENCY SAVINGS 1988-89 TO 1990-91

	88-89	89-90	90-91	Total
PES 85-86				
Declared savings (as adjusted)	283	288		571
PES 87 New Productivity Savings				
Customs:				
Containing Growth				
Passenger/Freight	252	273	323	848
Tape recording of suspects	10	10	5	25
HQ (Chief slippage)	(-19)	(-48)	4	(-63)
Excise:				
Productivity savings	53	56	55	164
VAT:				
Containing Growth in Register			54	54
HQ VISION/VALID new technology	11			11
Debt recovery computerisation Solicitor's Office	19	19	7	45
Other:				
Misc changes and general efficiency savings	68		20	88
Absorption of admin overheads			35	35
TOTAL PES 87 Savings	394	310	503	1207
Add PES 85/86 Savings	283	288		571
PRODUCTIVITY SAVINGS	677	598	503	1778
Additional Efficiency Savings (1)				
Keith Compliance:				
LVOs	160	68	10	238
HQ	35	51		86
Additional Efficiency Savings	195	119	10	324

(1) These savings were initiated by the Keith legislation and arise from a general streamlining of procedures in LVOs and HQ involving significant redeployment of staff. We have drawn a fine distinction between savings arising entirely from our own efforts and those which have an external dimension but in the broad sense both should be classified as efficiency savings.

CUSTOMS FREIGHT TRAFFIC

Fig 1.1

Import Entries Per Officer

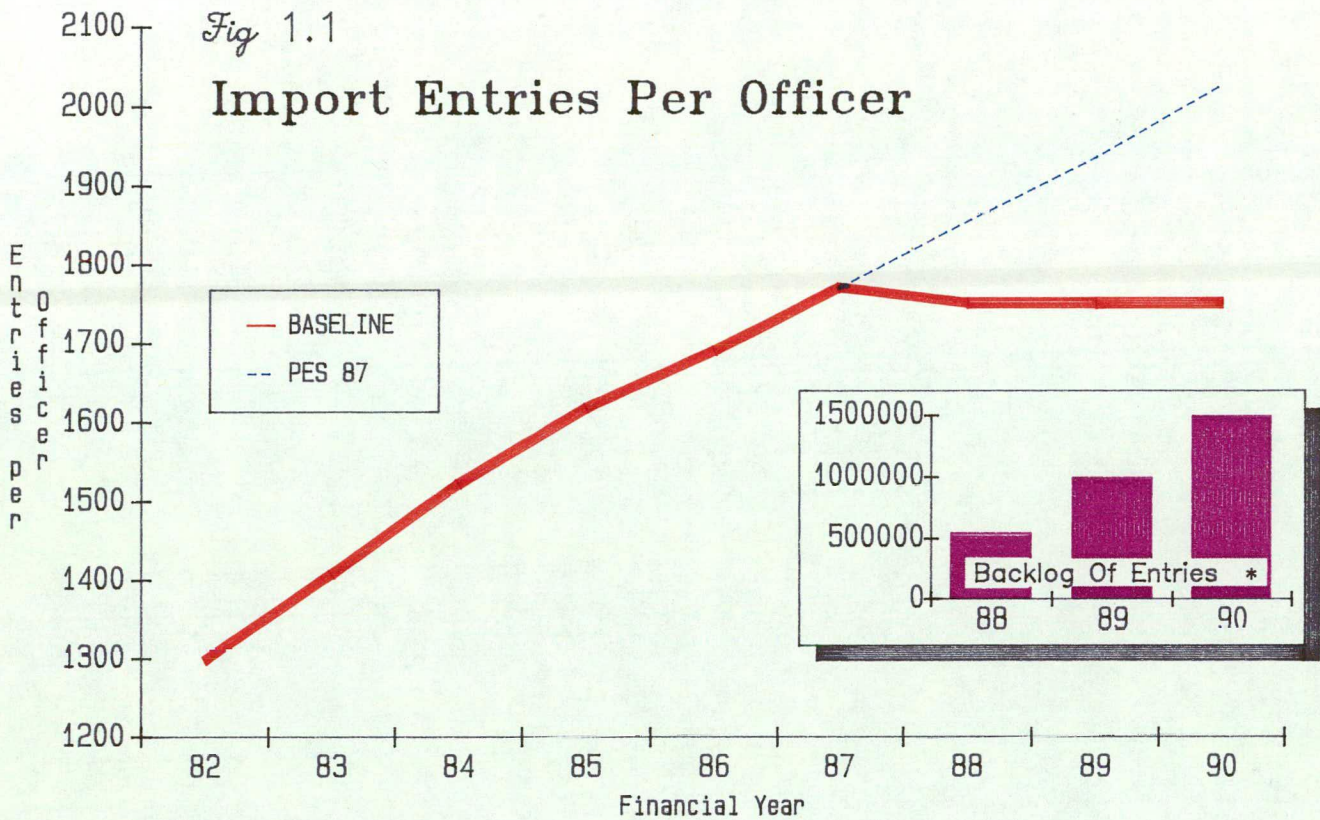
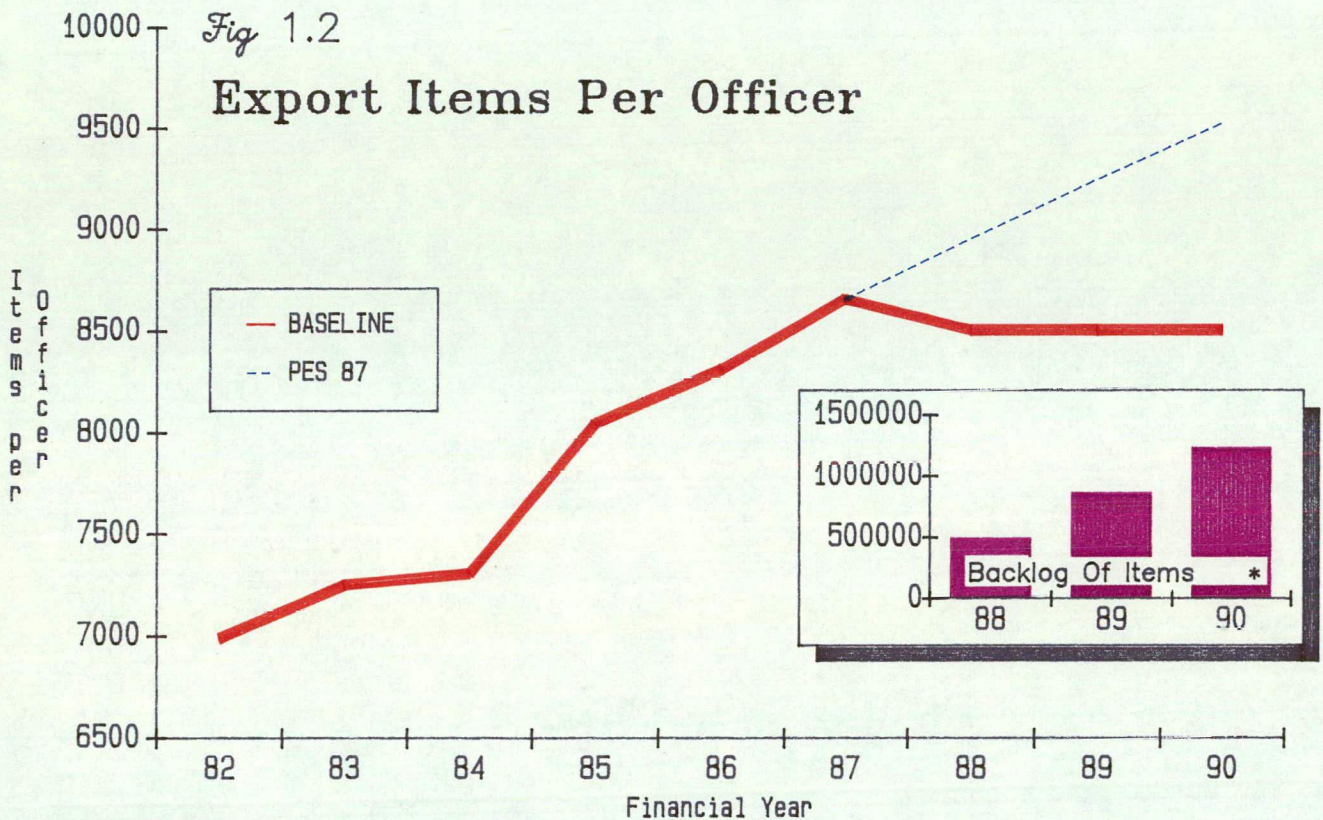


Fig 1.2

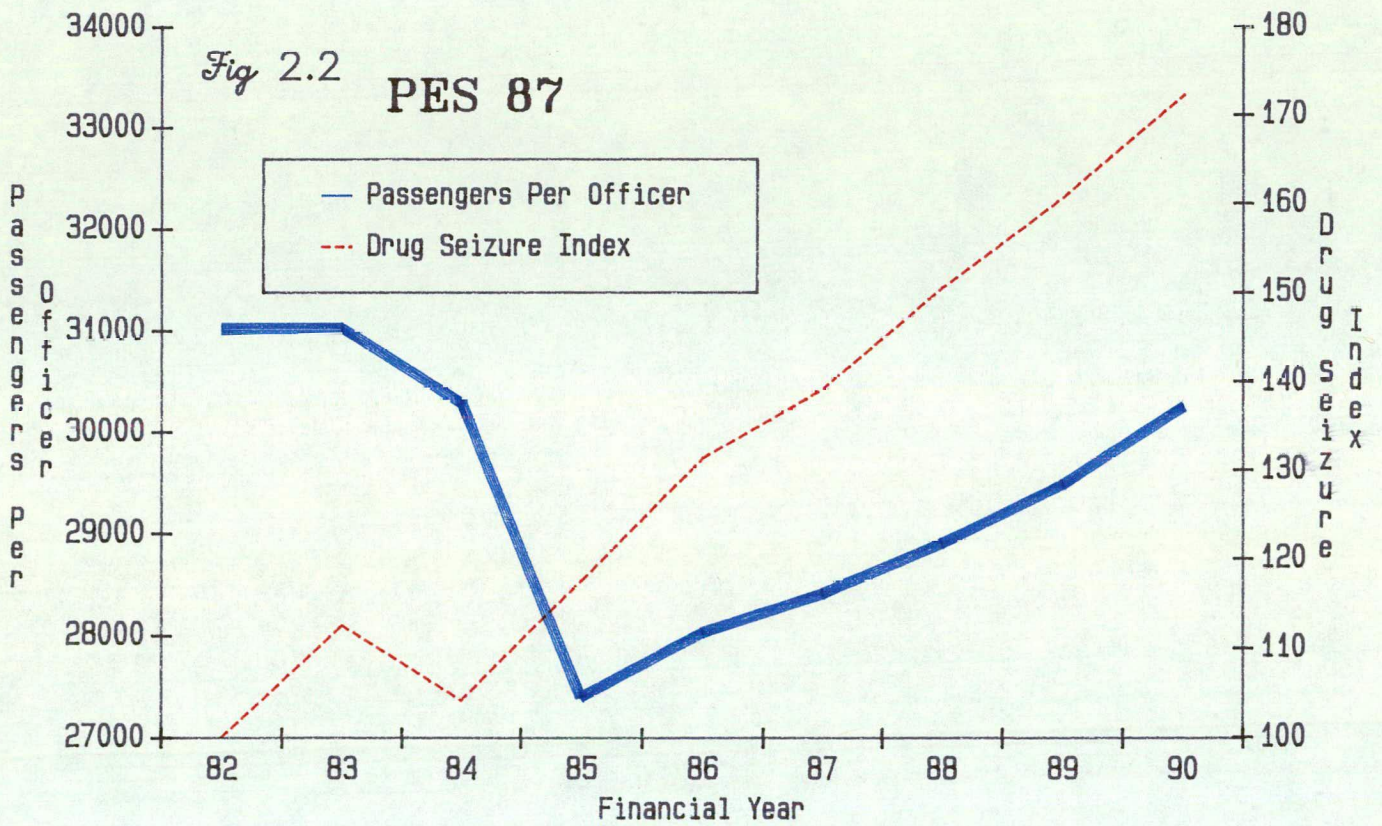
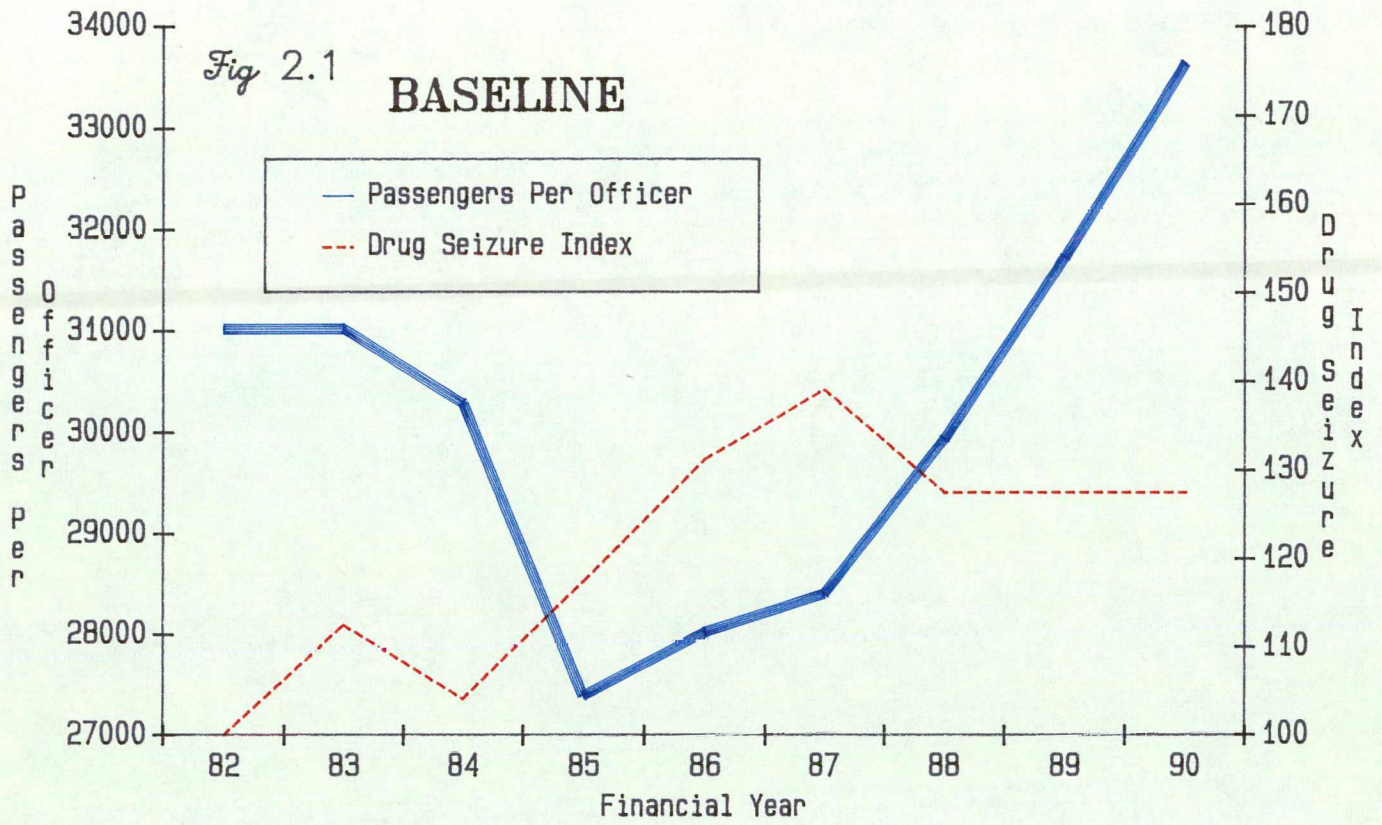
Export Items Per Officer



* Estimated backlog of work arising from insufficient resources represented by the Baseline for 88/89 to 90/91.

CUSTOMS PASSENGER TRAFFIC

Passengers Per Officer & Drug Seizure Index



VALUE ADDED TAX

Fig 3.1

VAT CONTROL

Value Of Underdeclarations Discovered On Control Visits.

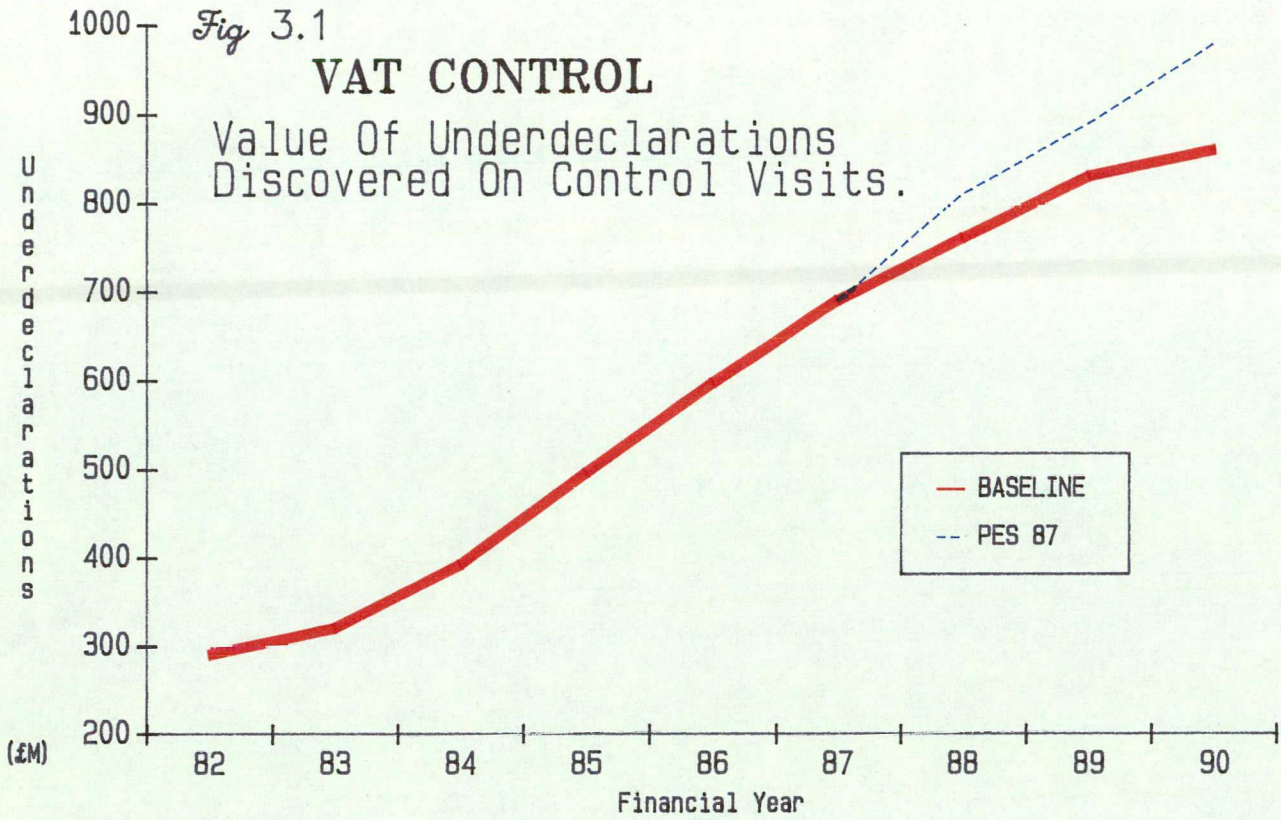
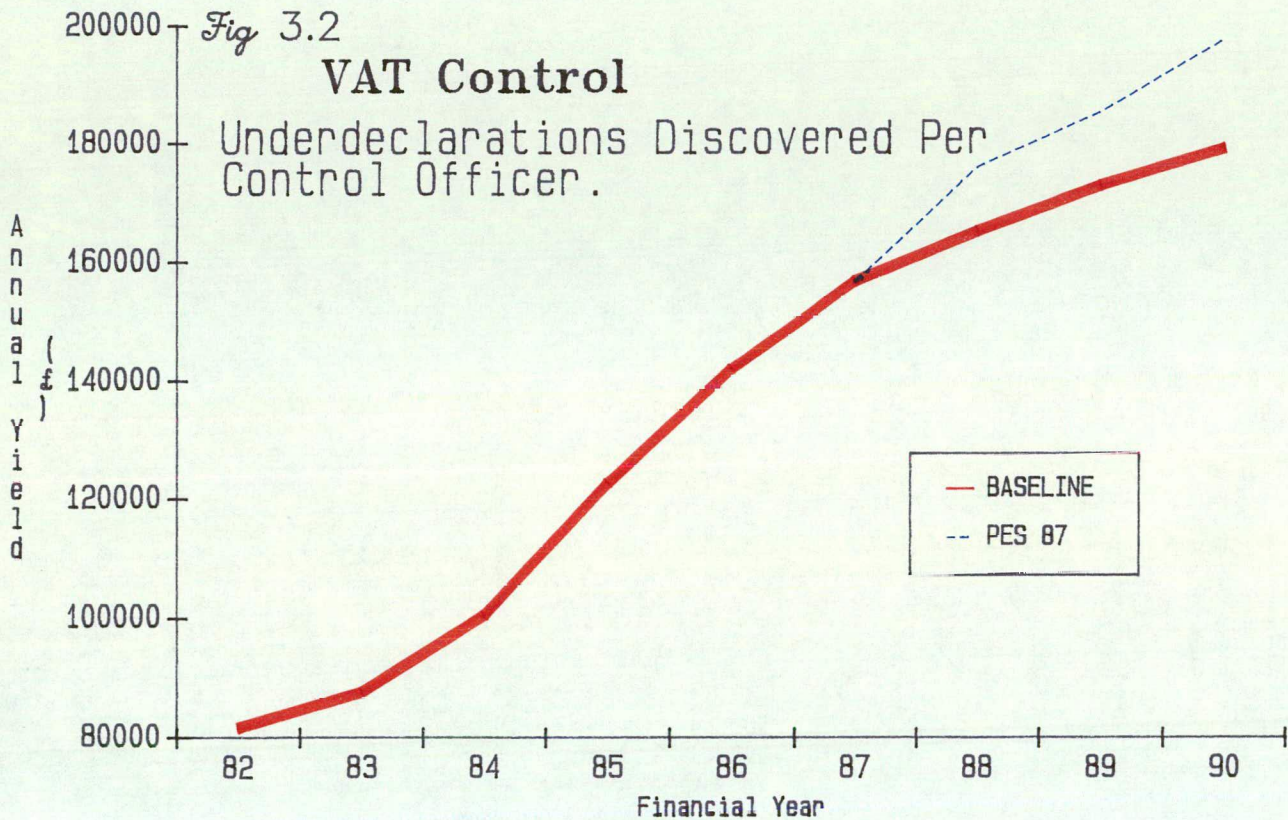


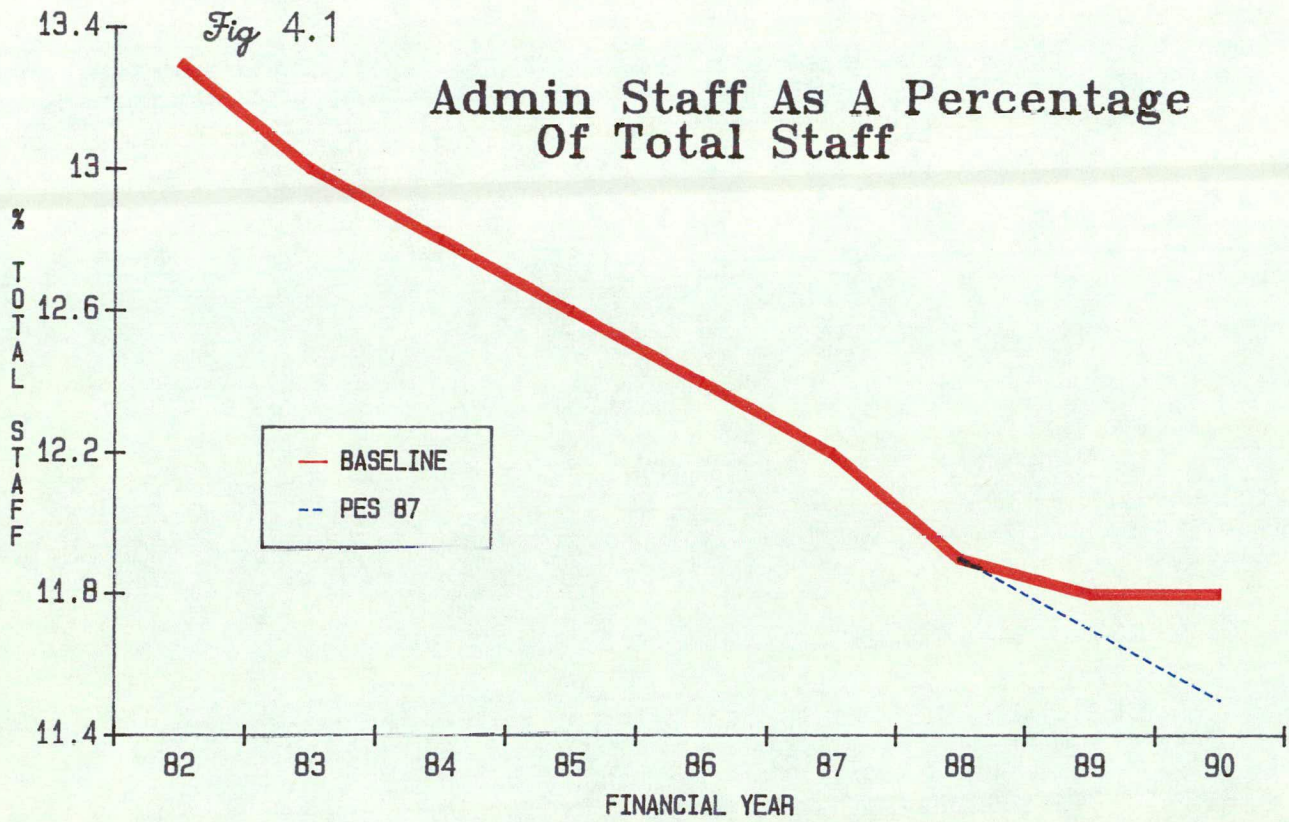
Fig 3.2

VAT Control

Underdeclarations Discovered Per Control Officer.



ADMINISTRATION



2. FORWARD LOOK TO 1991

2.1 General

2.1.1 In determining the Department's long term strategy, two of the major factors to be taken into account are, first, the continuing growth in VAT and customs work and, second, the increasing complexity of the work with growing diversification of large businesses, expanding use of computers and increasingly sophisticated methods used in drugs smuggling and VAT evasion and avoidance.

2.1.2 In VAT the Department's strategy is to improve trader compliance and control and to counter tax avoidance so that the proper yield from the tax is achieved. Both the "Keith" legislative provisions and the indirect ("preventive") effects of control visits to business premises are expected to result in more accurate tax returns and earlier payment of the tax due. In its control visiting the Department will aim for the time being to continue the upward trend in the real level of underdeclarations discovered and in cost-yield ratios by targeting control resources at the areas of greatest risk and potential revenue yield. There are many uncertain factors, but in broad terms the Department expects the total underdeclarations discovered over the period until 1991 to be in the range of £2 billion - £3 billion excluding the preventive effect which is estimated to be at least an equivalent sum. Increased attention will also be paid to the rules relating to tax liability with the aim of preventing tax loss by avoidance schemes.

2.1.3 In the customs area, overall levels of freight and passenger traffic are expected to grow steadily in the period to 1991. There are likely to be steep increases in certain types of traffic which are of particular importance from a departmental control viewpoint (eg container traffic). In the fight against drugs importation the Department will continue to enhance its efforts in accordance with the six point strategy referred to in paragraph 2.3.2. A main objective will be to continue to improve effectiveness in seizing drugs and catching drug traffickers. It is also intended to extend the current developmental use of tape recording of interviews with suspects throughout England and Wales. This will be phased over a number of years according to a timetable which will be settled by the end of the Summer 1987.

2.1.4 In excise, the period to 1991 is expected to be an opportunity for consolidation and assimilation of the reforms of previous years. Local risk assessment will be developed, backed by systems of management

information which will aim to match effort more effectively against results. Control will continue to demand high standards of technical expertise.

- 2.1.5 The work of the staff in the Department will become increasingly complex, demanding good technical knowledge particularly to deal with the increasing use of computer/information technology, both by traders and within the Department.

DEVELOPMENTS IN SPECIFIC AREAS

2.2 VAT

- 2.2.1 The maintenance and enhancement of the effective collection of VAT will continue to be one of the Department's top priorities in the period to 1991.
- 2.2.2 A very high priority will continue to be given to control visiting, which remains an increasingly cost-effective activity. Considerable importance will also be attached to the successful implementation of the Keith measures. In particular the default surcharge is expected to have halved the average arrears of VAT by 31 March 1989. This will have a considerable impact on the resources applied to enforcement. The introduction in Keith Phase III of interest on underdeclarations etc and a serious misdeclaration penalty should also prove beneficial to the control effort, although in these cases the effects may take somewhat longer to work through.
- 2.2.3 To limit tax avoidance, mainly affecting partial exemption and group treatment, changes to the law will be proposed in the 1987 Finance Bill and by Regulations. These will need to be implemented, but in any case the aim will be to operate existing controls more effectively. Such steps may not, however, be the end of the story. The accountancy profession is now taking a much more active interest in VAT: the increased care that is being given to running VAT accounts is welcome, but the Department is likely to find itself having a much greater continuing involvement with anti-avoidance measures than has previously been the case.
- 2.2.4 In October 1986 the Department published a consultative document on VAT and small businesses. The main features of this document are the inclusion of outline schemes of cash accounting for VAT and 'annual accounting' ie annual returns with payments on account. If legislation is enacted in 1987 cash accounting could be implemented before the end of 1987 and annual accounting the following year.
- 2.2.5 The introduction of work returns and improved visit analysis is scheduled for January 1988. This will greatly enhance the accuracy of assignment values to

the benefit of the revenue. It will also provide major improvements in management information, including measures of achievement.

- 2.2.6 Special attention will continue to be given to the control of the largest traders. By 31 March 1988 the control of all such traders should be based on the application of a systematic approach and audit techniques, and experience will be evaluated with a "pilot" regionalised large trader control unit to co-ordinate the control of the largest businesses. If the pilot scheme is successful, four other such units will be established in 1988-89. The initial phase of training 450 Accountancy Advice Officers will be completed in the Autumn of 1987. The intention is to continue this training at a replacement rate and to extend it to some Surveyors.
- 2.2.7 The Department is also committed to a thorough-going review of VAT training with a view to making any necessary changes in 1988-89 and subsequent years. A report on computer audit training recently made by independent consultants is being evaluated. If the recommendations are found to be broadly acceptable, changes in that form of training will be introduced as soon as practicable.
- 2.2.8 There has been a notable increase in the productivity of VAT staff and it is expected that it will be maintained at this high level. Considerable attention will continue to be given to the qualitative aspects of control visiting. Growth in the discovery of underdeclared tax on control visits over the next few years will be increasingly dependent on improvements in the effectiveness and expertise of LVO staff and the adaptation of control methods to utilise the full potential of new technology. Plans already exist to introduce local area networks for individual office technology projects and to make extended use of portable computers and programmable calculators. From 1988 however the availability of LVO terminals linked to regional computers will provide an opportunity to examine the use of so-called "expert systems" in which the accumulated knowledge and experience of the most able staff in HQ and the Outfield can be distilled into a database. This will be made available to LVO staff throughout the country in a form tailored to meet the particular needs of an individual control visit or trader enquiry.
- 2.2.9 On the organisational front, the tendency for business to be progressively more concentrated in the south-east is likely to call for the setting up of one or two additional LVOs in the London area; this may have implications for the Collection structure in the south-east.

Beyond the Department's immediate control, both the structure and the machinery of VAT could be influenced by European Community developments. The European Community's plans to complete the internal market by the end of 1992 would, if adopted in full, have a major impact on the Department's VAT and excise duty controls in regard to trade within the EC. It is too soon to say how far this will, in practice, be the case. A number of proposals for harmonisation directives await consideration, and progress on them is slow. The one which would have the most significant impact on a wide range of traders and in the Outfield would restrict deduction of input tax on certain purchases of a mixed business/private use character, but this has been opposed by a number of Member States including the UK. In 1987, the European Court of Justice is expected to consider the European Commission's allegations that the UK is infringing the Sixth Directive in respect of certain zero ratings. The UK case is being vigorously defended; but if it were lost, liability changes would be required, some of which could be of administrative significance.

2.3 Customs

2.3.1 The principal factors expected to influence planning for the period to 1991 are the continuing and changing nature of the drugs problem allied to external trends in the volume and nature of passenger and freight traffic, initiatives emanating from various external bodies (eg the European Community and other Government Departments) which have prime responsibility in fields where the operational responsibility lies with Customs, and the need to order internal priorities.

2.3.2 It is expected that drugs will continue to require priority attention. The Department will respond on the basis of its six-point strategy:

- a. recognising the continuing importance of the traditional skills of officers operating routine controls, ensuring that these controls are maintained in line with changes in traffic levels and continuing to improve the efficiency of their operations;
- b. seeking to ensure that the staff deployed in the fight against drugs are the best available and are properly trained;
- c. placing increasing emphasis on the use of risk assessment, intelligence and information in seeking specific targets or 'profiling' potential smugglers, both in applying routine controls and in carrying out special exercises;
- d. making greater use of mobile resources which can be flexibly and selectively deployed where needed;

- e. supporting the efforts of staff with
 - i. technical aids and equipment,
 - ii. cutters and aerial surveillance and
 - iii. drug detection dogs; and
- f. developing co-operation and sharing information with the UK police, overseas Customs administrations and other enforcement agencies.

- 2.3.3 Additional staffing resources are being allocated in 1987-88 but because of the volatility of drug smuggling, staffing requirements beyond then will continue to be reviewed on the basis of up-to-date assessments of need. In the period to 1991 the aim will be to have firmly established throughout the Department a planning system for drugs preventive work which takes fully into account risk analysis and, wherever appropriate, targets for results. Investment in technical aids to complement increased staff resources is expected to cost some £2 million per year: the objectives will be to ensure that these aids are used to their utmost effectiveness, to seek to devise reliable performance measures and to develop and introduce reliable "sniffer" equipment for the detection of drugs.
- 2.3.4 On import and export controls generally, where resources are already fully stretched, any proposals which would require additional customs resources will continue to be carefully examined. Where other Government Departments are concerned there are likely to be continuing pressures resulting from their policies. The Department will wish to consider in each case whether it is appropriate to ask for compensation or a contribution towards the cost of any additional work.
- 2.3.5 The prospective growth in both freight and passenger traffic will be contained as far as possible by increased productivity and efficiency, although the need to maintain standards and levels of control and to meet demands for new services and facilities will inevitably lead to pressures for increased resources.
- 2.3.6 To assist with this, a principal activity over the period will be to carry forward the co-ordinated programme of ADP developments which is fundamental to the Department's planning. The aim will be to achieve quicker and less labour-intensive processing of entries and trade statistics and to obtain better management information. Central to this strategy is the CHIEF project which will expand and enhance the existing computerised systems for entry processing. Currently no firm date for the implementation of the first phase of CHIEF has been agreed although it is unlikely to be before 1990. Work on the full study is

proceeding and is expected to be completed during the year. The system will be extended in subsequent phases and will eventually handle all import entries and the great majority of export entries. It is envisaged that facilities providing for direct input by traders of customs entry information will be extended to enable almost all import entries and a significant proportion of export entries to be processed more rapidly, to the benefit of both the Department and the trade. In due course the CHIEF system will also provide on-line controls over import quotas and new facilities such as trader retention of entries and paperless licensing procedures. The system will also incorporate EC requirements arising from the CADDIA and CD projects which envisage the adoption of international standards for communicating and processing data, and the co-ordinated development of customs computer systems by Member States to improve the efficiency of their administrative procedures.

2.3.7 As regards staffing, Phase I of CHIEF is expected to have a broadly neutral effect in the Outfield. The later phases are expected to result in some staff savings in the Outfield, although timing and quantification are difficult to predict precisely at this stage. Significant staff savings are expected in the Statistical Office as a result of the implementation of CHIEF.

2.3.8 New Community initiatives under consideration in the context of completion of the Internal Market are not sufficiently advanced to allow any meaningful assessment of their impact. As already noted in paragraph 2.2.10, however, the potential implications for the work of the Department are considerable - VAT and excise as well as customs. The Department will continue to play a focal part in inter-departmental discussions about Europe in 1993.

2.3.9 The Channel Fixed Link is due to open in 1993. Customs procedures and facilities are being planned in consultation with other Government Departments. Although there should be no significant call on Outfield resources until the year 1992-3, assessment of the potential impact on deployment of staff is difficult until planning and development are further advanced.

2.4 Excise

2.4.1 The effective collection of the high yielding excise duties and proper control of the important inland customs activities, whether involving the collection or disbursement of revenue, remain amongst the Board's top priorities. Over recent years, departmental controls in the excise have undergone extensive modernisation and streamlining, with a consequential large reduction in the official resources employed. The general principles applied are:

a. the trader takes full responsibility for duty etc accounting and security, including physical security, by exercising his own controls; the Department's role is to supervise these;

b. the wide range of activities in the excise and the diversity of traders mean that departmental controls and resource allocation must be based on local assessment; and

c. the guiding principle in resource allocation is revenue risk; this takes account of the incidence of the duty etc charge or refund, the way in which the trader's business is conducted, and a realistic view of the opportunities for loss to either UK or Community revenues.

2.4.2

The years to 1991 are seen as a period of consolidation. There is a need to assimilate fully the reforms of the last few years. Radical new departures are not planned.

- In oils work, the recent OWR changes are to be consolidated.
- In control of the drinks duties, the changes need to be more fully carried through into practice. Activities will continue to be affected by trade developments which blur the previous, long established distinctions between producers of different drinks; by rationalisation, particularly of the spirits industry in Scotland; and by changes in the pattern of distribution and sales (for example, the impact of the supermarkets).
- In betting and gaming, there will be increasing emphasis on credibility and risk assessment in planning visiting cycles.
- Customs changes such as the EC's standardised entry (SAD), tariff and statistical arrangements (HS/TARIC) will have a significant impact on work in the excise. Effort will be needed initially for training and implementation but once the changes have settled down the effect on resources should be broadly neutral.

2.4.3

Local risk assessment is a cornerstone of policy, but it cannot be done effectively in isolation; HQ Divisions have a responsibility to achieve common standards. In addition to standing instructions, guidance is given through seminars for local managers and control staff as well as local visits. These will continue throughout the period.

2.4.4

There is also a need for improved management planning and for information of a systematic character to be available to staff at all levels. This will assist policy review at the centre and effective planning and allocation of resources both centrally and locally. A development project has been set up. The intention is to build on existing locally held information, developing a planning system which will take assessed risk into account and match resources applied against results achieved.

2.4.5

Excise control will continue to demand good technical knowledge of the industries and their products but, increasingly, excise staff will have to be able to respond to the increasing use of computers/information technology, both by traders and within the Department. Areas of importance include the spread of computerised accounting and stock control, and the emergence of new measurement devices.

2.4.6

In framing excise duty policy, the Department can expect continued pressure to respond to social and environmental factors, for example from those concerned with alcohol abuse or the health risks associated with tobacco products.

2.4.7

The EC Commission will continue to press for further harmonisation of customs legislation and limited changes or modification to some inland customs procedures may be expected. The progress toward harmonisation of excise duty structure and completion of the internal market is impossible to predict. Complete removal of fiscal barriers to intra-Community trade would require far-reaching structural and operational changes. Meanwhile, development of inland customs clearance facilities will continue along the lines agreed by Ministers and within the constraints imposed by resource limitations.

2.5

Resource Management

2.5.1

Over the next few years the planning and budgeting systems already introduced will be considerably extended. It is expected that by 1989-90, after the pilot experiments which are planned to take place over the next year or two, Collection and operational unit plans will cover comprehensively all main activities and will relate resources to them, set targets and objectives and provide the main basis for monitoring and reviewing performance in relation to the Collection budget. HQ Directorates will also be running extensive budgets which will, as already happens in Collections, be related to plans.

2.5.2

Increasingly, inspection activity in the Outfield, especially by the Collectorate, will be carried out in the context of the development of these systems.

2.5.3

Line managers will be encouraged to use increasingly the consultancy services available to them from staff inspection and internal audit as well as Management Services Division, initiating their own ideas and intentions for the better use of resources.

2.6

Accommodation

A number of developments in the period to 1991 will affect significantly the management of the Department's estate:

a. there will be considerable rationalisation of the Department's estate. The principal changes will be the closure of a number of HQ London offices and the movement of staff to Sea Containers House and Maxwell House;

b. there will be a continuing objective to dispose of surplus accommodation thereby achieving challenging sq mtrs/head targets. This will to some extent offset the costs of the shift to the south-east and enable the Department, wherever possible, to improve the quality of the accommodation; and

c. the evolution of PRS is likely to result in a gradual transfer from PSA to client Departments of responsibility for management of their estates. This is a welcome development. The principal areas of likely change concern:

- **Major Works (ie over £150,000).** Following the change to departmental funding of major capital projects introduced in PES 1986, the Department will take over full Vote responsibility for such projects in 1988-89. The Department will introduce the concept of project "ownership" and "sponsorship" with an element of untying from PSA, possibly starting with one or two projects in the first year of operation; others will be added as departmental resources and expertise permit.
- **Minor Works.** The Department is dissatisfied with the existing "club subscription" system for works services costing between £5,000 and £150,000. Funding is planned to move to full repayment with an element of untying. This will allow the Department to set its own priorities and will overcome the disadvantage of the present system whereby Departments pay for all such works ordered as well as paying for them through the PRS accommodation charge (in effect paying twice). The timing of this change is not yet settled, depending as it does on the next major review of PRS due in 1988.

- **Maintenance.** The likely way forward on maintenance will be for the PSA to retain responsibility for initiating and funding essential (ie. statutory or contractual) aspects of maintenance, recovering its costs by a service charge levied on occupying Departments. Departments would take over responsibility for initiating and funding all other maintenance, with an element of untying.

All these developments will have resource and training implications for the Department both in HQ and the Outfield.

MANAGEMENT IN CONFIDENCE



10 DOWNING STREET

LONDON SW1A 2AA

From the Principal Private Secretary

2 February 1987

Dear Sir,

VALUE FOR MONEY IN CUSTOMS AND EXCISE

The Prime Minister held a Value for Money Seminar this afternoon with your Minister and the Chairman of the Board of Customs and Excise. Sir Robert Armstrong and Sir Robin Ibbs were present.

The Minister of State said that the legal powers for the administration of the Customs services were mostly vested in the Commissioners, not in Ministers. This helped the efficient management of the Department since the Board of Customs were able to get on with running the Department with Ministers setting priorities and monitoring value for money targets. The Service had been given clear targets, notably the reduction by a half of outstanding late payments of VAT (£1.2b.) and an increase in the yield by £2.2b. by 1990 from control visits. Targets, based on output measures, were also set for other areas of the work, including work on drugs. He had been much encouraged by the spirit with which the Department were tackling the programme to increase value for money.

The Chairman then gave a slide presentation of the Department's value for money programme, concentrating on VAT and drugs control. The points made included:

- i. The Board had decided to publicise its management plan so as to give an unambiguous signal of its commitment to improved value for money. The plan set out specific targets for the Service's operating officers. Despite the increasing workload, the Department had managed to reduce staff as a result of sharp productivity increases. There had been a determined and successful attempt to transfer staff from support functions to front line operational tasks.
- ii) The V... had depended to an important extent on the D...ent's efficiency. In the last 7 years... had been 287 per cent additional tax

47/2

from control visits and 262 per cent ^{average} additional tax ~~from~~ visits. This had been achieved by improved central planning of visits, greater expertise of staff, achieved for example through training, and a commitment throughout the Service to greater efficiency.

- iii) It was difficult to devise targets and outputs for the Department's drug control work because of the many factors outside management control. But the figures did appear to show that Customs investigators had had some real success, especially in combating the heroin trade. The approach was to focus on expectations. Next year the target focussed on an expectation of a 15% increase in seizures. Productivity had been increased by training, through intelligence, use of computers, drugs' liaison officers and the introduction of improved technical aids.

Concluding his presentation, the Chairman said that the changes introduced in the last few years into Customs, with their focus on results, output, targets and value for money, had significantly improved the Department's efficiency and the services it provided. The extra resources allocated to the Service would produce a good return. The Department was still working hard to make further improvements, though they were under certain restraints. It was important to persuade the Department's staff that their input into the value for money process was appreciated.

The following were the main points made in the discussion:

- i) The Department had been helped in its value for money programme because its Board structure gave the Commissioners a clear responsibility for management. There were, however, certain controls on the Board's activities which inhibited efficient management. The gross running costs control was a prime example. But the Treasury was showing flexibility in this area. Pay was also inhibiting recruitment as was the difficulty of persuading staff, eg at HEO level, to come to London because of the costs of housing. The possibility of tied housing for Customs' staff was not an attractive possibility. Another possibility in dealing with staff shortages was using agency staff for Customs work though this presented difficulty.
- ii) Once traders ^{had come through the transition into} [were in] the VAT system, they were less likely to complain about Customs administration. It was gratifying that there were only 150 complaints a year in relation to the 400,000 control visits. Staff training was important in securing good relations with taxpayers.

- iii) There was a real risk that the South American drug barons would switch attention to Europe now that the US market was saturated.
- iv) The Department did not have acute recruiting problems, even for the difficult and nasty drug control work. (The Prime Minister observed that she thought there was a good case for paying special bonuses to the staff involved in some of this work). The Department was, however, suffering from a loss of good trained staff attracted by higher salaries, especially to the accounting firms. Morale in the Service was reasonable, though there was a belief that the Service was not generally rewarded for the good results which it was achieving.
- v) The Board were well aware of the need to minimise the costs of compliance with regulations and were in close touch with the Secretary of State for Employment on this matter. They were taking active steps to simplify regulations.

Sir Robin Ibbs said that Customs were a prime example of the success in introducing quantified targets into management and of a devolved system of management based on a Board structure. Now that Customs, could demonstrate that it had a firm grip on outputs, it was ^{important} clear that the Treasury had been able to provide extra inputs for the Service.

Summing up the discussion, the Prime Minister said that Customs and Excise had an impressive story of management achievement in recent years for which everyone concerned at all levels in the Department should be congratulated. They had demonstrated the value of targeting and of focusing on outputs. Much had been achieved already, and she welcomed the commitment of Customs' management to work for further improvements.

I am sending copies of this letter to the Private Secretaries to the Chief Secretary, the Chairman of Customs and Excise, Sir Robert Armstrong and Sir Robin Ibbs.

L. Wick
Nigel Wicks

N. L. WICKS

Simon Judge, Esq.
HM Treasury

*Yes PES -
You must substitute
'unsatisfactory'
for 'radical',
LW*

Ch

*You will wish to see this.
If you agree, I will minute
out* that you still think
there is something radically
wrong with the way the
system is working.*

MR KUCZYS

FROM: MARTYN HAIGH

DATE: 7 July 1987

cc Mr Kemp
Mr Scholar
Mr Luce
Miss Sinclair
Mr McKenzie

HAIGH
TO
AWK
7/7

INLAND REVENUE : PES 87 BIDS

7/7

**only within HMT
of course LW*

You asked me to check on two propositions before you minuted out the Chancellor's comments.

2. First, the unrealism of 1988-89 provision as set in PES 86. The Chancellor is right to recall that we deliberately imposed the PES 86 uplift factor (ie 2½ per cent) on the provision for pay increases between 1987-88 and 1988-89 - the Revenue having initially bid for a 'realistic' 6 per cent increase. This was, of course, in addition to the element of continuing 'squeeze' implicit in PES 86 provision for pay in 1987-88. The point is at paragraph 6 in the attached extract from the minutes of the final wrap-up meeting between the Chancellor and Mr Battishill.

3. Second, the question whether the Revenue have now gone to the other extreme. The Revenue's total running cost bid is certainly high. Part of it is to correct the deliberate unrealism of the baseline provision for pay increases in 1988. But only a relatively small part - and we cannot really say that they have conspicuously over-corrected. Out of a total running cost bid of £85.6m in 1988-89, the Revenue are asking for

- £26.8m for a 'realistic' year-on-year increase between 1987-88 and 1988-89: that is, about 7% compared to 2½ per cent in the baseline. This covers about 1 per cent for maturing full-year effects of the 1987 settlement, plus about 4½ per cent for the main 1988 settlement, and a further 1½ per cent for special IR deals (eg one with the IRSF).

- £28.2m to cover accrued past pay underprovision up to and including this year's excess cost of the 1987 settlement
- £10.1m to cover extra manpower
- a balance of £20.5m to cover accommodation and other non-pay running costs, net of reduced requirements.

4. Our preliminary FP view is, I think, that the overall bids for pay are fairly realistic (even possibly too low, if an IRSF deal comes off) and that our main scope for resistance lies in the manpower and GAE bids, coupled with pressure for quantified additional efficiency savings as the quid pro quo for funding any special pay deals.



M HAIGH



FROM: A W KUCZYS
 DATE: 22 October 1986

cc Mr. Hing
2 p. 1986 IR
folder

MR BATTISHILL - INLAND REVENUE

cc PS/Chief Secretary
 PS/Financial Secretary
 Sir P Middleton
 Mr F E R Butler
 Mr Monger
 Mr Scholar
 Miss Sinclair

INLAND REVENUE 1986 PES

You discussed the Inland Revenue's Survey bid with the Chancellor and the Chief Secretary on Monday 20 October.

2. The Chancellor said he was very grateful for the way in which you had gone so far towards meeting the Chief Secretary's difficulties. We were now almost there, and the Chancellor hoped to reach final agreement at this meeting. The aim was to get the increase in Inland Revenue running costs down to around - though still slightly above - the average for all Departments (which would be about 6 per cent). The Chancellor and Chief Secretary had some suggestions as to how this might be achieved.

3. You said that you were convinced that the PES bid was already too low. You would come under pressure from staff and unions when the Peat Marwick work measurement exercise results came out, indicating a deficiency of 2,000 taxes clerical staff. And there would also be a difficulty on pay: if there were not differential pay increases for the Inspectorate, many more would "vote with their feet". So there was a good case for the Revenue's pay rising faster than other Departments'. Indeed, this was not just a problem of the Inspectorate: it affected clerical staff

AWK
 TO
 BATTISHILL
 22/10



increasingly (and, in answer to a question from the Chief Secretary, you said this was not confined to the South East); and data processing (you said that without special increases in DP costs, your running costs increase would have come out at only 5.7 per cent).

4. On pay, the Chancellor said that an assumption of 5½ per cent would be too high, and out of line with other Departments. 4½ per cent would be more realistic. He accepted that this assumption might mean some element of "squeeze", but nothing like as much as last year. You said that it would certainly not be possible to absorb such a pay gap two years running. You asked what would happen if, for whatever reason, there were such a large gap again. The Chief Secretary pointed out that, in the last resort, the Inland Revenue would be able to ask for access to the Reserve to meet the cost of an excessive pay settlement. He *added*, however, that he would only agree to a claim on the Reserve in the most exceptional circumstances. (You pointed out that you had not asked for money from the Reserve this year: you had only asked to be able to build up the staff deployed on black economy work more slowly, but this request had been turned down.)

5. You said that one difficulty was that the IRSF were making threatening noises about reimposing the overtime ban. They would be looking for another deal rather like last year's. However, of the 1,400 extra staff for which you had bid, only about 200 would be deployed in the taxes network. The Chancellor said that, if the overtime ban were reimposed, he would take a very jaundiced view of bids for extra staff. But he was prepared to see Tony Christopher if you thought that would help.

6. The Chancellor asked additionally that, to bring the Revenue into line with other Departments, the general uplift factor (rather than a specific pay assumption) should be applied to pay provision in the second and third survey years.

AA

AA

*last 1/2
business IR
Manpower @ work
Pom blabla*

FROM: R CARPENTER
DATE: 4th September 1987

- 1. MR HANSFORD *4/9.*
- 2. PS/CHANCELLOR

cc Attached list

*BT read
pro stated*

MANPOWER RETURNS FOR THE CHANCELLOR'S DEPARTMENTS

Attached are the Manpower Returns for the Chancellor's departments for the quarter 1 July 1987.

*Chancellor
↓
BKM
6/8/87*

2. In total, manpower in the Chancellor's departments showed a net decrease of 1031 compared with the figure for 1 April 1987. The largest changes were recorded by the Inland Revenue (a reduction of 672 due to savings arising from the computerisation of PAYE (COP)), HM Treasury (a reduction of 181½ mainly due to CISCO staff numbers falling as a result of the contractorisation of Devonport and Rosyth Dockyards) and the Department for National Savings (83½ reflecting a lower level of recruitment). Among the other departments only comparatively small changes have taken place since 1 April, the largest being reductions of 47 in Customs and Excise (due to a lower level of recruitment) and 25 in Her Majesty's Stationery Office.

3. Wastage rose in the quarter from 2.18 per cent to 2.95 per cent.

4. During the quarter the number of casuals showed a net increase of 266½ from 1282 to 1548½. Most of the increase was in the Inland Revenue where 217 additional casual staff were taken on to assist with seasonal work.

5. The latest permanent staff-in-post figure is 1531 below the published target figure for 1 April 1988.

R Carpenter

R CARPENTER

*2/16
/17*

PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary

Sir P Middleton

Mr F E R Butler

Mr Anson

Mr Turnbull

Mr C D Butler

Mr C W Kelly

Mr T R H Luce

Mr Scholar

Ms Boys

Ms Sinclair

Mr N M Hansford

Mr Instone

Mr Hoare

Mr Parrett

Mr Haigh

Mr Binns

Mr Tyrie

Mr A M W Battishill

Mr A D Fallows (VO)

Mr Rogers

Mr Crawley

Mr Marshall

Mr Gould

Sir Angus Fraser

Mr Hawken

Mr Russell

Mr Battle

Mr Patterson

Mr Lee (2 copies)

Mr Gravenor (Royal Mint)

Mr Goodwin (NULO)

Mr Royston (RFS)

Mr Dole (HMSO)

Mr Davies (HMSO)

Mr Bamford (COI)

Dr Renn (GAD)

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) Inland Revenue

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) Customs and Excise
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)

) Department for
) National Savings

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) Tables 1a, 1b,
) 2a, 2b only

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SUMMARY PICTURE OF MAIN DEPARTMENTS

DEPARTMENT	PERMANENT STAFF IN POST	RECRUITMENT	LOSSES	CASUAL STAFF
Treasury	3,177½ at 1.7.87 following a decrease of 181½ during the quarter	84 Permanent Staff were recruited	265½	An increase of 8 to 40
Customs and Excise	25,812½ at 1.7.87 following a decrease of 47 during the quarter	571 Permanent Staff were recruited	618	A decrease of 19 to 211½
Inland Revenue	67,126 at 1.7.87 following a decrease of 672 during the quarter	1,347 Permanent Staff were recruited	2,019	An increase of 217 to 1,091
National Savings	7,615½ at 1.7.87 following a decrease of 83½ during the quarter	84 Permanent Staff were recruited	167½	An increase of 13 to 36

PERMANENT STAFF IN THE CHANCELLOR'S DEPARTMENT

Table 1A

Departments	1.4.86	1.7.86	1.10.86	1.1.87	1.4.87	1.7.87
Treasury (inc. Cisco)	3,363	3,354	3,321	3,334½	3,359	3,177½
Customs and Excise	25,159½	25,109	25,277	25,311½	25,859½	25,812½
Department for National Savings	7,773	7,766½	7,653	7,666	7,699	7,615½
Inland Revenue	69,260½	69,441½	69,026	68,416	67,798	67,126
Her Majesty's Stationery Office	3,378	3,375	3,371	3,362	3,350	3,325
Central Office of Information	857½	831	821	815	824	807
Royal Mint	989½	994½	993½	991	976	970½
Registry of Friendly Societies	124½	122½	126	126	134	137
Government Actuary Department	61½	58½	57½	58½	59½	58
National Investment and Loans Office	52	52	52	52	51	50
TOTAL	111,019	111,104½	110,698	110,132½	110,110	109,079
		+85½	-406½	-565½	- 22½	-1,031

CASUAL STAFF-IN-POST

Table 1B

Departments	1.4.86	1.7.86	1.10.86	1.1.87	1.4.87	1.7.87
Treasury (inc. Cisco)	22	28½	30	30	32	40
Customs and Excise	236	234	211½	219	230½	211½
Department for National Savings	46	57	74	246	23	36
Inland Revenue	734	1,262	1,507	992	874	1,091
Her Majesty's Stationery Office	71	76	89	65	82	112
Central Office of Information	36	45½	39	30½	37½	52
Royal Mint	39	13	3	1½	3	4
Registry of Friendly Societies	1	2	3	3	0	0
Government Actuary Department	0	2	2	0	0	2
National Investment and Loans Office	0	0	0	0	0	0
TOTAL	1,185	1,720	1,958½	1,587	1,282	1,548½

WASTAGE (PERMANENT STAFF)

Table 2A

	1 Jan 86 to 31 Mar 86		1 Apr 86 to 30 June 86		1 July 86 to 30 Sept 86		1 Oct 86 to 31 Dec 86		1 Jan 87 to 31 Mar 87		1 Apr 87 to 30 June 87	
	NO.	%	NO.	%	NO.	%	NO.	%	NO.	%	NO.	%
Treasury (inc. Cisco)	84½	2.51	76	2.27	132	3.97	81½	2.44	90	2.68	265½	8.36
Customs and Excise	630	2.50	720½	2.87	631½	2.50	504½	1.99	578	2.24	618	2.39
Department for National Savings	175½	2.26	210	2.70	206½	2.70	181½	2.37	152½	1.98	167½	2.20
Inland Revenue	2,012	2.90	1,876½	2.70	1,847½	2.68	1,725	2.52	1,437	2.12	2,019	3.01
Her Majesty's Stationery Office	78	2.31	69	2.04	71	2.11	77	2.29	79	2.36	95	2.86
Central Office of Information	39½	4.61	41	4.93	45	5.48	35	4.29	33	4.00	34	4.21
Royal Mint	21	2.12	13	1.31	16	1.61	12½	1.26	20	2.05	12½	1.29
Registry of Friendly Societies	9	7.23	9	7.35	4	3.17	5	3.97	5	3.73	5	3.65
Government Actuary Department	2	3.25	3	5.13	3	5.22	3	5.13	1	1.68	1½	2.59
National Investment and Loans Office	0	-	0	-	0	-	0	-	1	1.96	1	2.00
TOTAL	3,051½	2.75	3,018	2.72	2,956½	2.67	2,625	2.38	2,396½	2.18	3,219	2.95

RECRUITMENT (PERMANENT STAFF)

Table 2B

	1 Jan 86 to 31 Mar 86	1 Apr 86 to 30 June 86	1 July 86 to 30 Sept 86	1 Oct 86 to 31 Dec 86	1 Jan 87 to 31 Mar 87	1 April 87 to 30 June 87
Treasury (inc. Cisco)	100½	67	99	95	114½	84
Customs and Excise	638½	670	799½	539	1,126	571
Department for National Savings	172½	203½	93	194½	185½	84
Inland Revenue	993	2,057½	1,432	1,115	819	1,347
Her Majesty's Stationery Office	69	66	67	68	67	70
Central Office of Information	19	14½	35	29	42	17
Royal Mint	17	18	15	10	5	7
Registry of Friendly Societies	11	7	7½	5	13	8
Government Actuary Department	5½	0	2	4	2	0
National Investment and Loans Office	1	0	0	0	0	0
TOTAL	2,027	3,103½	2,550	2,059½	2,374	2,188

FERB
↓
C/EX
15 SEPT

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*PSBR replaced
C/S category
revenue - manuals.*

FROM: F. E. R. BUTLER
15th September, 1987.

CHANCELLOR OF THE EXCHEQUER

c.c. Chief Secretary
Sir Peter Middleton

INLAND REVENUE PES

You asked for a note on the Inland Revenue Survey position for the meeting which you are holding with the Chief Secretary, Sir Peter Middleton and me on Thursday 17th September. A note, which is the outcome of discussions with the FP and running costs groups, is attached.

F. E. R. B.

F. E. R. BUTLER

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INLAND REVENUE PES 1987

Full details of the Revenue bid are set out in the annex. The running cost bid is as follows:

	<u>1988-89</u>	<u>1989-90</u>	<u>1990-91</u>
Net running costs bid	87.5	118.4	150.1
of which pay (excess of past pay costs and assumption of 6% for next year's settlement)	53.2	67.3	85.9
% running cost increase without (with) extra £14m. in 1987/88 for which bid expected next month	12.4(10.8)	7.1	5.5

2. Our aim on running costs generally is to cut bids to achieve the Cabinet's overall aim of holding down running cost growth to 1% in real terms. To meet the 1% target in the case of the Revenue would involve giving them only a further £15m. for running costs on the first year: this compares with their bid of £88m. which implies real growth of 8½%.

3. At the bilateral the Chief Secretary offered £15m. for pay, and perhaps £5m. for accommodation. Mr. Battishill made clear at the bilateral and subsequently that his first priority was to make realistic provision for his present pay bill and next year's settlement, together with unavoidable costs (eg PSA rents): extra activities could then be discussed on their merits. Both sides undertook to think further and the Chief Secretary asked Mr. Battishill to re-consider the pay bids and minor bids with a view to a reduction.

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4. Mr. Battishill has now come back with some suggested savings on running costs. The bulk of this comes from not putting forward the bid for £5m. for the Government Data Network: this is something the Chief Secretary told Revenue could be withdrawn anyway because of uncertainties about this project in 1988-89. In addition, Mr. Battishill offers a further £1.7m.-£4.3m. depending on Ministers' willingness to agree to withdraw pre-paid envelopes for certain correspondence with taxpayers, and Revenue's success in fending off a very late increase in PSA charges. We are advising the Chief Secretary to go for the £9.3m. offered by Mr. Battishill in the first year, reducing the bid in that year to £78.2m.

5. An offer in line with the Cabinet target in para. 2 would require the Revenue to cut numbers substantially in order to pay existing staff - at least in the short term. On the assumption that you want to go beyond that to meet Revenue's bid on their pay problems, Treasury Ministers could offer them an additional £55m. on running costs in the first year. This would cover their pay bid of £53 million in full, leaving £2 million or so for accommodation costs, the first year cost of independent taxation, and extra staff for Budget and collection work, on the following conditions:

- i. that they accept this as full and final settlement for all pay settlements up to and including 1988, ie they do not come back next year for more money to cover deficiencies in past pay settlements;
- ii. they accept that they have adequate provision in 1988-89 for independent taxation (cost =

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£2.9m.); and agree that subsequent years can be dealt with in the 1988 survey when the costings are clearer;

- iii. apart from staff needed for extra work arising from the 1987 budget any extra staff - say 200, a bit less than their bid - are employed on collection work (cost/yield 1:24) - first year cost around £1m.;
- iv. they give a firm commitment to improve their management planning, with the introduction of a system of unit cost targets over as much as possible of their work, by this time next year;
- v. the Revenue agree to absorb, or not to pursue, all other bids - casuals, overtime, extra supervisory staff etc.

6. Realistically, there is a danger however that £55 million would not be enough to meet their unavoidable commitments - the accommodation charge alone, even with the new savings offered by Mr. Battishill, is likely to be over £6 million. To deal realistically both with pay and the unavoidable items such as independent taxation and accommodation, it would be better to be prepared to fall back to an additional £65 million, though this would be more difficult in terms of the Chief Secretary's overall stance. This leaves them £13.2 million short of their bid for 1988-89, which they would have to distribute among their bids for extra man years (£9.1 million), casuals and overtime (£10.1 million) and other running costs (£11.4 million).

7. Arguments for an offer of £65 million are:

- (a) £65m. would solve Revenue's pay problems: if carried through to later years there would be no further wrangles about the cost of previous pay settlements (which account for one half of this year's pay bid of £53m.).

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- x volume
yrd*
- (b) Revenue could also meet unavoidable changes in costs eg from PSA, where ^{then} there are price takers. They would not be forced to cut numbers to pay staff, thus jeopardising the work state and possibly policy changes in pipeline.
 - (c) Revenue's current pre-occupation with meeting unavoidable costs, such as pay for existing staff, diverts management from future efficiency planning needed to hold down growth costs.
 - (d) If 1987-88 supplementary bid of around £14m. is accepted, the £65m. in 1988-89 would represent a year-on-year increase of 7.6% (2.6% above Cabinet target) in running costs.

8. Arguments against

- (a) Cabinet agreed we should aim to keep usual running costs shown in total public expenditure roughly constant. This means constraining rise overall to 1% a year in real terms.
- (b) £65m. for Revenue is year-on-year increase of 10.1% without supplementary £14m. in 1987-88 (8.6 per cent after the £14m.).
- (c) Latest forecast of overall running costs outcome including Revenue (+£65m.) and Customs (+£21m.), suggests Cabinet target will be exceeded by ½ per cent overall, ie a 1½% real increase in 1988-89 (but less if the GDP deflator is revised upwards between 1987-88 and 1988-89 - and in any case still within the likely overall growth of public expenditure generally).

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- WZ* (d) If settlements for Inland Revenue and Customs were restricted to 1% real growth Cabinet target would be achieved.

Conclusion and tactics

9. I recommend that Ministers settle at £65m. for Inland Revenue running costs for the reasons outlined above. I suggest an offer of £60m. in the first instance, falling back to £65m. to clinch the deal. Over and above £65m. on running costs I suggest that Ministers accept in full

- i. the LAPR/MIRAS bid (£40m., £40m., £61m.)
- ii. the independent taxation capital bid (£2.9m. in 1988-89).

10. Inland Revenue can show productivity gains of more than 1½ per cent in 1988-89 and 1989-90, but not 1990-91. In terms of the running costs policy, there is a case for conceding only pay increases beyond 1988-89 in line with the GDP deflator to put pressure on them to come up with a firm system of unit cost targets and acceptable productivity gains by next year's Survey. That is the approach which the line of figures on pay in the attached table embodies.

11. I see no advantage in pushing for an early settlement. It would be helpful to receive the supplementary bid for 1987-88 before the next bilateral. This suggests a second bilateral in mid-October.

1986-87 1987-88 1988-89 1989-90 1990-91

A. BASELINE

1,133.4 1,261.9 1,275.5 1,334.4 1,368.2

PERCENT INCREASE OVER PREVIOUS YEAR

11.3% 1.0% 4.6% 2.5%

B. PROPOSED RUNNING COST ADDITIONS

£m	<u>BID</u>			<u>OPENING POSITION/FALLBACK</u>			<u>FORECAST OUTCOME</u>		
	<u>1988-89</u>	<u>1989-90</u>	<u>1990-91</u>	<u>1988-89</u>	<u>1989-90</u>	<u>1990-91</u>	<u>1988-89</u>	<u>1989-90</u>	<u>1990-91</u>
B1 Pay	53.2	67.3	85.9	53.2	55.1	56.7	53.2	55.1	56.7
B2 Manpower	10.1	23.9	30.7	3.1	3.1	3.1	3.1	3.1	3.1
B3 Casuals & Overtime	9.1	7.0	1.0	0	0	0	0	0	0
B4 Accommodation	7.7	12.1	17.5	7.7	7.7	7.7	7.7	7.7	7.7
B5 ADP Current	-	6.4	3.8	-	-	-	-	-	-
B6 Other running costs	11.4	13.1	13.4	-	-	-	5.0	5.0	5.0
B7 Independent Taxation	2.9	-	-	2.9	-	-	2.9	-	-
GROSS RUNNING COST TOTAL	94.4	129.8	152.3	66.9	65.9	67.5	71.9	70.9	72.5

PROPOSED RUNNING COSTS REDUCTIONS

C1 Transferrable Allowances	4.9	9.3	-	4.9	9.3	-	4.9	9.3	-
C2 VAT refunds	2.0	2.1	2.2	2.0	2.1	2.2	2.0	2.1	2.2
SUB TOTAL	6.9	11.4	2.2	6.9	11.4	2.2	6.9	11.4	2.2
NET RUNNING COST TOTAL	87.5	118.4	150.1	60.0	54.5	65.3	65.0	59.5	70.3

	<u>BID</u>			<u>OPENING POSITION/FALLBACK</u>			<u>FORECAST OUTCOME</u>		
	<u>1988-89</u>	<u>1989-90</u>	<u>1990-91</u>	<u>1988-89</u>	<u>1989-90</u>	<u>1990-91</u>	<u>1988-89</u>	<u>1989-90</u>	<u>1990-91</u>
<u>CAPITAL ADDITIONS</u>									
B10 ADP	-	4.4	6.7	0	0	0	0	0	0
B11 Accommodation	5.6	4.5	3.0	0	0	0	0	0	0
B12 Independent Taxation	2.9	-	-	2.9	0	0	2.9	0	0
SUB TOTAL	8.5	8.9	9.7	2.9	0	0	2.9	0	0
<u>REDUCTIONS</u>									
C3 Capital	2.6	1.8	-	2.6	1.8	-	2.6	1.8	-
C4 Appropriations in Aid	6.3	6.7	6.9	6.3	6.7	6.9	6.3	6.7	6.9
SUB TOTAL	8.9	8.5	6.9	8.9	8.5	6.9	8.9	8.5	6.9
B15 LAPRA/MIRAS	40.0	40.0	61.0	40.0	40.0	61.0	40.0	40.0	61.0
<u>D. TOTALS</u>									
Implied net change to Baseline	127.1	158.8	213.9	94.0	86.0	119.4	99.0	91.0	124.4
IMPLIED NEW PROGRAMME TOTAL									
Cash	1402.6	1493.2	1582.1	1369.5	1420.4	1487.6	1374.5	1425.4	1492.6
Percentage increase on previous year	11.1	6.5	6.0	8.5	3.7	4.7	8.9	3.7	4.7

OPENING POSITION/FALLBACKFORECAST OUTCOME

	<u>1988-89</u>	<u>1989-90</u>	<u>1990-91</u>	<u>1988-89</u>	<u>1989-90</u>	<u>1990-91</u>
<u>E. GROSS RUNNING COSTS</u>						
Baseline	1011.7	1045.4	1071.5	1011.7	1045.7	1071.5
Percentage increase on previous year	3.5	3.3	2.5	3.5	3.3	2.5
Percentage increase in running costs per man year	6.4	4.9	2.6	6.4	4.9	2.6
TOTALS (After bids mins C1 & C2)	1071.7	1099.9	1136.8	1076.7	1105.2	1141.8
Percentage increase on previous year	9.6	2.6	3.4	10.1	2.6	3.3
Percentage increase in running costs per man year	12.4	4.2	2.9	12.9	4.7	3.2

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PPS Pl. (Minutes of mtg. with Mr Butler; Mr Butler's minute)

There is not a straightforward answer but I suspect that it would not be wildly wrong to say that the PSBR loss would be at least 7 times

FROM: MISS C E C SINCLAIR
DATE: 30 September 1987

- 1. MR F E R BUTLER the saving, as well
- 2. CHANCELLOR as causing all sorts of other disruption to present operations and future plans.

cc PS/Chief Secretary
Sir P Middleton
Mr Scholar
Mr Luce
Miss Hay

PSRB

Thanked!

INLAND REVENUE RUNNING COSTS

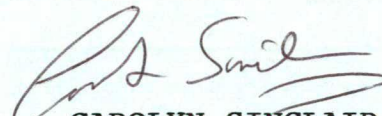
30.9.

You asked what the consequences would be for the PSBR if the Revenue were held to the Cabinet target of only 1 per cent real growth in running costs. This would imply an addition of £15 million to their running costs baseline in 1988-89, as compared with a bid for £88 million.

2. I am afraid we cannot give a straightforward answer. If the Revenue instituted a ban on all recruitment and promotion from next January, they might hope to save £25 million (equivalent to 4,500 staff) in 1988-89. But this would not be nearly enough to cover the gap between £15 million and their pay bid of £53 million for existing staff, let alone other essentials such as accommodation costs and independent taxation.

3. To make further savings the Revenue would have to sack people. This would involve redundancy costs and, industrial relations considerations apart, would be an expensive way of saving money.

4. What we can say is if Revenue cut 4,500 staff from discretionary work with an average cost/yield ratio of 1:7, they could save perhaps £25 million, but the PSBR would lose up to £200 million. This drastic measure would go only a small way towards bridging the gap between the Cabinet target and Revenue's needs. COP/CODA would certainly slip, since there would be no money for the overtime needed in local offices at the point of changeover to computers. Even taking a dispassionate view, the result would be some form of crisis.


CAROLYN SINCLAIR



Board Room
H M Customs and Excise
King's Beam House
Mark Lane London EC3R 7HE
Telephone: 01-382 5001

J B Unwin CB
Chairman

Rt Hon John Major MP
Chief Secretary
HM Treasury
Parliament Street
London
SW1P 3AG

CHIEF SECRETARY	
DATE	10 OCT 1987
ACTION	Mr Schwarz
TO	Mr Butler, Mr Anderson Mr Luce, Mr Turner Miss Sinclair, Mr Hoare Mr Hagen, Mr Romanowski Mr Grews

*PMG will
with 6 bills X
in Parliament*

John Chief Secretary

PES 1987 : CUSTOMS AND EXCISE ADDITIONAL BIDS

Following our meeting on 25 September I have, as you requested, had another hard look at the whole field of Customs and Excise expenditure with particular attention to the items you highlighted in our discussion. The outcome of my review is summarised below. I deal first with the group of general administrative expenditure items, together with accommodation; and then, in turn, with the VAT skills package, the basic control systems for VAT and customs work and, finally, capital expenditure.

General administrative expenditure (Gae)

2. To remove any misunderstanding, I should make it clear that in this context the term Gae does not refer simply to "pure" overheads. Much of it is directly and operationally linked to the achievement of targets in our main value for money areas, such as increased VAT control productivity, the targeting of mobile task forces to combat drug smuggling, and the increased number of prosecutions (up by 75% in two years). All these involve increased expenditure on overtime, travel and subsistence, stationery, telecoms, training and so on.

3. Our two additional bids for 1988-89 in this category were restricted to £0.3 million for training and £0.562 million for miscellaneous preventive expenditure. Both bids were lodged only after the most rigorous examination within the Department. Last year we introduced a systematic planning process for examining priorities in the training field. Nearly £1 million was removed from the bid before submitting it to you, by reducing yet again our efforts on management training and making the most optimistic assumptions we thought remotely tolerable about the turnover of (highly marketable) computer staff etc. Some of our training is mandatory, and the rest is essential to our key operations. Having combed through the figures again I see very little room for manoeuvre but, recognising the pressures that you face, I am willing to withdraw this bid.

4. This will undoubtedly have a cost as it will add to our existing backlog of preventive training. Since the main block of mandatory training will have to continue, it will mean cutting our desirable "marginal" training, particularly in the anti-drug smuggling field. I will, however, do what I can to minimise the impact of this.

5. Similarly, the £0.562 million for miscellaneous preventive expenditure, representing the current costs of cars, radios and other equipment, is closely linked to our targets on drugs, particularly in relation to drugs smuggling syndicates and the need for increased surveillance. This need was recognised in a staff inspection of our Investigation Division last year which found that investigations were not being pursued safely and properly because of the constraints on manpower and equipment. The staffing position is being put right and I am reluctant to risk jeopardising our efforts to break smuggling syndicates and organisations by cutting back on equipment. Despite these difficulties, however, I am prepared to withdraw this other Gae bid and to undertake to do our best to minimise the impact on our key drugs targets.

Accommodation

6. We discussed accommodation separately and I undertook to examine again our bid for £4.591 million in 1988-89. I am forced, however, to the conclusion that in face of PSA's sharp price increases, especially where existing leases in London are due to be terminated, we have absolutely no room for manoeuvre in the next year or two. I recognise that it is a purpose of the PRS system to bring pressure on Departments to find ways to reduce the impact of price changes and I repeat the assurance I gave you that I shall urgently review the scope for further dispersal from the high priced London and South-East areas. But any such dispersal will necessarily take time to arrange and indeed over the PES period could temporarily increase costs.

VAT skills package

7. At our meeting there was some debate as to whether the proposed additional expenditure of £7.0 million in 1988-89 was intended to maintain our level of performance on VAT control work or to enhance it. It was suggested that there was a contradiction. This is not so. First, we need to invest in more specialised training and a selective remuneration package to retain our best people simply in order to safeguard the VAT yield on its present path; in the private sector it would, I suppose, be called maintaining our competitive edge. Even if no additional revenue were forthcoming we would regard the expenditure as essential. Secondly, however, we believe that by targeting the resources carefully we can also produce - as a bonus, so to speak - a good return on the investment. As I mentioned, we estimate that the kind of package we have in mind would show a revenue return of 7:1 initially, and perhaps double that by 1990. Conversely, failure to introduce the package could cause substantial revenue loss.

8. We need to start implementing a package of measures very soon in order to prevent this. If we are not geared-up within two or three years the revenue will begin to suffer. At the same time, I take the point made by Michael Scholar about firming up the detailed elements of the package. It would be wrong to reach final conclusions until we see the outcome of the separate efficiency scrutiny on the London problem. If, however, we concentrate on the two critical areas of special training and a consequential remuneration package, and slow down the other elements, I believe that we could limit the overall expenditure in 1988-89 to some £5.5 million - a reduction in our bid of £1.5 million.

Customs and VAT control

9. The key question here you asked me to explore is whether we can absorb even more of the projected growth in customs passenger and freight traffic than we are already assuming, and find further offsetting savings from our VAT control programme. I have examined them both thoroughly and I regret that I see no justifiable scope for further reduction. If we had to take a cut, it would have to be at the high yielding margin which would cause our average efficiency to drop sharply.

10. Taking Customs first, we made a bid last year which was deferred until this year's PES so that an up to date assessment of traffic forecasts could be made. The Treasury accept those forecasts which are the basis of our renewed bid. Over three-quarters of the bid is for staff directly engaged in confronting passengers and physically examining freight. We have already set this at a level below the agreed traffic projections. To reduce the bid further would undoubtedly lower the standard of control. This would run directly counter - and be seen to run counter - to the Government's publicly declared undertaking that "these controls (ie routine controls by Customs and Excise at ports and airports) are maintained in line with increasing traffic". This is against a background where the Department seizes over 90% by volume of drugs and 90% of the number of seizures are made by our frontline staff at ports and airports.

11. Entry processing accounts for some 50 additional staff which assumes an annual productivity growth of some 5% to 6%. That is a formidable target, endorsed by Robin Ibbs, to achieve which will call on the combined efforts of our staff inspectors, management services and line managers. But there are a number of other considerations which make our task in this area even more difficult. In coping with the growing threat of using freight to smuggle drugs the importance of entry examination as a source of intelligence is increasing; as I explained, the extension of direct trader inputting of data has virtually reached its limits as a source of savings; and basic procedural changes are largely pre-empted by the introduction on 1 January next of the new EC harmonised and tariff entry arrangements. This is a major reform which, while providing considerable benefits to traders, is imposing a very heavy additional burden on the Department, most of which we have already planned to absorb. I believe it would be irresponsible of me to offer to go beyond this.

12. Nor, I fear, do I see any prospect of offering offsetting savings in the VAT area by extending the VAT control cycle beyond eight years. We are concerned here, not simply with the level of underdeclarations to be obtained from VAT control visits, but with the basic structure and credibility of the control system. In fact, we believe that there are strong arguments for reducing the control cycle from eight to six years in accordance with the recommendation of the Treasury staff inspection. To lengthen it, or to abolish it, would send quite the wrong signal to the VAT trader population. A good deal of effort has recently been invested in improving compliance, not least by legislating in line with the recommendations of the Keith Committee, with substantial benefit to the PSBR. Tampering with the basic structure of VAT control, for a quite modest staff saving, would risk undoing much of that work. If you decided that our bid had to be reduced here, I have to say that I would not feel able to extend the VAT control cycle beyond eight years.

13. To summarise, if our bids in these areas were cut back it would entail a switch from the highly cost-effective activities at the margin in order to protect the basic structure of control. Within VAT control we would need to make up any shortfall in maintaining the very minimum of control of small and medium sized traders by reducing the effort on large and complex traders which currently yields such a large revenue return. Similarly, on the customs front, the drugs effort would be significantly diminished by the need to divert resources to cope with and clear the increased throughput of freight, passengers and paperwork.

Capital Expenditure

14. Our bid here in 1988-89 is £5.0 million. As you know, we have a number of high priority projects in our Part 1 works programme. Most of them give little room for manoeuvre. We are, in particular, locked into a major programme in Northern Ireland to which public commitments have been made but for which the PSA costs have escalated. We have already had to assume within our bid that pressing construction work worth some £1 million will undesirably slip out of 1988-89. I would, however, be willing to work out with the PSA how we could phase the programme so that a further £1 million could be pushed back from 1988-89. This would reduce our additional bid for that year from £5 million to £4 million.

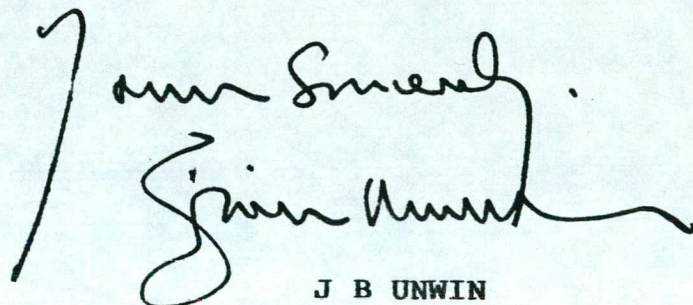
Conclusions

15. At our discussion Robin Butler suggested that we should aim to halve our additional running costs bid. It follows from what I have said above that a reduction of anything approaching that level would have a very serious impact on our key operations, especially in the top priority areas of VAT collection and the prevention of drug smuggling. It would also sharply reverse our progress in recent years in reducing all our unit costs of output and in achieving challenging value for money targets. We could not conceal this.

16. As set out above, however, I have examined again all our forecasts as you requested. Despite misgivings, I am willing to remove the bids from our miscellaneous groups of expenditure in 1988-89 and to slow down expenditure on the package of measures on VAT skills by £1.5 million and Part 1 works by £1 million. With rounding, I would be ready to trim this further at the edges to a reduction in the bid of £3.5 million in 1988-89. I shall also be looking as a priority at the scope for dispersal within the Department. I should perhaps add that since our meeting I have learned that the additions proposed this week by the Treasury to Society grades from 1 January 1988, together with earlier pay additions which came too late to be included in our bids, will add some £3.5 million to our pay bill in 1988-89. I am considering the implications of this, but you will appreciate that it makes the task of trimming our original bids even more difficult.

17. I recognise that that leaves our outstanding bid above the average level you are seeking. But I do believe that the Department, as a collector of over 40% of central Government revenue, is in a very special position. As I said at the outset of our discussion, the bulk of our spending is on 'people', and the majority of that on two very high priority areas - VAT and the prevention of drug smuggling. We are faced also with both quantitative and qualitative increases in demands in both customs and VAT that are well above average. Moreover, the bid is made against a background of very challenging targets for increased productivity and reduction in unit costs of output where all comparisons suggest that the Department has one of the lowest costs per member of staff of any of the large executive departments.

18. I am copying this letter to the Paymaster General.


J B UNWIN



FROM: J J HEYWOOD
DATE: 6 October 1987

PS/CHANCELLOR

*Ch/ You may like to have
a word with (ST) at the
Conference about handling,
and about the later years.*

cc PS/Chief Secretary
Sir P Middleton
Mr F E R Butler
Mr Scholar
Mr Luce
Miss Sinclair
Miss Hay
Mr Cropper

INLAND REVENUE RUNNING COSTS

Your minute of 21 September asked what scope there was for bringing forward Inland Revenue running costs expenditure from 1988-89 to 1987-88, with a consequent saving in 1988-89.

2. The Financial Secretary has considered this in the context of the Revenue's expected supplementary bid for this financial year. That bid will not be sure until later this week. The best central estimate is that it will amount to £14.3 million, but it could be as high as £18 million.

3. There is not a great deal of scope for bringing forward running costs expenditure, with a consequent saving in 1988-89. Perhaps £5 million could be shifted between the two years in this way, mainly by the timing of bills.

4. Added to the existing bid, this might give a supplementary of between £20 million-£23 million.

5. FP have suggested that there is a case for going further and giving the Revenue, over and above this, some money this year to improve the workstate by April 1988. Arrears are beginning to build up again, and the workstate is deteriorating. If nothing is done this is likely to be used by the Revenue as an argument against attempting to introduce independent taxation in 1990-91. The workstate, at least in terms of unanswered post, is not

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expected to be as bad as in 1985 even on gloomy forecasts. But the introduction of independent taxation requires it to be in tip-top condition. FP believe that there is a case for acting now, reaping the benefit in terms of improved morale and, probably, better value for money than if we wait until action is unavoidable.

6. This points to offering the Inland Revenue perhaps £15 million to be spent on improving the workstate in those districts which have the biggest problem. It would be for management to say how the money might best be spent - probably on a mix of casual staff and overtime.

7. There would not be a commensurate saving in 1988-89. But the workstate would be improved, helping the smooth and timely introduction of independent taxation, and the rate of growth in the Revenue's running costs between 1987-88 and 1988-89 would be reduced.

8. A supplementary on these lines would comprise:

	£ million
Current supplementary bid	14.3
Running costs expenditure brought forward from 1988-89	5
Workstate	15
<hr/> Total	<hr/> 35 <hr/>

If the Revenue's running costs limit is increased by £35 million this year, the year on year increase implied by an offer of £65 million for running costs in 1988-89 would be 6.3 per cent.

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CONCLUSION

9. The Financial Secretary is very reluctant to agree to this. He has not been impressed with Revenue management in a number of areas. But the Financial Secretary does think it likely that we will be forced into giving the Revenue more money in 1987/88 and he can see the attraction of pre-empting this (inevitable) further request. If we do agree, however, the Financial Secretary thinks we should make it clear to the Revenue that we are very disappointed indeed that the workstate has again deteriorated, despite the "management improvements" that were identified last year. Our defence will be that the extra resources are directed at ensuring a successful implementation of independent taxation.

A.H.

JEREMY HEYWOOD
Private Secretary

FROM: A M W BATTISHILL

THE BOARD ROOM
INLAND REVENUE
SOMERSET HOUSE

8 October 1987



Handwritten notes:
X S
clear
discuss
You have the previous
pps. on this.
8/10

CHIEF SECRETARY

INLAND REVENUE : WINTER SUPPLEMENTARY ESTIMATE

This note seeks approval for a Winter Supplementary Estimate for the Inland Revenue's running costs. The amount needed to deal with present operational plans is £m16.7. We can find increased receipts amounting to £m5 to offset part of the cost to the Reserve.

2. The note also seeks Ministers' views on two potential additional issues that have arisen in the course of the current PES discussions. First, in view of spending pressures next year, is there a case for allowing the Department to endeavour to bring some running cost expenditure forward from 1988-89 into 1987-88? Second, as a separate matter, should the Department be given some additional provision to improve the workstate in tax offices, having regard in particular to the need to prepare for the early introduction of Independent Taxation? We believe there could be scope under the first head for advancing perhaps up to £m7; if this could be added to the Supplementary it would save a similar amount in 1988-89. Under the second head the amount would be for discussion, if Ministers found the idea acceptable in principle. In this context a figure of £m10 was put to the Financial Secretary earlier this summer.

These points are covered in the FST's minute of 7/10.

Handwritten red 'X' mark.

cc Chancellor of the Exchequer
Financial Secretary
Mr Butler
Mr Scholar

Chairman
Mr Isaac
Mr Painter
Mr Rogers
Mr Pollard
Mr Fallows
Mr Crawley
Mr Nield

Background

3. It has been recognised since the beginning of the year that the Department's Estimate provision for running costs this year is not sufficient to carry out its operational plans. Our original forecast of the shortfall was £m17.5. I minuted the Financial Secretary about this on 6 April and 6 May, and there were discussions with the Financial Secretary on 10 April, and again on 5 May. To ease the position, a number of measures were taken which reduced the forecast shortfall to £m12.3. These included: increases in assessing tolerances; deferring the reintroduction of controls and checks put in abeyance as part of our workstate initiative last year; closure of the City Stamp Duty Office; reduced level of support from DP consultants; delay in extension of CODA (computerisation of Schedule D assessing) to all regions; and reduced activity in the Valuation Office.

4. At a meeting on 29 July to consider the implications of Independent Taxation, the Financial Secretary agreed that two of the cuts should be restored: support from DP consultants and reinstatement of the original CODA timetable. This increased the potential shortfall to £m14.3

5. With the approval of Treasury Ministers, the Department issued internal budgets based on the assumption that funds would be available to meet the shortfalls. It was agreed to proceed in this way because the alternative would have been to signal to some 1500 budget holders throughout the Department that there were very serious shortages of funds.

6. Thus the current position is that our managers are working to internal budgets for running costs that are £m14.3 in excess of the funds provided to us in the Estimates.

Our current forecast

7. During September, we have conducted a thorough review of the Department's expenditure, consulting all our major budget holders. We have sought to ensure that there is no unnecessary spending. The review indicates that we are broadly on target to hit our earlier forecasts, subject only to a point about additional pay costs to which I return below. Budget holders are generally expecting agreed plans to cost a little more than was originally expected at the beginning of the year but, again subject to the point on pay, by cutting back elsewhere it should be possible to contain the increases within the £m14.3 figure.

8. The reservation about pay arises as a result of pay settlements or offers made by the Treasury or in prospect that were not known at the time we made our earlier calculations. These have simply exacerbated the existing shortfall in our provision for pay. A list of them is at Annex A. Our best estimate is that these additional pay costs could cost us another £m2.4 this year. Not all of that amount is certain to materialise. About £m0.8 is intended to cover the possibility that the agreement for an extra 1.5% just reached with the SPCS will have to be extended to IRSF grades. The Treasury are hoping that the repercussions can be deferred until next year, but it is not yet clear that the position can be held until then. Without that uncertainty we should need to find only £m1.6 on top of the existing £m14.3 shortfall. The amount we shall need for London Weighting is also still uncertain; but at this stage we feel we must make some provision for the contingency that the current offer could be increased.

9. I am afraid, therefore, we must seek an additional £m16.7 on our running costs if we are to be sure of meeting our prospective pay bill in full.

10. At the same time I am glad to say we can increase by £m5 our estimate of receipts capable of being classified as Appropriations in Aid - as the result of renegotiating with DHSS the basis on which we charge for collecting National Insurance Contributions. This £m5 can properly be offset against the increase in our cash limit, but it would not, of course, reduce the increase needed in our running costs limit.

Opportunities

11. I have so far dealt with our requirement for a Supplementary arising out of the earlier exchange with Ministers and our agreed operational plans. But if Ministers agree that a Supplementary is in any event required, you may also wish to consider whether this provides an opportunity to take action to help with two of the other major problems facing us.

12. First, there is the problem of our additional bid for 1988-89. We have had some discussion with FP Division on the possible scope, if additional resources were available, for bringing forward some necessary 1988-89 expenditure into the current year. I can confirm that, if it would help, we should be able to bring forward up to £m5, or a little more if it were necessary, in running costs expenditure in this way, provided that an equivalent amount were added to the Supplementary. We would then reduce our PES bid for 1988-89 pro tanto.

13. This would be mainly achieved by the timing of bill payments. To meet the pressure on our running costs in the last year or two we have taken every opportunity to defer payment of bills into the following year where this can properly be done. With more funds this year we could bring back into 1987-88 payments we had been planning on deferring until next year. This would mainly be in areas such as computer maintenance and licence fees, and amounts we pay to HMSO.

14. Second, there is the continuing problem of keeping on top of our increasing workloads - particularly in tax offices now that we no longer have the funds for overtime working that Ministers provided in 1985-86 and 1986-87. By April we were showing a record improvement in the work and in July we published new ambitious targets (for post arrears and open Schedule E Cases). Without overtime I have to say that it looks as though we are slipping back again (though seasonal factors are at work too), and that unless we can inject more resources quickly (either overtime or casual help) the workstate next April may be a good way short of the targets we set. This is particularly worrying, given the need to prepare for independent taxation.

15. As Mr Isaac's minute of 7 July to the Chancellor underlined the changeover to independent taxation will depend on smooth handling by staff in over 600 tax offices. The timetable is already very tight coming so closely on the heels of the changeover to CODA (our computerised system for the self-employed) and planned major enhancements to the COP system. There are risks; but these will be greatly reduced if we can enter the run up to independent taxation with tax offices in the best possible state.

16. This is difficult to quantify but I do believe it is a crucial factor in achieving what the Chancellor wants. A figure for overtime and casuals of £m10 was discussed at Mr Isaac's meeting of 29 July with the Financial Secretary. We should have to handle this very carefully with the main staff association involved, the IRSF, who are currently operating an overtime ban (except for special purposes like the computer projects). But there is no point in tackling the IRSF too firmly on this unless funds are actually available for the staff to work overtime - as they were very happy to do last year in the weeks up to Christmas.

Contingencies

17. If Ministers approve a Supplementary for the Revenue we must do everything possible to live within it, and contain our expenditure within our running costs limit. That said, you will appreciate the difficulties in making a firm forecast of expenditure at this very early point in the year. We have only five full months expenditure to go on, and September figures will not be available until the end of next week. There are a number of pay settlements just implemented or still in the pipeline, where the costs are necessarily estimated at this stage. Wastage and recruitment rates for the remainder of the year may not be as expected. We may be thrown by unexpected demands from PSA. And so on. Even a Supplementary of £m16.7 will leave us with no significant margin for error on present workloads.

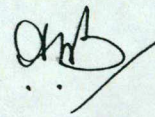
18. Last year, with Ministers' agreement, we used a certain flexibility on capital expenditure to deal with contingencies affecting our running costs. There is less scope for doing so this year with the new rules on virement from capital to current. At present we are planning to spend our capital provision fully. But there are some items timed for the year-end which we could defer into 1988-89 if that proved essential to offset, within the cash limit, unexpected demands on our running costs. Whatever the outcome of this minute it seems only prudent to plan on that basis.

Summary

19. In short, I need to seek your approval for a winter Supplementary estimate to increase our running costs limit by £m16.7 and to increase our cash limit by £m11.7 (after offsetting increased receipts of £m5.0). Over and above that, if you were able to approve a larger Supplementary, we can see ways of bringing forward expenditure of, say, £m5 from 1988-89 (with a

corresponding reduction in our PES bid for that year) and for using additional funds to improve the workstate over the remainder of this year (in the order perhaps of £m10, though that figure must be more tentative).

20. I am, of course, at your disposal if you or the Financial Secretary would like to discuss this more fully.



(A M W BATTISHILL)

Additional Pay Costs

1. Performance linked pay for grades 4-7 (excess over cost of performance bonuses).
2. London Allowance for Valuers.
3. Restructuring of grades in Valuation Office.
4. SPCS deal agreed in September.
5. Possible extension of SPCS deal to IRSF grades.
6. London Weighting (excess over 4.25%).



Inland Revenue

Policy Division
Somerset House

FROM: MISS R A DYALL
DATE: 6 NOVEMBER 1987

W4279

1. MR ISAAC *Seen in draft*

BAMace 6/11

2. FINANCIAL SECRETARY

INDEPENDENT TAXATION: SEX DISCRIMINATION IN THE TAX SYSTEM

1. This note considers the question of sex discrimination in the tax system and the action you might take to eliminate it in the context of Independent Taxation.

2. The Green Paper described the Government's approach to personal income tax as "founded on two principles: that the tax system should recognise the fact of marriage and the responsibilities that go with it; and that the system should recognise the independence and equal standing of the husband and wife within marriage". Independent Taxation will remove much of the inequality of treatment between married men and women. Husband and wife will be treated as independent taxpayers each having the same basic allowance, which can be set against any type of income, and their own set of rate bands. Each will have responsibility for returning their own income and meeting the tax liability on it. For the first time married women as well as married men will be eligible for age allowance.

cc Chancellor
Chief Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Mr Cassell
Mr Scholar
Miss Sinclair
Mr Cropper
Mr Tyrie
Mr Jenkins (Parliamentary
Counsel)

Mr Isaac
Mr Painter
Mr Lewis
Mr Beighton
Mr Matheson
Mr Cleave
Mr Mace
Mr Eason
Mr O'Brien
Mr J C Jones
Mr Yard
Mr Allen
Mr Munro

Mr Bousher
Mr Boyce
Miss Dyall
PS/IR

The married couple's allowance

3. There is one important and fundamental respect in which married men and women will not be treated equally under Independent Taxation. The married couple's allowance which you are proposing to introduce in place of the married man's allowance will always go to the husband rather than the wife where he has income to set it against. The wife can claim the allowance only to the extent that her husband is unable to use it, and then only with his consent. These rules are sex discriminatory in that they do not allow married men and women equal access to the allowance.

4. The married couple's allowance makes Independent Taxation very different in this respect from the system of independent taxation with transferable allowances described in the Green Paper, which would have treated married men and women equally. In these circumstances you will need to be cautious in presenting sex equality as a theme of the reforms. Nevertheless you may like to consider whether it would be appropriate to take action in some specific areas.

Interpretation Act

5. In practice, leaving aside the married couple's allowance, the problem of sex discrimination in the tax system is a relatively minor one, although it can of course arouse very strong feelings, particularly among women's organisations. The Interpretation Act 1978 allows references to the male to include the female in legislation passed after 1850 and references to the female to include the male for legislation since 1978, except where the contrary intention appears. In recent years legislation tends to have been drafted in more neutral terms, making it more obvious that it applies to both male and female.

Provisions proposed for abolition

6. Apart from the wife's earned income allowance, which will disappear under Independent Taxation there are a number of

discriminatory reliefs and allowances which we have already recommended should be abolished on other grounds. The additional personal allowance for married men with wholly incapacitated wives is not available to married women in similar circumstances, (my note of 8 October on the additional personal allowance). The dependent relative allowance is discriminatory both in having a higher rate for single women and in treating mothers and mothers-in-law more favourably than fathers and fathers-in-law, (Mr Payne's note of 9 October on the minor personal allowances). The mortgage interest and capital gains tax relief on homes purchased for dependent relatives reflect the same discriminatory definition of "dependent relative". This discrimination strengthens the case for abolishing these provisions, (although whether you would want to make the point presentationally depends on how far you decide to go in eliminating sex discrimination in other areas). If these allowances and reliefs were retained you might come under pressure to extend their scope (in order to remove the sex discrimination) even though they are already anomalous.

Widow's Bereavement Allowance

7. A more important example of a discriminatory allowance is the widow's bereavement allowance (WBA) which is available to a widow in the tax year of her husband's death and the following year. The WBA is equal to the difference between the single and married man's allowances so that, when added to the widow's single allowance gives her relief equivalent to the married man's allowance against income arising after her husband's death in the year of bereavement, and the following year.

8. The Green Paper left the future of WBA under transferable allowances open, but suggested it might be continued or even increased to the level of the basic single allowance. We see no case for increasing the level of the allowance under Independent

Taxation. Although the married man's allowance is to be abolished the amount of the WBA can be directly linked to the married couple's allowance. However, the response to the Green Paper revealed some support for extending the WBA to widowers, so that widows and widowers would be treated on an equal basis, (see Annex A).

Background

9. WBA was introduced (for the year of bereavement only) in 1980. A concession to widows of this kind (though not founded on any logical fiscal principle) was thought to be appropriate, while stopping short of the more extreme demands of the widows' organisations (for example for exemption from tax of widows' pensions). There has always been ready public sympathy for widows and the allowance was presented as recognising the special problems, both emotional and financial, facing a widow in the difficult period following her husband's death. It also had the practical advantage of reducing the likelihood of a widow building up an underpayment of tax because she failed to notify her tax office of the her change of circumstances and new sources of income (such as social security benefits or a pension from her husband's employer). The allowance was extended to the year following bereavement in 1983.

10. Extension of WBA to widowers was resisted on the grounds that it is usually the loss of the husband's income which is the cause of any financial problems on bereavement. Nevertheless although the husband's income will still normally be the larger, the wife's income may also be important to the couple's joint finances now that so many married women go out to work, and on retirement are increasingly receiving pensions in their own right. Unlike a widow, a widower receives no social security allowance or pension following bereavement, although he may qualify for one parent benefit (currently £4.70 per week) if he has children. As yet few occupational pension schemes provide for a widower's pension on the death of a married woman contributor. Yet a widower, like a widow, may face increased expenses, for example in having his children looked after, or help in the house, while he is working.

11. A good case can be made out along these lines for extending WBA to widowers, while the arguments in favour of restriction to widows only look increasingly thin. An even-handed approach would be attractive and there is some support for it, not least among women's organisations. On the other hand the pressure for change is not great and could be resisted. People do not have the same perception of the widower's position, difficult though it may be. There is also the possibility that, if the WBA were extended to widowers, an unfortunate contrast might be drawn with the married couple's allowance, (on the lines that the Government had taken action to deal with discrimination in the system against men but not the greater discrimination against women). We suggest that it is very much a matter for Ministers' judgment whether to take action on this or leave things as they are. Annex B sets out the allowances available to husband and wife, widower and widow, in the year of bereavement, if WBA were extended to widowers. The revenue cost would be about £20m and there would be a small staff cost of the order of 15-20 units.

Timing

12. If you find the proposal attractive in principle two options are open to you as regards timing. In our view the change fits most naturally in the context of independent Taxation which, although it does not achieve full equality of treatment between married men and women, goes a long way towards it. However, if you legislated in 1988 for extension in 1990/91 you could come under pressure for earlier implementation. There are operational reasons why implementation of the Independent Taxation cannot be earlier but these do not apply to the extension of WBA.

13. Since extension of WBA to widowers would be a relatively free-standing measure it could be legislated in 1988 and (subject to confirmation on the operational implications) take effect for the 1988-89 tax year. This timing would coincide with the abolition of the minor personal allowances and you would need to take a view on whether this would be helpful or unhelpful. On the

Annex B

one hand it would counterbalance the withdrawal of some reliefs by the extension of another (although the benefit would go to different people). On the other, it might provoke more criticism of the abolition of the minor personal allowances.

14. A final decision on this proposal could be left until nearer the Budget. However, it would be helpful to have your preliminary view now so that we can instruct Parliamentary Counsel on a contingency basis if necessary. It would be easier to have a provision drafted which could subsequently be dropped than to wait until February or March when the pressure of work on his office is greater.

Approval of occupational pension schemes

15. There is one further small change which you might like to consider in this context concerning tax approval for occupational pension schemes. Section 19 FA 1970 requires us to approve pension schemes if their rules satisfy certain, very restrictive, conditions. As drafted, the legislation permits schemes which provide benefits for widows but not widowers. This does not give rise to difficulties in practice, since virtually all schemes opt for discretionary approval - which is much more flexible - under Section 20 FA 1970. We would not raise the point in isolation, but, since we shall be legislating anyway, there may be some advantage in tidying up Section 19 - the amendment, which would not be controversial, would necessitate a line or two in the schedule of amendments consequential to Independent Taxation.

Conclusion

16. The questions for decision are

- i. Do you wish to extend the widow's bereavement allowance to widowers (paragraph 11)?

ii. If so, do you wish to

a. legislate in 1988 for implementation in 1990-91
(paragraph 12);

✓ b. legislate in 1988 for implementation in 1988-89
(paragraph 13)?

✓ iii. Are you content to make the minor amendment suggested in
the pensions legislation (paragraph 15)?

Robin Dyall

MISS R A DYALL

WIDOW'S BEREAVEMENT ALLOWANCE: RESPONSE TO THE GREEN PAPER ON THE REFORM OF PERSONAL TAXATION

The response to the Green Paper indicated a limited measure of support for extending WBA to widowers. Six organisations, all but one of those commenting on the section in the Green Paper on widows, raised the issue, but only one of the 400 individuals responding mentioned it. The organisations were:-

National Federation of the Self-Employed (NFSE)
National Council of Women of Great Britain (NCWGB)
Institute of Taxation (IOT)
Institute to Chartered Accountants, Scotland (ICA(S))
Women in Management (WIM)
Law Society (Scotland)

Five of the six merely drew implicitly or explicitly on the principle of sex equality. Only the IOT examined the likely scenarios in practice.

NFSE: simply commented "we can see no reason why the bereavement allowance should be restricted to widows and call for the inclusion of widowers"

NCWGB: likewise, proposed extension to widowers without giving any particular reason.

IOT: - Pointed to double discrimination against widowers - in both social security and tax.

- Pointed out WBA is a recent development - the implication presumably being that one cannot explain the sex discrimination on the basis that it is a provision from a bygone era.

- said some widowers do face financial difficulties in three ways

(a) where children are present, there may be increased expenses as a single parent;

(b) where wife worked, there will be a drop in income;

(c) unlike a widow, the widower will be unlikely to get a pension based on wife's former employment.

NB The IOT also brought up the point of sex-discrimination in the definition of "dependent relative" - they did not say whether they had in mind DRA, MIR or CGT.

ICAS: Said "if the objective of the Green Paper is to give equal treatment for men and women, the present inequality for widowers cannot be allowed to continue".

ICAS also pointed to dependent relative sex-discrimination.

WIM: Simply said WBA should be extended to widowers
Pointed to sex-discrimination in DRA single woman rate.

Law Society (Scotland): criticised unequal treatment of widowers on grounds of "fairness".

ANNEX B

This annex shows the allowances available (in 1987-88 terms) in the year of the bereavement and the following year if WBA were extended to widowers under Independent Taxation.

	Year of Bereavement		Following Year
<u>Widow</u>			
	Single allowance	£2,425	£2,425
Self:	WBA	£1,370	£1,370
Late Husband:	Single allowance	£2,425	
	MCA	£1,370	
<u>Widower</u>			
Self:	Single allowance	£2,425	£2,425
	MCA	£1,370	
	WBA	£1,370	£1,370
Late wife:	Single allowance	£2,425	

While the widower would have £1,370 more than the widow to set against his own income that year (because of MCA), the widow's spouse would have had the benefit of £1,370 more than the widower's spouse. The couples' aggregate allowances would thus be equal.

In the special case where a widow was bereaved before her husband's income had reached the level of the single allowance + MCA, she would be entitled to any unused part of the MCA, so there would also be parity of treatment between widows in this category and their male counterparts.



INLAND REVENUE
STATISTICS DIVISION
SOMERSET HOUSE

FROM: R J EASON

DATE: 4 FEBRUARY 1988

*Thanks - 15
Release - 15
Budget - 15
Pensions - 15*

copy no 1 of 38

CHANCELLOR OF THE EXCHEQUER

INCOME TAX - OPTION 3

1. As requested at the overview meeting on 1 February, I
... attach a table showing the real increases since 1978-79 in
the main personal allowances if Option 3 were introduced in
1988-89. Real increases are calculated by reference to the
forecast change in the RPI over the appropriate financial
years.

cc. Principal Private Secretary
Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Sir T Burns
Sir G Littler
Mr J Anson
Sir A Wilson
Mr I Byatt
Mr M C Scholar
Mr R Culpin
Mr P Sedgwick
Mr J Odling-Smee
Miss C Evans
Mr A Hudson
Mr P McIntyre
Mr P Cropper
Mr A Tyrie
Mr M Call
Miss C E C Sinclair
Mr C J Riley
Mr Unwin (Customs & Excise)
Mr Knox (" & ")

Chairman
Mr Isaac
Mr Painter
Mr Beighton
Mr Calder
Mr Lewis
Mr Mace
Mr Cayley
Mr Eason
Mr Ko
Miss White
PS/IR

2. The table also shows changes to the first higher rate threshold (in terms of taxable income) and to the starting point for higher rate tax for married men and for single people, taking account of allowances. Real increases up to 1987-88 are given for comparison.

3. The main conclusions are that, under Option 3, both the married man's allowance and the single allowance would be, in real terms, over 25% or a quarter higher than they were in 1978-79. And the starting point for higher rate tax would be about 20 per cent higher for both married and single people.

4. The changes between 1987-88 and 1988-89 under Option 3 are not equal to the extra increase in allowances of 3.7%, because of statutory rounding and because the real increases are calculated from financial year averages of the RPI. For 1988-89, the growth in the RPI over 1987-88 is currently forecast to be 4.5%.



R J EASON

BUDGET SECRET - TASK FORCE LIST

REAL⁽¹⁾ INCREASES IN PERSONAL ALLOWANCES
AND FIRST HIGHER RATE THRESHOLD
SINCE 1978-79

	to 1987-88 %	to 1988-89 under Option 3 %
Single and wife's earned income allowance	22.6	26.1
Married man's allowance	23.1	27.2
Additional personal allowance	24.1	29.1
Aged single allowance		
65-79	13.4	16.6
80 and over	17.6	21.4
Aged married allowance		
65-79	12.2	15.7
80 and over	16.3	19.6
Aged income limit	22.0	26.3
Higher rate threshold	11.4	19.2
Starting point for higher rate tax		
- married man	13.3	20.5
- single	12.7	19.9

(1) Based on changes in the RPI for financial years.

? taxable man,
or gross man?