

• PO-CH/NL/0365 PT A

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PART A

1988 BUDGET FINANCIAL
SECTOR BORROWING
REQUIREMENTS

NL/0365

PO -CH

PART A

D's 25 years NAG's 30/11/95

26-2-88

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CLASSIFIED BY:

PART B

FSBR. PAPERS 1988.

PART. A.

S

305-

COPY NO 1 OF 30

FROM: MISS C E C SINCLAIR
DATE: 15 February 1988

CHANCELLOR

- cc Chief Secretary
- Financial Secretary
- Paymaster General
- Economic Secretary
- Sir P Middleton
- Sir T Burns
- Sir G Littler
- Mr Anson
- Sir A Wilson
- Mr Byatt
- Mr Scholar
- Mr Culpin
- Mr Sedgwick
- Mr Odling-Smee
- Mr Riley
- Miss Evans
- Mr A Hudson
- Mr Cropper
- Mr Tyrie
- Mr Call

- Mr Battishill)
- Mr Isaac) - IR
- Mr Painter)
- Mr Calder)
- Mr Unwin)
- Mr Knox)
- Mr P R H Allen) - C&E
- Mrs Hamill)

yes. as stated
@ Unwin
yes

Ch.
 Agree with Miss Sinclair's
 advice that we follow last
 year's model?

25 15/2

a
 Agreed @ Overview
 - detailed description
 A means clearly need
 a lot more work
MA

FSBR CHAPTER 4, TABLE 4.1

Mr Culpin's minute of 11 February told you of the work which is in hand on the behavioural effects of Budget measures. Since this work is not complete, we cannot yet advise you on what to publish in Chapter 4 of the FSBR; but we hope to be in a position to do this when we submit the first draft of that Chapter on 22 February.

2. Meanwhile, as a separate point, it would be most helpful to have an early view on the number of columns/years to be shown in Table 4.1 of the FSBR (there is a knock-on as well to Table 1.1).

3. There are three options:

- (i) to show two years, as last year, with the first year measured against both an unindexed and an indexed base; and the second year against an indexed base only;
- (ii) to show three years, thus including the first year cost of independent taxation - if the first year were measured against both bases, the Table would have four columns instead of the present three;
- (iii) to show four years, thus including the first and second year costs of independent taxation - this would produce five columns if we continued to show first year costs measured against an unindexed base.

4. Now that independent taxation is the only major change which will not come into effect until 1990-91, the case for going beyond the first and second years for all the Budget measures does not look strong. We changed the presentation of Table 4.1 both in 1986 and 1987, and although this aroused little or no comment, too much chopping and changing may do so. If the Table were to follow last year's pattern, independent taxation would appear as a line in the Table, but the cost in 1990-91 and 1991-92 would be shown in the notes to the Table (as would full year costs for other measures where these can be estimated and are likely to be substantially different from the effect in the first or second years).

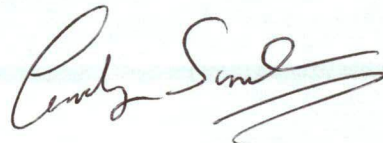
5. The argument for a three year approach is that it would allow the first year cost of independent taxation to be seen readily in relation to the third year costs of the rest of the package. Against that, the first year cost by itself is fairly misleading as a guide to the eventual cost of independent taxation. A three year approach, even with the third year measured against an indexed base, would inflate the cost of some measures, such as the income tax reductions, because earnings are forecast rise faster than

prices. Moreover, having moved to a three year presentation (because of one measure in the 1988 Budget), you might find it hard to revert to two years in future.

6. These problems all look worse with a four year approach. While this would have the advantage of showing the second year cost for independent taxation, the fourth year total would not be a proxy for the full year costs of the Budget package; yet it would look large. A four year approach would either involve a five column table - which seems unmanageable; or a further Table showing the costs of indexation. These have always been shown, one way or another, in the FSBR and to drop them altogether might arouse comment. But at this point Chapter 4, which we tried to streamline and improve in 1986, would start to become a bit cumbersome against.

7. Our view is that the arguments point firmly to following last year's model, showing first year costs measured against both bases, and second year costs against an indexed base only. We would be grateful to know if you agree. I am submitting separately (Chancellor only) mock ups of both a two year and a four year presentation.

8. Table 1.1 is normally a condensed version of Table 4.1. We presume that you will want to show the same number of columns in the two tables, although with a four-year presentation in Table 4.1, it would still be possible to show the usual two year presentation in Table 1.1.



CAROLYN SINCLAIR



FROM: A P HUDSON

DATE: 15 February 1988

MISS SINCLAIR

cc Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Scholar
Mr Culpin
Mr Odling-Smee
Mr R I G Allen
Mr Pickford
Mr Cropper
Mr Tyrie
Mr Call
Mr Mace - IR
PS/IR

FSBR CHAPTER 4: INDEPENDENT TAXATION

For the record, the Chancellor said, in the course of a discussion about Budget Day pamphlets, that he thought there was a strong case for including a section on Independent Taxation in Chapter 4 of the FSBR, setting out a clear summary account of the reform in reasonable detail. Please could you include something in the next draft, for him to look at?

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

A P HUDSON

Hudson
15/2

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COPY NO 1 OF 1

FROM: MISS C E C SINCLAIR
DATE: 15 February 1988

CHANCELLOR

FSBR CHAPTER 4: TABLE 4.1

In my separate note of today's date, I said I would submit mock ups (covering the main Budget measures only) of Table 4.1 on a two year basis (as last year), and on a four year basis. These are attached.



CAROLYN SINCLAIR

B.L.O.

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Table 4.1 Direct effects of changes in taxation

Proposal Number	Proposal	£ million		
		Estimated effect on receipts in: 1988-89	1989-90	Changes from an indexed base
1	Excise Duties	+550	Nil	-35
2	Double indexation of main personal allowances	-1390	-690	-940
3	Reduce basic rate of IT to 25p	-2500	-2500	-3100
4	Increase higher rate IT threshold to £20,000	-300	-220	-420
5	Abolish higher rates of IT above 40p	-835	-780	1670
6	Independent taxation from 1990-91	Nil	Nil	Nil
7	Freeze £6,600 CGT exemption, add remaining gains to income and tax at IT rates (25%/40%)	+70	+70	+80
8	Rebase CGT to 1982 - CGT for individuals and trusts - CT on companies gains	Nil -Neg	Nil -Neg	-70 -210
9	Restrict MIR to residence basis from 1.8.88 and leave ceiling unchanged at £30,000	+5	+5	+20
10	Abolish tax relief on home improvement loans	+80	+80	+200
11	Abolish tax relief on new covenants between individuals; change rules for maintenance payments	+35	+35	+100
12	Increase car scales by 100 per cent in 1988-89 and by 10 per cent in 1989-90	+220	+220	+315
13	Reduce small companies' CT rate to 25p in 1988-89	-Neg	-Neg	-50
14	Reduce life assurance premium relief to 12.5 p	Nil	Nil	+70
15	Raise IHT threshold to £107,000 and single rate of 40%	-145	-120	-255
16	Minor starters	+40	+40	+35
TOTAL TAX MEASURES		-4170	-3860	-5930

Based on Table 1 of Budget Scorecard for 8 February Overview Meeting. This table would need to be supplemented by the following note in the Annex to Chapter 4:

Illustrative note 6 (Independent taxation)

[Detail of change to independent taxation.] The changes will be introduced in 1990-91. The direct revenue effects will be:

	1990-91	1991-92
Income tax	-xxx	-xxx
Capital gains tax	Nil	-xxx

These costs include [description of any behavioural effect allowed for].

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Table 4.1 Direct effects of changes in taxation

	Changes from an indexed base			£ million
	Estimated effect on receipts in:			
	1988-89	1989-90	1990-91	1991-92
1 Excise Duties	Nil	-35	-80	-155
2 Double indexation of main personal allowances	-690	-940	-1000	-1040
3 Reduce basic rate of IT to 25p	-2500	-3100	-3250	-3550
4 Increase higher rate IT threshold to £20,000	-220	-420	-490	-550
5 Abolish higher rates of IT above 40p	-780	-1670	-1900	-2170
6 Independent taxation from 1990-91	Nil	Nil	-560	-900
7 Freeze £6,600 CGT exemption, add remaining gains to income and tax at IT rates (25%/40%)	+70	+80	+100	+140
8 Rebase CGT to 1982				
- CGT for individuals and trusts	Nil	-70	-170	-210
- CT on companies gains	-Neg	-210	-440	-540
9 Restrict MIR to residence basis from 1.8.88 and leave ceiling unchanged at £30,000	+5	+20	+40	+50
10 Abolish tax relief on home improvement loans	+80	+200	+300	+400
11 Abolish tax relief on new covenants between individuals; change rules for maintenance payments	+35	+100	+160	+175
12 Increase car scales by 100 per cent in 1988-89 and by 10 per cent in 1989-90	+220	+315	+335	+345
13 Reduce small companies' CT rate to 25p in 1988-89	-Neg	-50	-90	-90
14 Reduce life assurance premium relief to 12.5 p	Nil	+70	+60	+55
15 Raise IHT threshold to £107,000 and single rate of 40%	-120	-255	-300	-330
16 Minor starters	+40	+35	+20	+15
TOTAL TAX MEASURES	-3860	-5930	-7265	-8355

* Annex based on Table 1 of Budget Scorecard for 8 February Overview Meeting. This table would need to be supplemented by a further table in the Annex to Chapter 4 showing the costs of indexation, a mock-up of which is shown in Annex Ci overleaf.

A. Taxes subject to statutory indexation : The table below shows the direct revenue effects in 1988-89 and 1989-90 of indexing the income tax main allowances and thresholds, the capital gains tax exempt amount and the inheritance tax thresholds and bands to 1988-89 levels by 3.7 per cent, the increase in the RPI over the year to December 1987.

	£ million	

	Estimated effect on receipts in	
	1988-89	1989-90

Income tax allowances and thresholds	-835	[-1370]
Of which:		
Increases in main personal allowances	-700	[-1080]
Increase in the basic rate limit*	-80	[-160]
Increases in further higher rate thresholds*	-55	[-130]
Inheritance tax thresholds and bands	-25	[-60]
Capital gains exempt amounts	Nil	[-10]

* Additional costs after previous changes have been introduced.

B. The table below shows the direct revenue effects in 1988-89 and 1989-90 of indexing the excise duties first by reference to the increase of 3.7 per cent in the RPI over the year to December 1987.

	£ million	

	Estimated effect on receipts in	
	1988-89	1989-90

Beer, cider and perry	+60	[+75]
Wine	+20	[+25]
Spirits	+25	[+25]
Tobacco	+100	[+115]
Petrol	+195	[+225]
Derv	+50	[+55]
VED	+100	[+105]
Minor duties	+5	[+5]
Bus fuel grants	-5	[-5]
Total	+550	[+625]

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COPY NO 31 OF 31

FROM: J M G TAYLOR

DATE: 16 February 1988

MISS SINCLAIR

cc PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Anson
Sir A Wilson
Mr Byatt
Mr Scholar
Mr Culpin
Mr Sedgwick
Mr Odling-Smee
Mr Riley
Miss Evans
Mr A Hudson
Mr Cropper
Mr Tyrie
Mr Call

Mr Battishill - IR
Mr Isaac -IR
Mr Painter - IR
Mr Calder -IR

Mr Unwin -C&E
Mr Knox - C&E
Mr P R H Allen - C&E
Mrs Hamill - C&E

FSBR CHAPTER 4, TABLE 4.1

The Chancellor has seen your minute of 15 February. He agrees with your advice that table 4.1 of the FSBR should follow last year's model (as stated at Overview, yesterday).

A handwritten signature in dark ink, appearing to be 'J M G Taylor'.

J M G TAYLOR

BUDGET CONFIDENTIAL

From: J ODLING-SMEE

17th February 1988

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
 Sir Peter Middleton
 Sir Terence Burns
 Mr Anson
 Mr Monck
 Mr Scholar
 Mr Culpin
 Mr Turnbull
 Ms Sinclair
 Ms Evans

*OK as in
 reply to
 ACSA.*

*Ch. - Agree with Mr O-S's
 recommendations (para 7, below)?*

25/17/2

TREATMENT OF EXPENDITURE MEASURES IN FSBR

There are two expenditure measures, on student grants and forestry, both of which are linked with the removal of tax reliefs. It would be helpful if you could indicate how you would like them to be treated in the FSBR so that we can take account of your views in the first drafts of Chapters 1, 4 and 5 which you will receive next week.

2. This minute assumes that you will want to announce them in the Budget Statement and hence they will be recorded as Budget measures. It would be difficult not to treat them as such: it would probably require an announcement before the Budget which would be damaging given the sensitivity of the tax measures involved.

Precedents

3. Apart from the increases in the Reserve in the 1985 FSBR and adjustments to the planning total because of NIS reduction and abolition in the 1983 and 1984 FSBRs, there have been three recent Budgets which included expenditure measures: 1983, 1985 and 1986. The treatment then was as follows:

	1983	1985	1986
First year cost (net) (£m)	238	75	100
Increase in planning total or charged to Reserve?	Charged to Reserve	Increase in planning total	Charged to Reserve
Treatment in Table 1.1	Not shown	Shown separately Added to tax measures to show "total direct effects" of Budget	Shown separately Not added to tax measures, implying that only tax measures cost money

Table 1.1 from the 1985 and 1986 FS8Rs is attached. In all three years the measures were described, with numbers, in Chapter 5 (Chapter 4 in 1983).

The 1988 Measures

4. On current figures the public expenditure cost of the 1988 measures rises steadily from £25m in 1988-89 (all student grants) to £65m in 1989-90 and £120m (of which roughly £10m is forestry) in 1991-92. This is small relative to total public expenditure and is considerably smaller than the cost of the measures in 1983, 1985 and 1986. Although the 1988-89 planning total is very tight, the amount involved in that year is not large enough to justify a formal increase in the planning total; and in the later years the amounts can be taken into account in the Survey. We therefore recommend that it should be charged to the Reserve and not added to the planning total.

5. The presentation of these costs in the FSBR will need to be consistent with the Chief Secretary's statement that there will be no new expenditure measures in the Budget. This means that they must be shown as consequential elements of the relevant tax measures, as indeed they are. Specifically:

a. No specific mention need be made in the text of Chapter 1. Table 1.1 should have a sub-total (in bold type) for the tax proposals, with these items included below it (perhaps in a single line) as "expenditure changes related to tax proposals", with a footnote indicating the tax measures to which they relate. They could be in plain type, and not be added to the tax total, so that they would appear as consequential elements rather than Budget measures in their own right.

b. In Chapter 4, which deals with the Budget tax proposals, the offsetting expenditure changes should be mentioned in the text of the paragraphs dealing with the relevant tax measures. They should not be incorporated in the detailed costing of the individual tax measures in Table 4.1, but there is a choice about whether to give figures in the text. Whether or not to do so probably hinges on the way in which you wish to deal with it in the Budget statement. If you give figures there, it might make sense also to do so in Chapter 4.

c. The expenditure changes, with figures, should be mentioned in Chapter 5, indicating that they are charged to the Reserve, and that they relate directly to the specific tax measures mentioned earlier in the FSBR, cross-referencing to the relevant paragraphs in Chapter 4.

6. The numbers for expenditure on forestry and student grants and the associated tax measures in Table 4.1 will not match exactly, but this can be easily explained away (if pressed later, not suitable for the FSBR). Some recipients of covenant relief are not students; and the increased level of forestry grant broadly reflects the cost of the previous tax regime at pre-Budget rates of income tax.

Do we have to split them out separately. Could we not just have "Budget measures" with footnotes saying include consequential PX increases? (see attached)

Summary

7. Do you agree that:

a. the expenditure changes should be charged to the Reserve?

b. they should be shown in the FSBR as indicated in paragraph 5 above?

Do-s

J ODLING-SMEE

Table
Could have
Change
Change
Change

1985 FSBR

1. The Budget Proposals

Definition of the Budget

1.01 The main proposals in the Budget are summarised in Table 1.1 below and described in detail in Parts 4 and 5. The Budget is defined to include tax changes and changes to national insurance contributions announced in the Budget Speech, together with certain other tax changes which have been announced since last year's Budget. It also includes the expenditure consequences of new measures announced in the Budget Speech for the plans set out in the Public Expenditure White Paper (Cmnd. 9428).

Table 1.1 Budget measures: direct effects on public sector transactions⁽¹⁾

	£ million at current prices			
	Effect in 1985-86		Effect in a full year ⁽²⁾	
	Changes from an indexed base	Changes from a non-indexed base	Changes from an indexed base	Changes from a non-indexed base
Tax proposals⁽³⁾				
Income tax allowances and thresholds	-730	-1 590	-910	-2 025
Capital taxes	-20	-30	-215	-260
VED	+130	+230	+130	+230
Other Excise duties ⁽⁴⁾	+105	+590	+110	+605
VAT	+60	+60	+190	+190
Other tax changes	-40	-40	+235	+235
Total tax proposals	-495	-780	-460	-1 025
Proposed changes in National Insurance Contributions				
Employers' NICs	-30	-30	-80	-80
Employees' NICs	-100	-100	-270	-270
Self employed etc. NICs	-30	-30	-100	-100
Total NICs proposals	-160	-160	-450	-450
Expenditure Measures⁽⁵⁾				
Youth Training Scheme	Nil	Nil	-150	-150
Community Programme	-75	-75	-250	-250
Total Expenditure measures	-75	-75	-400	-400
Total Direct Effects⁽⁶⁾	-730	-1 015	-1 310	-1 875

⁽¹⁾ +/- indicates an increase/decrease in revenue, or a decrease/increase in expenditure. All figures are rounded to the nearest £5 million.

⁽²⁾ See footnote (a) to Table 4.2.

⁽³⁾ The figures are estimates of the direct effects of the tax proposals on public sector transactions. They are not estimates of the total effects, both direct and indirect. See footnote (a) to Table 4.2.

⁽⁴⁾ Including bus fuel grants.

⁽⁵⁾ The figures show the direct expenditure consequences of these measures after allowing for consequential savings in unemployment and supplementary benefits as people who would otherwise be claiming benefit join the schemes. The figures shown in the full year columns are estimates of the cost in 1987-88.

⁽⁶⁾ Since these are estimates of direct effects the overall total differs from the effect of these measures on the PSBR—which is shown in paragraph 1.05.

1986 FSBR

Table 1.1 The Budget measures¹

	£ million		yield(+)/cost(-)
	1986-87		1987-88
	Changes from an indexed base	Changes from a non-indexed base	Changes from a non-indexed base
Tax proposals:			
Income tax basic rate ²	-950	-950	-1 305
Income tax allowances and thresholds	+15	-1 125	-1 470
Excise duties			
—petrol/derv	+135	+465	+495
—vehicle excise duty	-135	+5	+5
—tobacco	+175	+315	+335
—alcohol	-175	—	—
—gas oil	+25	+30	+30
—other minor oil duties	-25	-20	-20
Stamp duties			
—reduction in rate	-70	-70	-75
—extension of base	+70	+70	+85
Capital transfer tax (inheritance tax)	-35	-55	-100
Charities			
—package of reliefs	-10	-10	-70
—anti abuse measures	* ³	*	+20
Pension fund surplus rules	+20	+20	+120
Other tax changes	-25	-25	+65
Total tax measures	-985	-1 350	-1 885
Expenditure measures:			
			cost(+)/saving(-)
Counselling initiative and Jobstart allowance	+100	+100	+70
Community Programme	+60	+60	+120
New Workers Scheme	+25	+25	+50
Enterprise Allowance Scheme	+5	+5	+35
Loan Guarantee Scheme	*	*	+5
Total expenditure measures (gross)⁴	+195	+195	+290
Offsetting savings in social security benefits	-95	-95	-125
Net call on the Reserve	+100	+100	+165

¹ These measures, and the basis of the costings shown, are described in detail in Chapters 4 and 5.

³ Negligible.

² Figures include the effect of the consequential change in the rate of advance corporation tax.

⁴ Including Northern Ireland consequentials.

Very sneaky presentation.

Table 1.1 The Budget measures¹

	£ million		yield(+)/cost(-)
	1987-88	1988-89	1988-89
	Changes from a non-indexed base	Changes from an indexed base	Changes from an indexed base
Tax proposals			
Income tax			
basic rate ²	-2 200	-2 200	-2 820
personal allowances	-705	-10	-10
higher rate thresholds	-65	+40	+80
<i>covenants & maintenance³</i>	<i>a</i>	<i>b</i>	<i>c</i>
Excise duties			
oils	—	-240	-265
vehicle excise duty	+5	-90	-90
tobacco	—	-105	-110
alcohol	—	-105	-120
on-course betting duty	-20	-20	-20
gaming machine licence duty	+20	+20	+20
VAT			
partial exemption rules	+300	+300	+400
small business package	-115	-115	-60
other	-5	-5	+20
Inheritance tax	-90	-75	-170
Corporation tax			
small companies' rate	*	*	-45
capital gains	*	*	+60
dual resident companies	*	*	+125
payment dates	*	*	+100
Profit-related pay	*	*	-50
Pensions	*	*	-65
Other changes	-20	-20	+75
Total	-2 895	-2 625	-2 945

¹ These measures and the basis of the costings shown, are described in detail in Chapter 4.

* = Negligible. — = nil.

² Figures include the effect of the consequential change in the rate of advance corporation tax.

³ Figures are net of consequential increases in public expenditure.

BUDGET CONFIDENTIAL



FROM: A C S ALLAN
DATE: 18 February 1988

MR ODLING-SMEE

cc Chief Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Monck
Mr Scholar
Mr Culpin
Mr Turnbull
Miss Sinclair
Miss C Evans

TREATMENT OF EXPENDITURE MEASURES IN FSBR

The Chancellor was grateful for your minute of 17 February. He agrees that the expenditure changes should be charged to the Reserves. And he is generally content with your recommendations about how they should be shown in the FSBR.

2. However, he feels that an alternative presentation in table 1.1 should be used. This would be retain the title 'The Budget Measures', but would delete the side-heading 'Tax Proposals', and would not have a separate side-heading for 'Expenditure Measures'. Instead, the figures for covenants and maintenance and for forestry would be shown net, with a footnote on the lines 'Figures are net of consequential increases in public expenditure'. The group^{ing} of the various items in table 1.1 has, of course, yet to be decided.

A handwritten signature in black ink, appearing to read 'ACSA', with a horizontal line underneath.

A C S ALLAN



COPY NO. 15 OF 16

NOTE OF A MEETING IN THE CHANCELLOR'S ROOM HM TREASURY
AT 11.15AM ON FRIDAY 19 FEBRUARY

Present: Chancellor
Chief Secretary
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Odling-Smee
Mr Turnbull
Mr R I G Allen
Mr Mowl
Mr Ritchie
Mr Tyrie

PSBR IN 1987-88 AND 1988-89

The Chancellor said he was inclined to publish figures of -£2.9 billion for the PSBR in 1987-88 and -£3.1 billion for 1988-89, both rounding to -£3 billion. There were large margins of error, and the consequences of an overshoot were more serious than the consequences of an undershoot, so it made sense to be cautious. It appeared that publishing a PSBR of -£2.9 billion for 1987-88 would not present any great difficulties. The position was harder for 1988-89; but, for example, we could use a \$15 oil price assumption, and there was some scope for increasing the forecast for interest and other receipts. A PSBR of -£3 billion was consistent with an unchanged non-oil tax burden; while it was not necessary to show a fall in the tax burden next year, it would be highly undesirable to show an increase. The Chancellor said he would therefore be grateful for advice on how a published PSBR of -£3 billion for 1988-89 might be achieved.

2. Sir T Burns commented that, so long as we were prepared to say that we had been reasonably cautious in our estimates, this should be possible and defensible.

Distribution: Those present.

ACSA
A C S ALLAN

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COPY NO. 1 OF 16 COPIES

FROM: P N SEDGWICK
DATE: 18 FEBRUARY 1988

CHANCELLOR

cc Chief Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Odling-Smee
Mr S Davies
Mr Mowl
Ms C Evans
Mr Ritchie
Ms Turk
Mr Cropper
Mr Tyrie

Mr Turnbull)
Mrs R Butler) Sections 1a
Mr Gieve) and 1c
Mr Richardson)
Mr Franklin)
Mrs Todd)

Mr Calder I/R)
Mr R Allen C & E) Sections 1a
and d only

THE PSBR IN 1987-88 AND 1988-89

The attached note by Colin Mowl, Allen Ritchie, and me presents the latest forecast for the PSBR in 1987-88 and in 1988-89 taking account of the latest package, and assesses what numbers to publish in the PSBR. We need guidance on the latter in order to prepare the figuring for Chapter 6.

You will receive on Wednesday February 24 a first draft of Chapter 6 that will incorporate detailed figures consistent with your provisional decisions on the PSBR. There will be a final submission from us on PSBR prospects on Wednesday March 9 by which time the February PSBR will be available. It will be possible to make further changes to the PSBR figuring at that stage if necessary.

P.N.S.
P N SEDGWICK

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up 2/16 about
ns x*

[some m.a. package]

*Ch
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a strong case for
3/-3 - otherwise
tax under rises.*

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THE PSBR IN 1987-88 AND 1988-89

INTRODUCTION AND SUMMARY

The main conclusions of our latest exercise are as follows:

1987-88 - The PSBR in 1987-88 is likely to be a surplus of £3½b. This implies total borrowing of £3½b. in February and March, a little above the average in real terms for recent years.

TABLE 1 : PSBR IN 1987-88 (£ billion)

	<u>1987 Budget forecast</u>	<u>Winter forecast</u>	<u>Latest Forecast</u>
CGBR (O)	3.6	-2.3	-3.3
LABR	1.2	0.9	1.1
PCBR	-0.9	-1.4	-1.2
PSBR	3.9	-2.8	-3.4

- Public expenditure in 1987-88 will be significantly below the levels assumed in the 1988 PEWP. GEP's latest February assessment is that the Planning Total will be £146.4b. but they say that later information suggests that this might be too high. The latest CGBR figures also point to downside risk on the GEP assessment. We have assumed a planning total of £146.0b. and GGE of £171.6b. Only a small proportion of the shortfalls on the 1988 PEWP numbers of £1.3b. and £1.0b. respectively are the result of economic activity being higher and unemployment lower than previously expected. Some departments - notably MOD with its ability to carry over £0.9b. of expenditure to 1988-89 - are spending much less than previously expected.

- With GGE in 1987-88 lower than expected in the 1988 PEWP the GGE ratio (excluding privatisation proceeds) is at 41½ per cent 1 per cent lower than in the PEWP.

- While CT receipts have been lower than expected both income tax and VAT - the taxes that are most sensitive to the current level of activity - have been very buoyant. The share of non-North Sea taxes and NIC's in GDP has probably

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risen slightly by $\frac{1}{2}$ per cent in 1987-88 to 37 $\frac{1}{2}$ per cent, the highest level since 1984-85.

- The LABR is forecast to be £1 $\frac{1}{2}$ b. in 1987-88, £1b. up on the 1986-87 level. There is no information on LAs' income and expenditure that explains this higher level of borrowing. The PCBR is forecast to be slightly higher than in 1986-87.

1988-89

- Our central forecast for the PSBR in 1988-89 is for a surplus of £5b., after taking account of the current package and on the assumption that activity is as in the draft of Chapter 3 of the FSBR. The PSBR effect of the package is almost the same as that of the fiscal adjustment assumed in the Winter Forecast. The underlying forecast for the PSBR surplus has been increased by £1 $\frac{1}{2}$ b.

- The central forecast of public expenditure is for an overspend on the cash plans of £ $\frac{1}{2}$ b., a somewhat smaller overspend than in the January forecast. This forecast takes account, *inter alia*, of likely pressures on NHS and MOD spending, possible expenditure on Rover a small overspend on social security (due to high positive 'underlying' growth) and continued overspending by local authorities. Taken with our latest assessment for 1987-88 it would imply a very small fall of $\frac{1}{4}$ per cent in the GGE ratio to 41 $\frac{1}{4}$ per cent.

- Non-oil government revenues are forecast to be very buoyant in 1988-89. In particular the further high growth in profits being recorded for 1987 - as a result of very high output growth and a further widening of margins - implies further strong growth in CT receipts, though the effective rate on 1987 accruals does not change much because of the build up in investment allowances. The share of NICs and non-North Sea taxes in GDP rises by $\frac{1}{2}$ per cent, notwithstanding the tax cuts in the package.

- There are some elements of 'prudence' in our forecast for government revenues. The effective VAT rate barely rises in spite of recent experience. Furthermore there is no allowance for beneficial indirect effects on the income tax take as a result of the cuts in marginal rates. There is no

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satisfactory basis for scoring such effects and in any case such effects are more likely to be experienced in the years after 1988-89. On the other hand in contrast to last year the sterling oil price assumption, and therefore forecast North Sea revenues, are not below the levels thought most likely to occur.

- The LABR and PCBR are both forecast to rise by some £½b. in 1988-89. Central government moves further into surplus.

Presentation in the FSBR

- If the aim were to present a PSBR surplus for 1987-88 that was more likely to be overshoot than undershot, it would be just about possible on the evidence now available to publish a surplus in the range of £2¼-3b. A lower surplus than this would too obviously appear to be a deliberate attempt to understate the strength of public finances, and would not be presentationally useful. Outsiders now generally see £3b. as the minimum surplus.

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- There would be problems in publishing for 1988-89 a PSBR surplus that is no higher than the published forecast outturn for 1987-88. If the FSBR has a surplus of £3b. for both 1987-88 and 1988-89 this on its own would involve deducting up to £2b. from forecast receipts for 1988-89 in our (internal) central forecast. The deduction would be larger if the published surpluses for 1987-88 and 1988-89 were lower. Furthermore the FSBR will show the public expenditure plans for 1988-89, not our (higher) central forecast. Publishing a surplus of £3b. in 1987-88 and 1988-89, together with showing the public expenditure plans would involve deducting up to £2¼b. or 1½ per cent from the forecast of general government receipts in 1988-89. (Most of this adjustment would inevitably be to central government taxes.) This would bring the increase in (post package) general government receipts below the growth of money GDP.

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- We can find no precedent for making any adjustments in the FSBR to the Revenue Departments' best estimates of taxes in the year ahead, given the assumed behaviour of the economy

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shown in the Industry Act forecast. There has been for certain taxes a tradition of 'prudence' (as, for instance, described above for the VAT effective rate), but never on the scale of the possible downward adjustments to revenues shown above. Quite apart from any concern they have for producing central forecasts of aggregate taxes the Revenue Departments answer hundreds of PQs and queries every year on individual taxes on the basis of the FSBR figures. For that and other reasons they are keen for their forecasts to be as unbiased as possible.

- While no-one would want to go to the stake for the sake of the central forecasts of revenues, it is worth bearing in mind that the record in the past few years has been to underestimate revenues. To adjust taxes down would produce what would inevitably be a suspiciously low growth of revenues, even given the package, in relation to money GDP.

(1) THE FORECAST

After this is recapitulated in more detail.

(a) 1987-88

2. The outturn for the PSBR for the 10 months to January was a surplus of £6.9 billion. The latest forecast for February and March is for borrowing of £3.5 billion, putting the PSBR for 1987-88 as a whole at a surplus of £3.4 billion (which rounds to $\frac{1}{4}$ per cent GDP). Annex IV includes the usual monthly note charts and tables, comparing the outturn and new forecasts with the Budget profiles.

TABLE 2 : THE PSBR PROFILE FOR 1987-88

	<u>Outturn to January</u>	<u>Latest Forecast</u>		
		February	March	Total for year
CGBR(O)	-6.0	0.1	2.6	-3.3
LABR	0.1	-0.1	1.1	1.1
PCBR	-0.9	-0.3	0.0	-1.2
PSBR	-6.9	-0.3	3.8	-3.4

3. The forecast PSBR for February and March is a little above the levels recorded in real terms in the previous five years, but lower

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than in 1982-83, when it totalled £4.8 billion at 1987-88 prices. (See Annex I for figures for recent years). Even if borrowing in February and March were to turn out at the real level of 1982-83 the PSBR for 1987-88 would still be a surplus of over £2 billion. But there are no compelling reasons for thinking that borrowing in the rest of the year will turn out so high.

Central Government

4. The January outturn figures have removed one of the major uncertainties on central government borrowing, namely that the surplus in the main tax gathering month would not be as high as recent forecasts have envisaged. Nevertheless there have been some unexpected developments. While they were very large by past standards, corporation tax (CT) receipts in January were significantly below recent monthly forecasts, and the CT forecast for 1987-88 has been revised downwards as a consequence to £15.8 billion - only £0.8 billion above the FSBR forecast. Income tax and VAT are now forecast to be £1½b. and £1b. higher respectively in 1987-88 than in the Budget forecast.

**TABLE 3 : CENTRAL GOVERNMENT TAX AND NATIONAL INSURANCE
CONTRIBUTIONS RECEIPTS 1987-88
- £ billion (per cent in brackets)**

	Changes since 1987 Budget	Changes since Winter forecast
Income Tax	1.2	0.1
Corporation tax (including ACT)	0.8	-1.0
PRT	0.5	0.0
Stamp Duty	0.4	0.1
Other Inland Revenue	0.2	0.1
Total Inland Revenue	3.2	-0.7
VAT	1.0	0.2
Excise duties	-0.2	0.0
Other	0.0	0.1
Total Customs & Excise	0.9	0.3
Other taxes*	0.2	0.2
National Insurance Contributions	0.5	0.3
TOTAL	4.8	0.0

* VED, gas levy and oil royalties.

5. There are still some uncertainties remaining on the revenue side

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about the outturn for individual taxes. The main ones are tobacco duty - where Budget forestalling always complicates analysis of the monthly figures at this time of year - and stamp duties, where the outturn, for both December and January has been higher than expected. In neither case is the potential error involved likely to be more than £0.2b.

6. On the expenditure side of the central government account the uncertainties are rather greater. Indeed the main surprise with recent monthly figures for central government borrowing has been the emergence of a growing undershoot of the 1987 Budget profile for central government expenditure. For the 10 months to January departmental expenditure (on a cash basis) was £1.7b., 1½ per cent, below the Budget profile. Data from central government funds and accounts in February shows the expenditure undershoot may have increased further.

7. A major problem in analysing this central government expenditure undershoot is that it is much larger than the undershoot shown in the monthly (APEX) figures collected by GEP for the purposes of monitoring spending on the planning total. GEP's APEX figures show an undershoot of the Budget profile of £1.1b. for 'supply' expenditure plus national insurance benefits - the nearest equivalent to the cash-based departmental expenditure figure consistent with the CGBR which is derived from cash data on government funds and accounts.

8. This 'cash' measure used for the CGBR is based on cheques clearing through the Paymaster General's Account, while the APEX system measures cheques issued by departments. One would expect therefore there to be a timing difference between the two measures as it takes some time for cheques to clear after they have been issued. Also the cash measure scores certain receipts (most of which count as negative expenditure in APEX) when they are received in departmental balances, whereas there can in some circumstances, be a delay in the recording of these receipts in APEX due to departmental accounting practices. But the discrepancy this year is much larger than can be explained by these timing differences. By its very nature the cash measure is highly accurate, but the APEX measure, the composite of a lot of individual departmental returns, has in the past proved to be less so - at least within year. (GEP currently have in hand a major exercise designed to improve the quality of APEX data.)

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**TABLE 4 : ALTERNATIVE MEASURES OF CENTRAL GOVERNMENT
EXPENDITURE - DIFFERENCES FROM BUDGET PROFILE**

	£ billion	
	April-January Outturn	1987-88 Forecast
1. Social Security	-0.5	-0.4
2. Other voted expenditure (APEX data)	-0.9	-1.0

3. Total APEX and NIBs (=1+2)	-1.4	-1.4
4. Cash/APEX discrepancy*	-0.6	-0.6
5. Other	<u>0.3</u>	<u>0.4</u>
6. Total departmental expenditure, on a cash basis (net of certain receipts) = 3 + 4 + 5	-1.7	-1.6

* the PMG residual

9. The forecast of the CGBR reported here assumes that the cash/APEX discrepancy is only partially unwound by the end of the year from its estimated mid-February level and that most of the cash undershoot to date persists.

10. Part of the cash undershoot has been taken as implying a 1987-88 planning total of £146.0b., lower than the £146.4b. in GEP's latest assessment. (Until the 1987-88 expenditure figures are properly recorded the next of the forecast undershoot may show in the balancing item in the national accounts and be counted - incongruously - as miscellaneous CG receipts in the FSBP in table 1.2 and chapter 6.)

LABR

11. The LABR in the first ten months of 1987-88 was £0.1 billion, in line with the Budget profile, but £0.7 billion higher than in the same period of 1986-87. The forecast for the remaining two months of the year is based on a view of borrowing itself, taking into account the outturn to date and the level of borrowing in the final two months in earlier years, rather than, as in the case of central government, on forecasts of income and expenditure. Monthly estimates of LA income

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and expenditure are not available and the level of borrowing so far is much higher than can easily be reconciled with the few scraps of data on LAS income and expenditure during 1987-88.

12. The LABR in February has on average been relatively small, but borrowing in March is always high, averaging over the past five years £1½ billion in today's prices. Taking February and March together the forecast is for a LABR higher than last year but, because net borrowing in the first 10 months has been above average, lower than the five year average.

PCBR

13. The Budget forecast was for a rise of £½ billion in the PCBR between 1986-87 and 1987-88, because the 1986-87 figures included substantial negative borrowing by subsequently privatised industries, such as BGC. Nevertheless borrowing by the industries remaining in the public sector was expected to fall. In the event borrowing by those industries' still in the PC sector has fallen by more than expected at Budget time. By end December the PCBR was £½ billion below the Budget profile, with BSC, the Post Office and water authorities more than accounting for the undershoot.

14. The PCBR in the final two months of this year is forecast to be a small surplus of about £¼ billion, much the same as in the same period of 1986-87. This gives a forecast surplus for the year as a whole of £1½ billion, compared with a surplus of just under £1 billion forecast at the time of the 1987 Budget.

1987-88 Summary

15. The revised forecast, in the general government/national accounts format, is summarised and compared with earlier forecasts in Table 5.

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TABLE 5 : RECEIPTS, EXPENDITURE AND BORROWING IN 1987-88

	1987 FSBR	£ billion	
		Winter Forecast	Latest Forecast
<u>General Government Receipts</u>			
Taxes and NICs	156.3	161.4	160.8
Other receipts	12.6	12.3	13.3
Total	168.8	173.7	174.1
<u>General Government Expenditure</u>			
Planning total	148.6	146.8	146.0
Debt interest	17.9	17.4	17.5
Other	5.4	7.6	8.1
Total	173.5	171.9	171.6
GGBR	4.7	-1.9	-2.5
PCMOB	-0.8	-0.9	-0.9
PSBR	3.9	-2.8	-3.4
PSBR (%)	1.0	0.8	0.8

Why has this increased? What is it?

(b) 1988-89

16. On the basis of an assumed fiscal adjustment of £4 billion, the Winter Economic forecast had a PSBR surplus in 1988-89 of £3½b. The new forecast substitutes the latest Budget package for the assumed fiscal adjustment and incorporates changes to the underlying forecasts of receipts and expenditure in the light of later information and changes to the rest of the forecast. The new forecast is for a larger PSBR surplus of about £5 billion. This is due to an upward revision of £1½b. to the underlying level of receipts. The forecast of GGE has hardly changed. The PSBR effect of the Budget package is virtually identical to that of the fiscal adjustment in the Winter Forecast.

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TABLE 6 : RECEIPTS, EXPENDITURE AND BORROWING IN 1988-89

£ billion

	1987 FSBR	Winter Forecast	Latest Forecast
General Government Receipts	175.0*	185.7*	187.3
General Government Expenditure	180.5	183.5	183.4
CGBR	5.5	-2.2	-3.9
PCMOB	-1.1	-1.2	-1.2
PSBR	4.4	-3.4	-5.1

* after fiscal adjustments of £3.2b. in 1987 FSBR and £4b. in Winter forecast.

(c) Expenditure

17. The Winter Forecast included a forecast of the planning total outturn in 1988-89 which was about £1 billion above the level provided for in the 1988 PEWP. The forecast overspend has been revised down a little to £½b. The forecast level of social security expenditure has been revised down by £¼ billion and some of the downward revision to CG spending this year has been assumed to imply lower spending next year. Going in the opposite direction is some allowance for possible expenditure on Rover which is now in the forecast. The revised forecast is summarised in Annex II.

18. The forecast still assumes privatisation proceeds of £5 billion, although as Mr Moore's minute to the Chancellor of 16 February indicates, this total will be exceeded by at least £½ billion if the BSC sale goes ahead in 1988-89. The effect on public expenditure in total would be smaller than the BSC proceeds because of the loss of BSC's negative EFL. Nevertheless the possibility of the privatisation of BSC represents a significant downside risk to the forecast of both the planning total and GGE.

19. The forecast of gross debt interest payments in 1988-89 has been revised down slightly, and, at £17.2b., is £¼ billion lower than in the 1988 PEWP.

20. The new forecast of the GGE ratios (excl. privatisation proceeds) are as follows:

	1986-87	1987-88	1988-89
1988 PEWP	44	42½	42
Latest forecast	43¼	41½	41¼

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It would not take much to wipe out the forecast fall in the ratio between 1987-88 and 1988-89.

(d) Revenues

21. The underlying buoyancy of non-oil tax revenues is expected to continue in 1988-89. Even with the Budget package, the tax burden is forecast to rise by around $\frac{1}{2}$ percentage point, whether measured in terms of total taxes and total GDP, or in terms of non-oil taxes and non-oil GDP.

TABLE 7 : THE TAX BURDEN

	1986-87	1987-88	1988-89
Taxes and NICs as % of GDP	37.8	37.7	38.3
Non-oil Taxes and NICs as % of Non-oil GDP	37.3	37.5	38.1

22. The main contributor to tax buoyancy is again expected to be corporation tax, where a forecast 30 per cent plus increase in non-North Sea receipts is in line with the average of the two previous years. As compared to the Winter forecast 1988-89 non-North Sea CT receipts have been revised downwards by £0.9b. - a smaller reduction than the £1.2 billion for 1987-88 in the light of the January outturn. The level of gross trading profits for non-North Sea ICCs in 1987 has been revised upwards by around £1 billion since the Winter forecast; at the same time, the estimate of ACT in 1987-88 has been revised downwards (implying for given profits in 1987, more MCT in 1988-89). These factors outweigh the effects of a lower basic rate on ACT payments in 1988-89. There is still a good deal of uncertainty over the CT forecast and we will be going over the figures again with the Inland Revenue as more data on 1987 profits become available.

23. Another area where buoyancy of revenues is forecast to continue, for 1988-89 at least, is capital taxes (CGT and CT on capital gains, plus Inheritance Tax). The Budget package is estimated to have a marginal net effect (less than £0.1 billion) in reducing receipts in 1988-89; the forecast is for an increase in excess of 20 per cent for the fourth year in succession. The latest forecast for 1988-89 represents an upward revision of £0.5 billion on the Winter forecast,

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which partly reflects later information on the level of receipts in 1987-88.

24. The underlying (ie pre fiscal adjustment/package) forecast of income tax revenues in 1988-89 is now £½b. higher than in the Winter forecast. The forecast assumes the continuation of the trend widening of the income distribution experienced in the 1980s, it does not, however, make any explicit allowance for any further boost to revenues from the proposed reduction in the higher rates of income tax, along the lines suggested by the work of Lawrence Lindsey in the United States. Lindsey's analysis has been replicated for the UK by Inland Revenue statisticians, who showed that the direct costs of cuts in the higher rates in 1979 had been more than recouped from higher rate taxpayers by 1986-87 because the widening income distribution has generated higher tax liabilities. Lindsey ascribed similar results for the United States to the effects of tax cuts, but in the case of the UK many other factors are known to have contributed to the changes in the distribution of income, and it is difficult to substantiate a similar claim. For this reason, no such effects are explicitly included in the costings of higher rate reductions. This is not to say that such effects will not occur - although to the extent that they do, it is likely to be in the years after 1988-89. Assumed behaviour effects of tax changes are reflected in the forecasts for other taxes, notably CGT.

25. The forecast for VAT receipts shows hardly any increase in the effective tax rate (VAT receipts as a percentage of GDP). This is arguably a conservative projection, although there is no firm evidence from the past two years of a connection between a rising effective tax rate and real growth in consumers' expenditure.

26. Among other expenditure taxes, the main contributor to continuing buoyancy of tax receipts is a forecast 14 per cent rise in local authority rates. (This is the forecast increase in rates

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receipts, net of rebates which are assumed to fall in 1988-89 as the social security reformed - not the increase in rate poundage.) This represents an upward revision of £0.7b. to the Winter forecast. Stamp duty receipts, however, are forecast to fall - following three years' growth at an average rate of around 40 per cent - as a result of lower stock market prices.

27. North Sea revenues are expected to fall by around £0.7 billion (15 per cent). This is a rather smaller reduction (by £0.4 billion) than in the Winter forecast, reflecting a lower sterling/dollar exchange rate.

TABLE 8 : GENERAL GOVERNMENT RECEIPTS FORECAST - % changes

	Shares in 1987-88	1985-86	1986-87	1987-88	1988-89
Income Tax	0.24	+ 7½	+ 7½	+ 6½	+2½
Corporation Tax (excl. North Sea)	0.08	+22	+34	+24	+30
Capital Taxes	0.02	+31	+21	+29	+28
VAT Receipts	0.14	+ 4½	+10½	+13½	+ 8½
Local Authority Rates	0.10	+ 6½	+13	+ 9	+14
Stamp Duties	0.02	+38	+46	+39	-13½
Other Expenditure taxes	0.15	+10½	+ 6½	+ 3	+ 6½
North Sea Revenues	0.03	- 6	-58	- 5	-15
Other Taxes	0.00	- 1	- 2½	-51	+ 8½
Total Taxes and Royalties	0.76	+ 7½	+ 5	+ 10	+ 8½
National Insurance Contributions	0.17	+ 8½	+ 8½	+ 8	+ 9½
Interest and other receipts	0.08	+ 6	+ 10½	- 1½	- 6½
TOTAL	1.00	+ 8	+ 6	+ 9	+ 7½

(2) PRESENTATION IN THE FSBR

(a) 1987-88

28. It seems to be a view generally held outside that the Treasury

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deliberately publishes forecasts of the PSBR that are too high. The forecast outturns in the FSBR for the year just ending have been too high in each of the last three FSBRs (see Annex III). Over longer periods of time there is no systematic bias on PSBR.

29. The provisional February outturn figures will be published the day after the Budget, ie after outside analysts have given their initial reactions to the Budget, but in time to be taken into account in their second thoughts, for example in memoranda to the TCSC. The PSBR outturn for 1987-88 in the FSBR will therefore have to be reasonably convincing in the context of the cumulative outturn to February. As we do not yet have this, recommendations and decisions at this stage must be provisional.

30. Table 7 shows the average level of borrowing in March, at today's prices over the past five years. It also shows borrowing in March last year which outsiders would tend to look at in particular when judging the plausibility of the forecast, possibly also adjusting for known special factors. Last March there were £b. privatisation proceeds, but the informed outsider would know that this was largely offset by £b. one-off expenditure on Rover.

31. Special factors affecting central government borrowing in March 1988 are more subtle and may not be as obvious to an outsider. They are the cash payments, on redemption on 30 March, for uplift on 2 per cent Index Linked (1988), and 5 national insurance benefit payment days compared with 4 last year.

TABLE 8 : BORROWING IN MARCH

	£ billion, 1987-88 prices			
	CGBR(0)	LABR	PCBR	PSBR
1982-83 to 1986-87 average	1.8	1.3	0.1	3.2
1986-87	2.3	1.0	0.1	3.5
1987-88 (Best estimate)	2.6	1.2	0.0	3.8

32. There are a number of major inconsistencies in the accounts of all three sectors for 1987-88 which will make presentation of even our best estimate in the FSBR a little difficult:

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- the discrepancy between the two measures of CG expenditure which would show up as large positive miscellaneous receipts if carried through to the FSBR;
- a higher LABR than implied by LA income and expenditure which would show up in the FSBR as large negative miscellaneous receipts for LAs;
- lower borrowing by individual nationalised industries within EFLs, than is implied by the aggregate PCBR figures.

33. It would be possible, on current figuring, to publish a PSBR from 1987-88 about £ $\frac{1}{2}$ - $\frac{3}{4}$ b. lower than our best estimate, without distorting the tax figures, by reducing miscellaneous CG receipts. This would imply a forecast of £ $2\frac{3}{4}$ -3b., or $\frac{3}{4}$ per cent of money GDP.

+ £2.9 bn

(b) 1988-89

34. The best estimate of the PSBR in 1988-89 is a surplus of £5b., or 1 per cent of GDP. This is based on a forecast planning total £ $\frac{1}{2}$ b. higher than in the 1988 PEWP. Even if we were to publish a £5b. surplus therefore we would have to reduce the forecast of receipts by up to £ $\frac{1}{2}$ b. (it would be possible to offset some of the planning total reduction by increasing the forecast of expenditure outside the planning total). If it were decided to publish a PSBR figure no lower than the published forecast for 1987-88, say £3b. This would require a further reduction in receipts of £2b., giving a total reduction in receipts of up to £ $2\frac{1}{2}$ b. If the published 1988-89 surplus were lower than £3b. the adjustment to receipts would be correspondingly lower.

35. It would not be possible to reduce the forecast of receipts by up to £ $2\frac{3}{4}$ b. simply by reducing miscellaneous receipts, the usual way of squaring this sort of circle. There would have to be major reductions in the forecast of tax receipts. Not only would this make the forecast of tax receipts suspiciously low, it would distort the tax burden. Each £1b. off tax receipts (for given GDP) reduces the tax burden by 0.2 percentage points.

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then!

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TABLE 8 : TAX BURDEN - %

	<u>Total</u>		<u>Non-oil</u>	
	1987-88	1988-89	1987-88	1988-89
<u>Before Budget changes</u>				
Best estimate	37.7	39.1	37.5	39.0
Consistent with -f3b PSBR	37.7	38.5	37.5	38.3
<u>After Budget changes</u>				
Best estimate	37.7	38.3	37.5	38.1
Consistent with -f3b. PSBR	37.7	37.7	37.5	37.5

seem highly desirable!

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ANNEX I: BORROWING IN FEBRUARY AND MARCH

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£ billionExcluding
Privatisation
proceeds

	PSBR	CGBR(O)	LABR	PCBR	PSBR	CGBR(O)
<u>Current prices</u>						
1982-83	3.8	2.2	1.3	0.3	N/A	N/A
1983-84	2.6	1.8	1.2	- 0.3	N/A	N/A
1984-85	2.3	1.0	1.5	- 0.1	2.4	1.0
1985-86	2.6	1.4	1.2	0.0	3.0	1.8
1986-87	2.9	2.3	0.8	- 0.3	4.0	3.5
Average	2.8	1.7	1.2	- 0.1		
1987-88	3.5	2.7	1.1	- 0.3	3.4	2.7
<u>1987-88 prices</u>						
1982-83	4.8	2.7	1.6	0.4	N/A	N/A
1983-84	3.2	2.2	1.4	- 0.4	N/A	N/A
1984-85	2.7	1.1	1.7	- 0.1	2.7	1.2
1985-86	2.8	1.6	1.3	0.0	3.3	2.0
1986-87	3.0	2.5	0.9	- 0.3	4.3	3.7
Average	3.3	2.0	1.4	- 0.1		
1987-88	3.5	2.7	1.1	- 0.3	3.4	2.7

BORROWING IN MARCH

£ billion

Excluding
Privatisation
proceeds

	PSBR	CGBR(O)	LABR	PCBR	PSBR	CGBR(O)
<u>Current prices</u>						
1982-83	2.9	1.5	1.2	0.2	N/A	N/A
1983-84	2.3	1.4	1.1	- 0.2	N/A	N/A
1984-85	2.4	1.5	1.1	- 0.2	2.5	1.5
1985-86	3.0	1.4	1.2	0.4	3.4	1.8
1986-87	3.3	2.2	0.9	0.1	4.0	2.9
Average	2.8	1.6	1.1	0.1		
1987-88	3.8	2.6	1.2	0.0	3.8	2.6
<u>1987-88 prices</u>						
1982-83	3.6	1.9	1.5	0.3	N/A	N/A
1983-84	2.7	1.7	1.3	- 0.3	N/A	N/A
1984-85	2.7	1.7	1.2	- 0.2	2.8	1.8
1985-86	3.2	1.5	1.3	0.4	3.7	2.0
1986-87	3.5	2.3	1.0	0.1	4.2	3.1
Average	3.2	1.8	1.3	0.1		
1987-88	3.8	2.6	1.2	0.0	3.8	2.6

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ANNEX II : FORECAST ADDITIONS TO EXPENDITURE PLANS

	1987-88		1988-89	
	PEWP	Forecast	PEWP	Forecast
	1987	Claims on Reserve	1988	Claims on Reserve
£ billion				
<u>Allocated to programmes</u>				
1. Social Security (including HB)	44.7	0.2	46.9	0.3
2. LA current (excluding HB)	32.5	1.1	34.9	2.0
3. CG pay	24.8	0.7	26.8	1.0
4. CG procurement	24.6	-0.4	25.5	0.4
5. LA capital	4.3	-0.6	4.0	0
6. EC	0.9	0.8	0.8	0.3
7. Nationalised industries	0.7	-0.3	0.7	-0.2*
8. Other	17.8	-0.6	18.8	0.4
9. Total programmes	150.1	0.9	158.3	4.2
10. Privatisation proceeds	-5.0	0.0	-5.0	0.0
11. <u>Expenditure met from existing reserve</u>				
(i) allocated to programme baseline	0.0	0.9	0.0	3.5
(ii) unallocated	3.5	0.0	3.5	0.0
12. <u>Underspend (-)</u> <u>Addition to</u> <u>Reserve(+)</u>	0.0	-2.6	0.0	0.7
13. PLANNING TOTAL	148.6	-2.6	156.8	0.7

* includes EFL offsets to assumed privatisation of the Giro (-£60m.) in 1988-89.

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A. Year Just finishing	Forecast £b	Outturn £b	Error £b	Error % of GDP
1967-68	2.0	2.0	0.0	0.0
1968-69	0.3	0.5	+ 0.2	+ 0.5
1969-70	- 0.6	- 0.5	+ 0.1	+ 0.2
1970-71	0.6	0.8	+ 0.2	+ 0.4
1971-72	1.3	1.0	- 0.3	- 0.6
1972-73	2.9	2.5	- 0.4	- 0.7
1973-74	4.3	4.5	+ 0.2	+ 0.3
1974-75	7.6	7.9	+ 0.3	+ 0.3
1975-76	10.8	10.6	- 0.2	- 0.2
1976-77	8.8	8.5	- 0.3	- 0.2
1977-78	5.7	5.6	- 0.2	- 0.1
1978-79	9.2	9.2	0.0	0.0
1979-80	9.1	10.1	+ 1.0	+ 0.5
1980-81	13.5	13.3	- 0.1	0.0
1981-82	10.6	9.0	- 1.6	- 0.6
1982-83	7.5	9.4	+ 1.8	+ 0.7
1983-84	10.0	10.2	+ 0.2	+ 0.1
1984-85	10.5	10.2	- 0.3	- 0.1
1985-86	6.8	5.8	- 1.0	- 0.3
1986-87	4.1	3.4	- 0.7	- 0.2
Average Absolute Errors	Whole period		0.5	0.3
	Last 10 years		0.7	0.3
	Last 5 years		0.8	0.3
Bias	Whole period		- 0.1	0.0
	Last 10 years		0.0	0.0
	Last 5 years		0.0	0.0

B. Year ahead	Forecast £b	Outturn £b	Error £b	Error % of GDP
1967-68	1.5	2.0	+ 0.5	+ 1.2
1968-69	1.0	0.5	- 0.5	- 1.1
1969-70	- 0.3	- 0.5	- 0.2	- 0.4
1970-71	- 0.2	0.8	+ 1.0	+ 1.9
1971-72	1.2	1.0	- 0.2	- 0.3
1972-73	3.4	2.5	- 0.9	- 1.3
1973-74	4.4	4.5	+ 0.1	+ 0.1
1974-75	2.7	7.9	+ 5.2	+ 5.8
1975-76	9.1	10.6	+ 1.5	+ 1.4
1976-77	12.0	8.5	- 3.5	- 2.7
1977-78	8.5	5.6	- 2.9	- 1.9
1978-79	8.5	9.2	+ 0.7	+ 0.4
1979-80	8.3	10.1	+ 1.8	+ 0.9
1980-81	8.5	13.3	+ 4.8	+ 2.0
1981-82	10.6	9.0	- 1.6	- 0.6
1982-83	9.5	9.4	- 0.1	0.0
1983-84	8.2	10.2	+ 2.0	+ 0.7
1984-85	7.2	10.2	+ 3.0	+ 0.9
1985-86	7.1	5.8	- 1.3	- 0.4
1986-87	7.1	3.4	- 3.7	- 1.0
Average Absolute Errors	Whole period		1.8	1.3
	Last 10 years		2.2	0.9
	Last 5 years		2.0	0.6
Bias	Whole period		+ 0.3	+ 0.3
	Last 10 years		+ 0.3	+ 0.1
	Last 5 years		0.0	0.0

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CHART 1
87-88 COMPARISONS
WITH 87 BUDGET
PROFILES

ANNEX IV

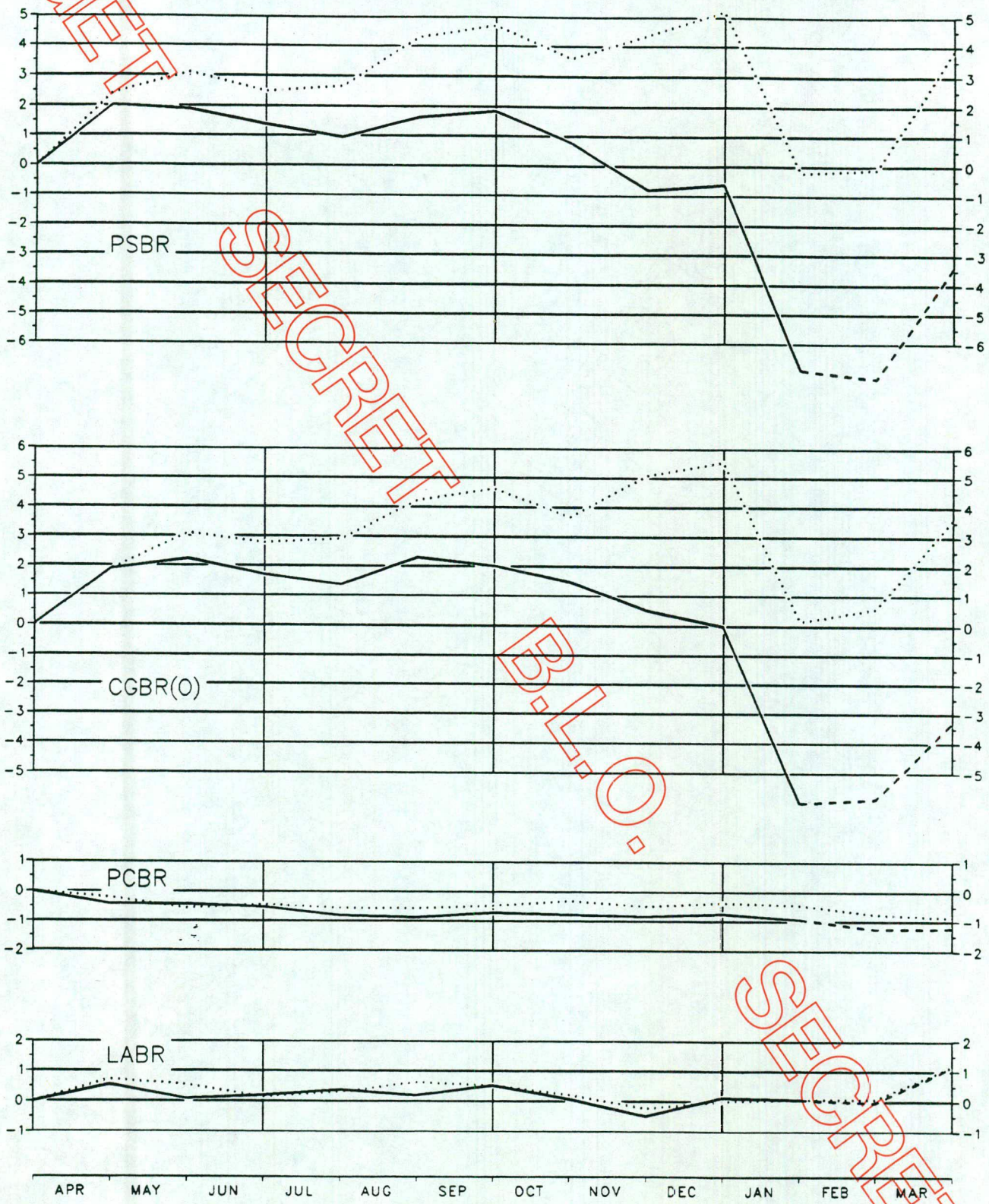
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Chart 1 : 1987-88: Comparisons with 1987 Budget profiles

£ billion cumulative

- = Estimated outturn in 1987-88
- - - = Latest forecasts
- = Budget: profile



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CHART 2
87-88 COMPARISONS
WITH OUTTURNS
FOR 86-87

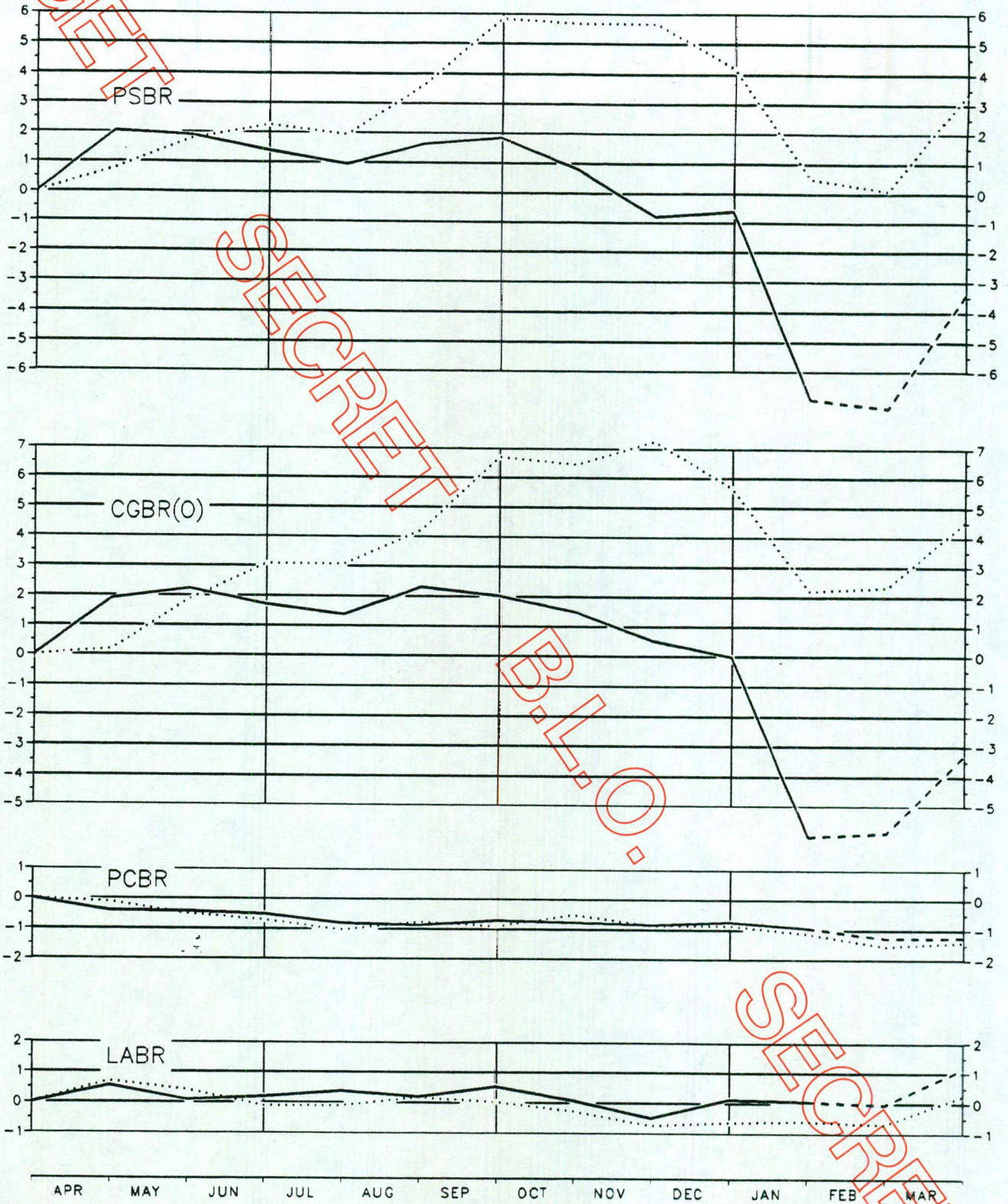
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Chart 2: 1987-88: Comparisons with outturns for 1986-87

£ billion cumulative

- = Estimated outturn in 1987-88
- - - = Latest forecasts
- = 1986-87 outturn



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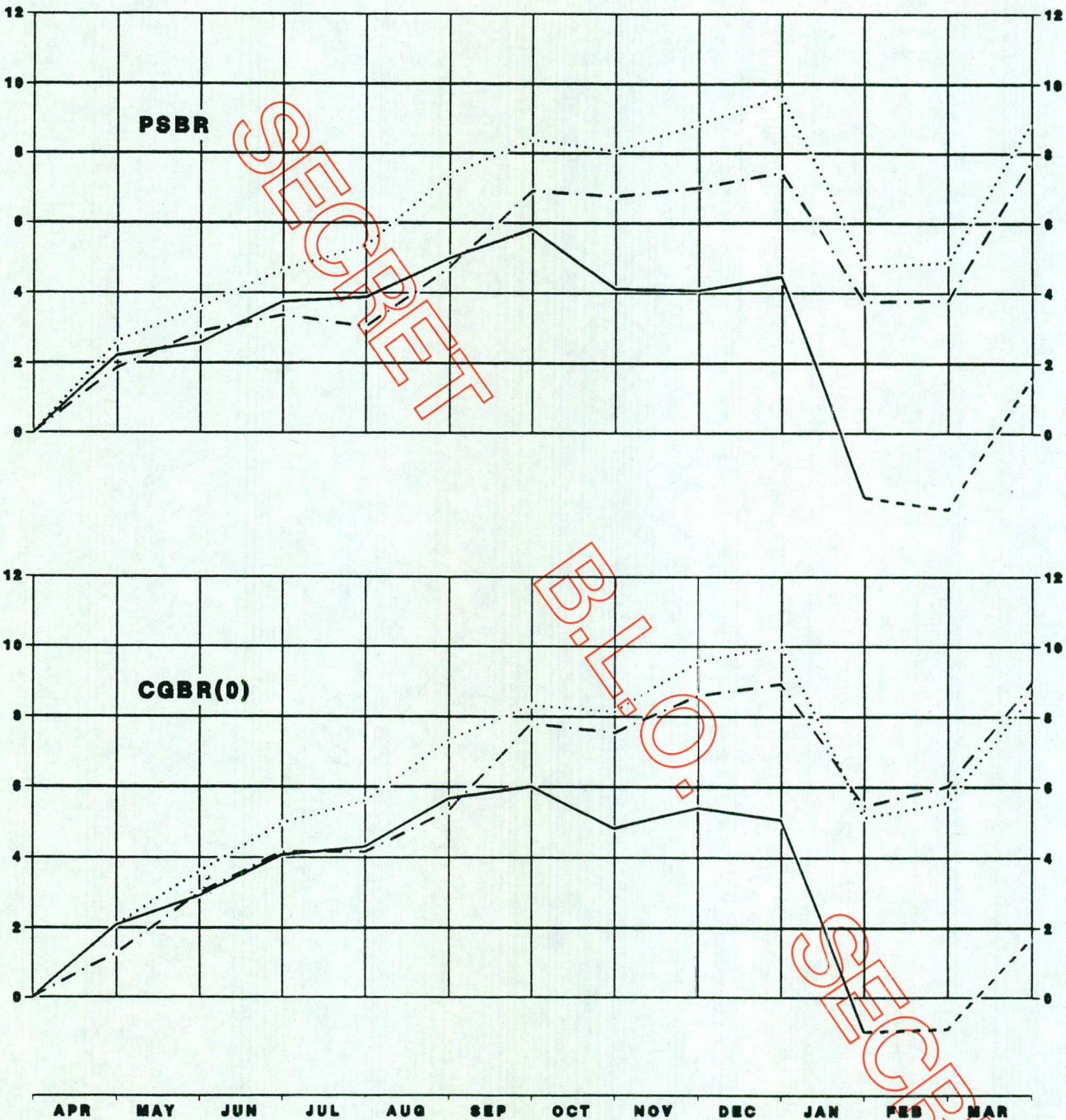
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Chart 3: Comparisons excluding privatisation proceeds

£ billion cumulative

- = Estimated outturn in 1987-88
- - - = Latest forecasts
- · - · = 1986-87 outturn
- = 1987-88 Budget profiles



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**PSBR for 1987-88 - comparisons with 1986-87
and 1987 Budget profile**

£ billion

	1986-87	1987-88		Differences from	
	Outturn	Budget profile	Latest update ⁽¹⁾	1986-87 outturn	Budget profile
	1	2	3	3-1	3-2
Apr	0.8	2.4	2.0	1.3	-0.4
May	1.0	0.7	-0.1	-1.1	-0.8
Jun	0.5	-0.6	-0.5	-1.0	0.1
Q2	2.3	2.5	1.4	-0.9	-1.1
Jul	-0.3	0.2	-0.4	-0.1	-0.6
Aug	1.7	1.6	0.7	-1.0	-1.0
Sep	2.2	0.4	0.2	-2.0	-0.2
Q3	3.6	2.2	0.5	-3.1	-1.7
Oct	-0.2	-1.1	-1.1	-0.9	-
Nov	-	0.8	-1.6	-1.6	-2.4
Dec	-1.5	0.8	0.2	1.7	-0.6
Q4	-1.6	0.5	-2.5	-0.8	-3.0
Jan	-3.7	-5.4	-6.3	-2.6	-0.9
Feb	-0.4	0.1	-0.3	0.1	-0.4
Mar	3.3	4.0	3.8	0.5	-0.2
Cumulative					
Apr	0.8	2.4	2.0	1.3	-0.4
May	1.8	3.1	1.9	0.1	-1.2
Jun	2.3	2.5	1.4	-0.9	-1.1
Jul	1.9	2.7	0.9	-1.0	-1.7
Aug	3.6	4.3	1.6	-2.0	-2.7
Sep	5.8	4.7	1.8	-4.0	-2.8
Oct	5.7	3.6	0.8	-4.9	-2.8
Nov	5.7	4.4	-0.8	-6.5	-5.2
Dec	4.2	5.2	-0.6	-4.8	-5.8
Jan	0.5	-0.2	-6.9	-7.4	-6.7
Feb	0.1	-0.1	-7.2	-7.3	-7.1
Mar	3.4	3.9	-3.4	-6.8	-7.3

⁽¹⁾Figures for April - January are outturns

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Borrowing requirement monthly profiles April–March, 1987–88
(Budget profiles in italics for comparison) £ billion

	PSBR		CGBR(O)		LABR		PCBR	
Apr	2.0	<i>2.4</i>	1.9	<i>1.9</i>	0.5	<i>0.7</i>	-0.4	<i>-0.2</i>
May	-0.1	<i>0.7</i>	0.3	<i>1.2</i>	-0.5	<i>-0.2</i>	-	<i>-0.4</i>
Jun	-0.5	<i>-0.6</i>	-0.5	<i>-0.3</i>	0.1	<i>-0.4</i>	-0.1	<i>0.1</i>
Jul	-0.4	<i>0.2</i>	-0.3	<i>0.1</i>	0.2	<i>0.2</i>	-0.3	<i>-0.1</i>
Aug	0.7	<i>1.6</i>	0.9	<i>1.3</i>	-0.2	<i>0.3</i>	-0.1	<i>-</i>
Sep	0.2	<i>0.4</i>	-0.3	<i>0.4</i>	0.3	<i>-0.1</i>	0.2	<i>0.1</i>
Oct	-1.1	<i>-1.1</i>	-0.5	<i>-1.0</i>	-0.5	<i>-0.3</i>	-0.1	<i>0.2</i>
Nov	-1.6	<i>0.8</i>	-1.0	<i>1.4</i>	-0.6	<i>-0.5</i>	-0.1	<i>-0.2</i>
Dec	0.2	<i>0.8</i>	-0.5	<i>0.5</i>	0.6	<i>0.2</i>	0.1	<i>0.1</i>
Jan	-6.3	<i>-5.4</i>	-6.0	<i>-5.4</i>	-0.1	<i>0.1</i>	-0.2	<i>-0.1</i>
Feb	-0.3	<i>0.1</i>	0.1	<i>0.4</i>	-0.1	<i>-</i>	-0.3	<i>-0.3</i>
Mar	3.8	<i>4.0</i>	2.6	<i>3.0</i>	1.2	<i>1.1</i>	-	<i>-0.1</i>
Cumulative								
Apr	2.0	<i>2.4</i>	1.9	<i>1.9</i>	0.5	<i>0.7</i>	-0.4	<i>-0.2</i>
May	1.9	<i>3.1</i>	2.2	<i>3.1</i>	0.1	<i>0.6</i>	-0.4	<i>-0.6</i>
Jun	1.4	<i>2.5</i>	1.7	<i>2.8</i>	0.2	<i>0.1</i>	-0.5	<i>-0.4</i>
Jul	0.9	<i>2.7</i>	1.4	<i>2.9</i>	0.4	<i>0.3</i>	-0.8	<i>-0.6</i>
Aug	1.6	<i>4.3</i>	2.3	<i>4.2</i>	0.2	<i>0.6</i>	-0.9	<i>-0.6</i>
Sep	1.8	<i>4.7</i>	2.0	<i>4.6</i>	0.5	<i>0.5</i>	-0.7	<i>-0.5</i>
Oct	0.8	<i>3.6</i>	1.5	<i>3.7</i>	0.1	<i>0.2</i>	-0.8	<i>-0.3</i>
Nov	-0.8	<i>4.4</i>	0.5	<i>5.1</i>	-0.5	<i>-0.2</i>	-0.8	<i>-0.5</i>
Dec	-0.6	<i>5.2</i>	-	<i>5.5</i>	0.1	<i>-</i>	-0.7	<i>-0.4</i>
Jan	-6.9	<i>-0.2</i>	-6.0	<i>0.2</i>	0.1	<i>0.1</i>	-0.9	<i>-0.4</i>
Feb	-7.2	<i>-0.1</i>	-5.9	<i>0.6</i>	-	<i>0.1</i>	-1.3	<i>-0.8</i>
Mar	-3.4	<i>3.9</i>	-3.3	<i>3.6</i>	1.1	<i>1.2</i>	-1.2	<i>-0.9</i>

	Excluding privatisation proceeds				Memo item: privatisation proceeds	
	PSBR		CGBR(O)			
Apr	2.2	<i>2.6</i>	2.1	<i>2.1</i>	0.2	<i>0.2</i>
May	0.4	<i>1.0</i>	0.8	<i>1.5</i>	0.5	<i>0.3</i>
Jun	1.2	<i>1.1</i>	1.2	<i>1.4</i>	1.7	<i>1.7</i>
Jul	0.1	<i>0.7</i>	0.2	<i>0.6</i>	0.6	<i>0.5</i>
Aug	1.1	<i>2.0</i>	1.4	<i>1.7</i>	0.4	<i>0.4</i>
Sep	0.8	<i>1.0</i>	0.3	<i>1.0</i>	0.6	<i>0.6</i>
Oct	-1.7	<i>-0.3</i>	-1.2	<i>-0.2</i>	-0.6	<i>0.8</i>
Nov	-	<i>0.8</i>	0.6	<i>1.4</i>	1.5	<i>-</i>
Dec	0.4	<i>0.8</i>	-0.3	<i>0.5</i>	0.2	<i>-</i>
Jan	-6.3	<i>-4.9</i>	-6.0	<i>-4.9</i>	-	<i>0.5</i>
Feb	-0.4	<i>0.1</i>	0.1	<i>0.4</i>	-0.1	<i>-</i>
Mar	3.8	<i>4.0</i>	2.6	<i>3.1</i>	-	<i>-</i>
Cumulative						
Apr	2.2	<i>2.6</i>	2.1	<i>2.1</i>	0.2	<i>0.2</i>
May	2.6	<i>3.6</i>	2.9	<i>3.6</i>	0.7	<i>0.5</i>
Jun	3.8	<i>4.7</i>	4.1	<i>5.0</i>	2.4	<i>2.2</i>
Jul	3.9	<i>5.4</i>	4.3	<i>5.6</i>	2.9	<i>2.7</i>
Aug	5.0	<i>7.4</i>	5.7	<i>7.3</i>	3.4	<i>3.1</i>
Sep	5.8	<i>8.4</i>	6.0	<i>8.3</i>	4.0	<i>3.7</i>
Oct	4.1	<i>8.1</i>	4.8	<i>8.2</i>	3.3	<i>4.5</i>
Nov	4.1	<i>8.9</i>	5.4	<i>9.6</i>	4.9	<i>4.5</i>
Dec	4.5	<i>9.7</i>	5.1	<i>10.0</i>	5.1	<i>4.5</i>
Jan	-1.8	<i>4.8</i>	-1.0	<i>5.1</i>	5.1	<i>5.0</i>
Feb	-2.2	<i>4.9</i>	-0.9	<i>5.6</i>	5.0	<i>5.0</i>
Mar	1.6	<i>8.9</i>	1.7	<i>8.6</i>	5.0	<i>5.0</i>

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NOTE OF A MEETING IN THE CHANCELLOR'S ROOM HM TREASURY
AT 11.15AM ON FRIDAY 19 FEBRUARY

Present: Chancellor
Chief Secretary
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Odling-Smee
Mr Turnbull
Mr R I G Allen
Mr Mowl
Mr Ritchie
Mr Tyrie

PSBR IN 1987-88 AND 1988-89

The Chancellor said he was inclined to publish figures of -£2.9 billion for the PSBR in 1987-88 and -£3.1 billion for 1988-89, both rounding to -£3 billion. There were large margins of error, and the consequences of an overshoot were more serious than the consequences of an undershoot, so it made sense to be cautious. It appeared that publishing a PSBR of -£2.9 billion for 1987-88 would not present any great difficulties. The position was harder for 1988-89; but, for example, we could use a \$15 oil price assumption, and there was some scope for increasing the forecast for interest and other receipts. A PSBR of -£3 billion was consistent with an unchanged non-oil tax burden; while it was not necessary to show a fall in the tax burden next year, it would be highly undesirable to show an increase. The Chancellor said he would therefore be grateful for advice on how a published PSBR of -£3 billion for 1988-89 might be achieved.

2. Sir T Burns commented that, so long as we were prepared to say that we had been reasonably cautious in our estimates, this should be possible and defensible.

Distribution: Those present.

ACSA
A C S ALLAN

NOTE OF A MEETING IN THE CHANCELLOR'S ROOM HM TREASURY
AT 11.15AM ON FRIDAY 19 FEBRUARY

Present: Chancellor
Chief Secretary
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Odling-Smee
Mr Turnbull
Mr R I G Allen
Mr Mowl
Mr ~~Mitchie~~
Mr Tyrie

PSBR IN 1987-88 AND 1988-89

The Chancellor said he was inclined to publish figures of ~~£~~[£] 2.9 billion ^{of} the PSBR in 1987-88 and ~~£~~[£] 3.1 ^{hillion} for 1988-89, both rounding ^{to} -£3 billion. There were large margins of error, and the consequences of an overshoot were more serious than the consequences of an undershoot, so it made sense to be cautious. It appeared that a PSBR of £2.9 billion for 1987-88 ^{publishing} could be achieved without ^{great} difficulties. ^{assumption} ~~It was harder for 1988-89;~~ ^{would not present any} ~~two options were~~ ^{but, for example, we} to use a \$15 oil price, and to increase the forecast for interest and other receipts. ^{could} ^{there was some scope for}

2. Sir T Burns ^{commented} ~~thought~~ that, so long as we were prepared to say that we had been reasonably cautious in our estimates, this should be possible and defensible. ~~Mr Mowl noted that it should be possible to reduce the forecast of debt interest by about £1 billion without changing the forecast of interest receipts.~~

3. The Chancellor ^{said he would therefore} ~~asked~~ for advice on how ^{a published PSBRA - £3.1 billion} ~~this~~ might be achieved. ^{he grateful}

~~A PSBRA - £3 billion was~~
constant with an unchanged
non-oil tax burden; ~~as a~~

A C S ALLAN

~~percentage of GDP and this seemed highly~~
while it was not necessary to show a full ~~the~~ tax burden ~~next~~ year, it would be ^{highly undesirable to show an increase.}

**NOTE OF A MEETING IN THE CHANCELLOR'S ROOM HM TREASURY
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Sir P Middleton
Sir T Burns
Mr Anson
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Mr Culpin
Mr Odling-Smee
Mr Turnbull
Mr R I G Allen
Mr Mowl
Mr Ritchie
Mr Tyrie

Final

PSBR IN 1987-88 AND 1988-89

The Chancellor said he was inclined to publish figures of -£2.9 billion for the PSBR in 1987-88 and -£3.1 billion for 1988-89, both rounding to -£3 billion. There were large margins of error, and the consequences of an overshoot were more serious than the consequences of an undershoot, so it made sense to be cautious. It appeared that publishing a PSBR of -£2.9 billion for 1987-88 would not present any great difficulties. The position was harder for 1988-89; but, for example, we could use a \$15 oil price assumption, and there was some scope for increasing the forecast for interest and other receipts. A PSBR of -£3 billion was consistent with an unchanged non-oil tax burden; while it was not necessary to show a fall in the tax burden next year, it would be highly undesirable to show an increase.

2. Sir T Burns commented that, so long as we were prepared to say that we had been reasonably cautious in our estimates, this should be possible and defensible.

BM The Chancellor said he would therefore be grateful for advice on how a published PSBR of -£3 billion might be achieved.

1w1988-89

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COPY 1 OF 27

FROM: MISS C E C SINCLAIR
DATE: 22 February 1988

CHANCELLOR

cc Principal Private
Secretary
Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Sedgwick
Mr Odling-Smee
Mr Riley
Miss Evans
Mr A Hudson
Mr Cropper
Mr Tyrie
Mr Call

Mr Battishill
Mr Issac - IR
Mr Calder
Mr Painter

Mr Unwin - C&E
Mr Knox

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a
Some comment.

AA

And some from Mr. M.

B.L.O.

FSBR CHAPTER 4

I attach a draft Chapter 4 of the FSBR, plus Table 4.1 and the Annex.

2. It would be very helpful to know if you are content with the narrative section. This describes in summary form the significant tax changes. You will see that in the case of covenants and forestry the reader is referred to Chapter 5 for details of the parallel public expenditure measures. Non-tax and non-public expenditure measures - such as disclosure of importers' details - will not be mentioned in the FSBR.

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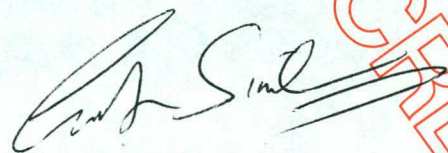
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3. You asked us to include a section on independent taxation, setting out a clear summary account of the reform in reasonable detail (Mr Hudson's minute of 15 February). This is currently at the end of the narrative section. The printers should be able to get it all on to one page. If you wished, it could be put in a box, or all printed in heavy type, in either case without paragraph numbers. We think it comes most naturally at the end of the narrative.

4. You will want to note that we have shortened and revised the first part of the introduction to the Annex to Table 4.1. We have moved away from suggesting that the Inland Revenue and Customs and Excise adopt different approaches to costing tax changes. The new formula on all taxes other than VAT and excise duties is designed to leave you maximum freedom of manoeuvre to include, or not include, assumptions about behavioural response in the FSBR.

5. The attached draft of Table 4.1 takes behavioural effects into account in costing the CGT changes and independent taxation (both the effects on income tax and CGT receipts). This is explained in the accompanying notes. Behavioural assumptions have also been made in the case of the BES costings, although these are largely guesswork. They are not explained in the notes, which simply say that the cost depends on take-up and is highly uncertain.

6. Papers will be coming forward this week on the behavioural effects which may be expected as a result of other tax changes, such as increasing the car scales and abolishing relief for home improvement loans. We shall offer you advice on whether these should also be taken into account and explained in the FSBR, though on the whole we doubt if they warrant this.



CAROLYN SINCLAIR

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*OK, but
if it can
be boxed &
kept on
page, p. 10*

?

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4 The Budget tax proposals

4.01 The main tax changes proposed in the Budget are summarised below. A full list of changes is given in Table 4.1

Make this new para numbers

Income tax

4.02 The basic rate of income tax will be reduced to 25 per cent. There will be a single higher rate of income tax of 40 per cent. ~~The scale of charge will be:~~

Rate of tax per cent	Taxable income £
25	1-20,000
40	above 20,000

This looks odd

4.03 The main income tax personal allowances will be increased by twice the amounts due under the statutory indexation provisions (based on the increase of 3.7 per cent in the RPI in the year to December 1987). This will mean that:

the single person's and wife's earned income allowances will rise from £2,425 to £2,605;

the married allowance will rise from £3,795 to £4,095;

the age allowance for those aged 65 to 79 will rise from £2,960 to £3,180 (single) and from £4,675 to £5,035 (married);

the age allowance for those aged 80 or over will rise from £3,070 to £3,310 (single) and from £4,845 to £5,205 (married);

the income limit for age allowance will rise from £9,800 to £10,600;

the additional personal allowance and widow's bereavement allowance will rise from £1,370 to £1,490.

4.04 The housekeeper allowance, dependent relative allowance and the allowance for the services of a son or daughter will be abolished.

Which will apply to taxable income over £20,000.

may need amending to 10% option.

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talk to march space, I think

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4.05 From [6 April 1989] an unmarried couple will not be entitled to more than one additional personal allowance. ^{claim}

Life assurance premium relief

4.06 The rate of premium relief for life assurance policies taken out before 14 March 1984 will be reduced to [12½ per cent] from 6 April 1989.

Benefits in kind

4.07 Car benefit scale charges for 1988-89 will be set at twice their 1987-88 levels, and for 1989-90 they will be increased by 10 per cent above the 1988-89 levels.

[Should we spell out new levels?]
Baker H. H. H. 'at least' or omit, depend on context.

4.08 The gross income threshold above which employees are liable to tax on certain benefits will be raised from £8,500 to £10,000.

(the "PIID limit")

4.09 The exemptions from tax for luncheon vouchers up to the value of 15p per day, and for the benefit of meals provided at less than cost by an employer in a canteen or dining room not available to staff generally will be withdrawn from 6 April 1989.

? A car park

yes (v consolidated) simplify

Mortgage interest relief

4.10 For loans taken out from 1 August 1988, tax relief for two or more people borrowing to buy the same property as their only or main residence will be limited to the interest on £30,000 in total for the residence. Relief on new loans for home improvements and new loans for the purchase of residences for dependent relatives and divorced or separated spouses will be abolished from 6 April 1988.

[I had not picked this up before. Should you mention BPM?]
yes - in mortgage covenants

The tax treatment of covenants will be reformed and simplified.

4.11 Non-charitable covenants made by individuals on or after Budget day will no longer attract tax relief. Relief for covenants made before Budget Day will continue. There will be parallel changes in the student grant system (see paragraph 5[]). Covenants to charities will not be affected, nor will non-charitable covenants made before Budget day.

and income from (such) covenant made after Budget day will not be taxable in the hands of the recipient.

Charitable giving

4.12 The limit on charitable donations qualifying for tax relief under the payroll giving scheme will be increased to £240 a year from 1988-89.

Maintenance payments

4.13 The tax treatment of maintenance payments will be reformed. Under new maintenance arrangements recipients will not be liable to tax on the payments; relief for those making payments will be restricted to payments to a divorced or separated spouse, up to a limit of

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£1,490

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[£2,605]. Transitional provisions will be introduced to protect existing maintenance arrangements.

Employee share schemes

4.14 [From 6 April 1989, options granted under an approved discretionary share option scheme will only qualify for tax relief if the company also operates an approved all-employee share or share option schemes.]

Income tax charge

4.15 Following consultation last year, the scope of the income tax charge on unapproved employee share schemes under Section 79 of the 1972 Finance Act will be reduced.

Trusts

4.16 The additional rate of income tax on discretionary trusts will be [abolished from 1988-89] reduced to ~~xx~~ per cent for 1988-89.

Capital gains

4.17 The capital gains tax annual exempt amount will remain at £6,600 in the case of individuals and £3,300 in the case of most trusts.

(to be deducted)

4.18 The base date for capital gains will be brought forward from 6 April 1965 to 31 March 1982; The present indexation provisions will continue to apply to gains accruing from 31 March 1982. The proposal will also apply to companies' gains.

gains made before that date will no longer be liable to tax.

4.19 Gains, after deduction of the exempt amount and allowing for rebasing to 1982 and indexation, will be added to income and taxed at income tax rates (as if they were the marginal slice of income).

4.20 From 6 April, 50 per cent of any gains between £125,000 and £500,000 will qualify for retirement relief, subject to the general conditions for the relief.

Inheritance tax

4.21 From Budget Day the threshold will be increased from £90,000 to £107,000. Chargeable transfers above this amount will be taxed at a single rate of 40 per cent.

for inheritance tax

£100,000

This is v high profile

4.22 The limit on the amount which can be given to a political party without incurring IHT will be removed.

The limit on the amount that can be given to a political party without incurring inheritance tax will be abolished.

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Business tax

4.23 The ~~small companies'~~ rate of corporation tax will be reduced to 25 per cent. The rate of advance corporation tax (ACT) will go down automatically to 1/3 as a consequence of the reduction in the basic rate of income tax.

4.24 The main rate of corporation tax for the financial year 1988 will be 35 per cent.

4.25 [The ceiling above which capital allowances on cars are restricted will be increased from £8,800 to [£10,000] for expenditure after 15 March 1988.]

4.26 The cost of entertaining ~~overseas customers~~ ^{businessmen or overseas suppliers} will no longer be an allowable business expense for tax purposes. This change will take effect from Budget Day, except for commitments entered into before that date. From 1 August 1988 the VAT paid by businesses on this entertainment will no longer be deductible.

4.27 A number of changes will be made to prevent tax charges arising on the conversion of building societies into public limited companies.

4.28 The Business Expansion Scheme will be changed to permit relief on investment in companies providing private rented housing.

4.29 A general limit of [] will be set on relief under the Business Expansion Scheme for investment in any one company in any period of twelve months, with a higher limit of [] for investment in companies providing private rented housing, ^{or shipping.}

4.30 Changes will be made to the present administrative arrangements for taxing members of Lloyd's.

4.31 The legislation on Lloyd's reinsurance to close will be modified to give relief to Lloyd's members who leave syndicates at the end of the underwriting year.

Forestry

4.32 Income from the occupation of commercial woodlands will be removed from the scope of Income Tax and Corporation Tax. (See paragraph [5.] for details of the proposed increase in grants for forestry.)

In common with other business entrepreneurs,

✓ Too flat - needs expanding
Business Expansion Scheme

Is this the way to go here?

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Oil taxation

4.33 Oil allowance for Petroleum Revenue Tax (PRT) will be reduced to 100,000 tonnes per chargeable period for all Southern Basin and onshore fields given development consent on or after 1 April 1982. (At the same time the Secretary of State for Energy proposes to abolish royalty payments for these fields.)

4.34 A new capital gains relief will be provided for disposals of oil licence interests in undeveloped areas wherever the consideration includes a work programme or another licence interest.

Company residence and migration

4.35 Section 482(1) (a) and (b) of the Taxes Act will be repealed with effect from Budget Day. In future companies will not need to apply to the Treasury for consent to move their residence abroad for tax purposes. The proposed new arrangements will:

extend the definition of UK company residence, so that companies either incorporated in the UK, or centrally managed and controlled here, will be deemed to be resident here for tax purposes;

require UK incorporated companies wishing to change their residence to change the country of their incorporation and to pay any tax arising on doing so; and

require UK resident companies not incorporated here wishing to change their residence to provide for the payment of their tax (including tax on accrued gains) before they do so.

*Shorten considerably?
rjw*

Keith Report

4.36 Following recommendations of the Keith Committee, a number of changes will be made to encourage people to notify the Inland Revenue if they are liable to tax. These include the introduction of a tax-geared penalty for failing to notify liability. There will be changes to the information powers of the Inland Revenue to help identify those who fail to notify liability to tax.

4.37 Legislation will be introduced to charge interest where payment to the Inland Revenue of income tax deducted by employers is delayed beyond the end of the tax year. The interest charge will be implemented when the necessary Inland Revenue computer systems

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are in place. [There will be parallel social security legislation to extend the interest charge to late payment of Class I or Class IV National Insurance contributions.]

VAT

4.38 From 16 March 1988 the registration limits will become £22,100 per annum and £7,500 per quarter.

4.39 The VAT civil penalty system, introduced in 1985, has been reviewed and various amendments are proposed. These include the introduction of a time-related penalty for late registration; the halving of daily penalties; changes to the rules about eligibility to repayment supplement; and changes to the rules for persons who persistently misdeclare their liability.

4.40 The provision for applying VAT to confectionery will be ^{amended} brought up-to-date with the main effect of taxing all cereal bars at the standard rate.

Excise duties

4.41 The duty on beer, light wine and sparkling wine will rise by the equivalent of [1p] on a typical pint of beer, [4p] on a bottle of table wine and a little over [6p] on a bottle of sparkling wine (all inclusive of ~~consequential~~ VAT). The duties on spirits and fortified wines will remain unchanged. The minimum duty charge for beer will be abolished and provision will be made for restructuring the duties on low strength mixed drinks.

4.42 The duty on leaded petrol will be increased by the equivalent of [just over 5½p] a gallon (inclusive of ~~consequential~~ VAT). The duty on unleaded petrol will remain unchanged. The duty on derv will rise by the equivalent of [just under 5p] a gallon.

4.43 The specific duties on cigarettes, hand-rolling tobacco and cigars will rise by the equivalent of [over 3p] on a packet of 20 cigarettes and [nearly 2p] on a packet on 5 small cigars. The duty on pipe tobacco will remain unchanged.

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Do we need this?
probably - check

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**Independent
taxation for
married couples**

The present system of taxing husbands and wives, under which a married woman's income is treated in law as if it belonged to her husband, has been unchanged since the earliest days of income tax. Green Papers published in 1980 and 1986 have considered how the system might be reformed. There is general agreement that the present law is no longer acceptable, and wide support for an early change to a new and more up-to-date system.

A major reform of the system is therefore proposed to give husbands and wives independence and privacy in their tax affairs and remove the tax penalties on marriage which can occur under the present system. The new system will be introduced from 6 April 1990 to give the Inland Revenue time to make the necessary preparations.

From 6 April 1990, husbands and wives will be taxed independently on their income and chargeable capital gains. This will mean that:

husband and wife will become independent taxpayers each with their own allowances and rate-bands to set against their own income (from whatever source); each will be responsible for handling their own tax affairs with the Inland Revenue;

every taxpayer will be entitled to a personal allowance, equivalent to the existing allowance for single people;

there will be a new married couple's allowance (equal to the difference between the present married allowance and the single allowance). This will be set first against the husband's income, but any unused amount may be transferred to the wife;

married women will qualify in their own right for the higher levels of personal allowance for taxpayers aged 65-79 and those aged 80 or over. Higher levels of married couples allowance will apply where either partner in a couple is aged 65-79 (or aged 80 or over).

there will be transitional protection for the small number of couples whose allowances would be reduced as a result of the change to the new system;

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a husband's and wife's capital gains will be taxed independently; each spouse will be entitled to the same exempt amount as a single person;

the existing exemptions from capital gains tax and inheritance tax on transfers of capital between husband and wife will continue;

the new system will mean that a number of provisions, including the wife's earnings election and separate assessment, can be abolished.

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Table 4.1 Direct effects of changes in taxation

£ million

See Annex 4
Paragraph numbers

Estimated effect on receipts in:		1989-90
1988-89	1988-89	1989-90
Changes from a non-indexed base	Changes from an indexed base	Changes from an indexed base

for? start +10

Income tax and corporation tax

36 Forestry - removal of commercial woodlands from scope of tax	-	-	*
37 (Personal pensions - minor changes)	[-10	-10	-5]
38 Refunds of employee pension contributions	+15	+15	+15
39 Occupational pensions - minor amendments	-	-	-
40 End of year interest on PAYE and subcontractors deductions	-	-	-
41 Capital allowances - motor cars	*	*	-30
42 Capital allowances - exempt persons	-	-	-
43 Capital allowances - safety at sports grounds	*	*	*
44 Capital allowances - abolition of quarantine premises relief	*	*	*
45 Withdrawal of relief for entertaining overseas customers <i>business</i>	*	*	+5

Income tax, corporation tax and capital gains tax

46 Rebasing capital gains to March 1982	-25	-25	-340
47 Keith Committee administrative changes	+10	+10	+20

This shd be split in 2, one for CT & one for CGT, each in appropriate section

Income tax, corporation tax, capital gains tax and stamp duties

48 Conversion of building societies into public limited companies - changes in tax rules	-	-	-
--	---	---	---

Corporation tax

49 Reduction in rate of ACT to 1/3 rd of the amount of the distribution	-380	-380	-200
50 Reduction in small companies' rate to 25 per cent	*	*	-50
51 Company residence and migration - new rules	-	-	-
52 Definition of an investment trust	-	-	-
53 Indexation allowance - intra-group transactions	-	-	-
54 Intra-group share exchanges	-	-	-
55 Capital allowances - assured tenancies relief	-	-	-

surely we should get in Budget speech! right!

Corporation tax and capital gains tax

56 Rollover relief <i>for</i> on satellites, spacecraft, milk and potato quotas	*	*	-5
---	---	---	----

Capital gains tax

57 Charging gains of individuals and trusts at income tax rates	+70	+70	+40
58 Annual exempt amount	-	-	+10
59 Retirement relief	-	-	-10
60 Building and Co-operative society shares	*	*	*
61 Homes provided for dependent relatives	-	-	*

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* = Negligible - = Nil

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Table 4.1 Direct effects of changes in taxation

		£ million		
		Estimated effect on receipts in:		
		1988-89	1989-90	
See Annex A Paragraph numbers		Changes from a non-indexed base	Changes from an indexed base	Changes from an indexed base
Oil taxation				
62	Reduction in PRT oil allowances for certain fields	+30	+30	+30
63	New capital gains relief for certain oil licence disposals	-5	-5	-5
64	Petroleum revenue tax relief for certain tariff related costs	-	-	-
Inheritance tax				
65	Changes to rates and bands <i>spell out</i>	-110	-90	-180
66	Abolition of limit on gifts to political parties <i>increase in threshold → change of rate</i>	*	*	*
Stamp duties				
67	Stamp duty and reserve tax on paired shares	-	-	-
TOTAL INLAND REVENUE		-4760	-3895	-6020
CUSTOMS AND EXCISE				
Value added tax				
68	Keith Committee - review of civil penalties	*	*	*
69	Increase in registration limits	*	*	*
70	Revised registration requirements	*	*	*
71	Change in liability of certain confectionery	+5	+5	+10
72	Revision of approved self-billing arrangements	+5	+5	+5
73	Revised treatment of business entertainment for overseas customers	*	*	*
Excise duties				
74	No change in rate of spirits duty	-	-25	-30
75	Increase in rate of beer duty	+80	+20	+20
76	Abolition of minimum duty charge for beer	*	*	*
77	Increase in rate of duty on cider and perry	+5	+5	+5
78	Increase in rate of duty on light wine and made-wine duties	+20	+5	+10
79	No change in rates of duty on fortified wines	-	-5	-5
80	Revised duty regime for low strength mixed drinks	*	*	*
81	Increase in rate of duty on leaded petrol etc <i>Should there be a 'no change' on unleaded petrol?</i>	+275	+80	+50
82	Increase in rate of duty on dery	+75	+25	+30
83	No change in rates of minor oil duties	-	-5	-5
84	Increase in rates of duties on cigarettes, hand-rolling tobacco and cigars	+100	-	-
85	No change in rate of duty on pipe tobacco	-	*	*
TOTAL CUSTOM AND EXCISE		+565	+110	+90

* = Negligible - = Nil

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Table 4.1 Direct effects of changes in taxation

£ million

Estimated effect on receipts in:		
1988-89	1989-90	
Changes from a non-indexed base	Changes from an indexed base	Changes from an indexed base

See Annex 4
Paragraph numbers

Vehicle excise duty

86	No change in VED on car, light van and main lorry rates	-	-100	-105
87	Increase in certain other VED rates	+15 +20	+15 +20	+20
88	New VED class for exceptional loads	*	*	*
Other				
89	Bus fuel grants	-5	*	-5
TOTAL VED AND OTHER		+10	-85	-90
TOTAL CHANGES IN TAXATION		-4185	-3670	-6020

* = Negligible - = Nil

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Annex to Chapter 4

How the figures in Table 4.1 have been calculated

Table 4.1 gives the direct effects of changes in taxation. Estimates are rounded to the nearest £5 million. "Negligible" means less than £3 million.

The direct effect of a tax change is the difference between the yield of the tax which would arise on the basis of the rate of tax, allowances, etc prevailing before the Budget (the pre-Budget regime) and the yield after the changes proposed in the Budget (the post-Budget regime).

In the case of VAT and the excise duties the calculation takes into account, where possible, the effect of the tax change on the pattern of consumers' expenditure and the resulting impact on other expenditure taxes but makes no allowance for secondary effects: in particular, it is assumed that total consumers' expenditure does not change. A fuller description of the methodology is in Economic Trends, March 1980. First round behavioural responses are also taken into account in the case of some direct taxes.

Table 4.1 shows the expected change in receipts of tax resulting from the Budget proposals. Additional information is provided in the commentary below for those proposals where the effect on tax liabilities in the first complete year to which the change applies (full year effect) is substantially different from the effect on receipts in either 1988-89 or 1989-90; or where the impact of the proposal is expected to build up over a period of years.

The figures in the first column of Table 4.1 show the direct effect of the Budget proposals on receipts in 1988-89. Budget proposals are compared with a non-indexed base - that is, with the pre-Budget regime of allowances, thresholds and rates of duty at 1987-88 levels.

The figures in the second column show the direct effect of the Budget proposals on receipts in 1988-89, measured against an indexed base. The indexed base for 1988-89 is obtained by increasing 1987-88 allowances, thresholds and rates of duty by 3.7 per cent, the increase in the RPI over the year to December 1987.

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*PSR UK
Same word as last year
[This miss more questions than it answers - last year's letter, even it makes differences explicit]*

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The figures in the third column show the direct effect on receipts in 1989-90, also measured against an indexed base. For this comparison, both the Budget proposals and the indexed base for 1988-89 have been further indexed by the forecast movement in the RPI between the fourth quarters of 1987 and 1988 (shown in Table 3.13).

The estimates shown in Table 4.1 do not reflect changes in the tax base arising from changes in money incomes and in the general level of prices and other economic variables which may result from the proposed tax change. These secondary effects are, of course, taken into account in estimating the impact of the tax change on the PSBR. The base for the post-Budget forecast of each tax (given in Table 6B.3) takes account of the effects, direct and secondary, of all the measures announced in the Budget.

Table 4.1 does not include certain measures announced and implemented before Budget day. These are the tax treatment of entertainment and gifts costing £100 or less provided for an employee by someone other than his employer, and the correction to the treatment for capital gains tax of losses incurred in a personal equity plan. [Other possibilities.] These measures are reflected in the baseline for costing the effect of tax changes in the Budget.

The remainder of this annex provides a commentary on the Budget proposals in Table 4.1. The paragraph numbers refer to the lines in this table.

Is this wrong?

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Income tax

1 and 2. The basic rate will be reduced to 25 per cent and there will be a single higher rate of 40 per cent.

*NB
(same as
last year)*

//

The cost figures in the table for items 1 and 2 assume that the changes in items 3-8 have been made first. Item 1 includes the saving in public expenditure on mortgage interest relief to those below the tax threshold. The effect of the consequential change in the rate of advance corporation tax (ACT) is shown in line [4⁹] of Table 4.1.

*NB different
treatment - but
direct rather than
discretionary change*

3 to 7. The increases in the main income tax personal allowances are twice those due under statutory indexation (based on the increase of 3.7 per cent on the RPI in the year to December 1987).

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8. The basic rate limit will rise from £17,900 to £20,000. The increase is ~~£1,400 more than the~~ amount due under statutory indexation.

check/

three times the

9. The housekeeper allowance, dependent relative allowance and the allowance for the services of a son or daughter will be abolished.

10. From [6 April 1989] an unmarried couple will not be entitled to more than one additional personal allowance.

11. Following the reductions in the basic rate of income tax in successive Budgets, the rate of relief for life assurance premiums on policies taken out before 14 March 1984 will be reduced to [12.5] per cent from 6 April 1989. The starting date is to allow life offices time to make the necessary preparations.

from 15 per cent

12. For 1988-89 the scale for taxing car benefits in respect of company cars provided for directors and for higher paid employees will be double the 1987-88 levels. The previously announced scales for 1988-89 will not apply. Costs are measured from these previously announced scales. [A further increase of 10 per cent will be made for 1989-90.] [No change is proposed for 1988-89 and 1989-90 to the scale charges for car fuel benefit also used for VAT purposes.]

not less than

13. For 1988-89 the rate of remuneration at which an employee is regarded as higher-paid and liable to tax in respect of certain benefits received by reason of his employment is to be increased from £8,500 to £10,000.

(the 'PIID' limit)

14. [The provision of a car parking space for the use of directors or higher-paid employees ~~on premises occupied by the employer~~ will be exempt from tax from 6 April 1988.]

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15. [The extra-statutory concession exempting from tax luncheon vouchers up to the value of 15p a day will be withdrawn with effect from 6 April 1989. The exemption from tax of the benefit of subsidised meals provided by an employer for directors and higher-paid employees in a canteen or dining room which is not open to the staff generally will also be withdrawn from the same date.]

16. [The benefit to employees of sports facilities provided on premises occupied by the employer and available to the staff generally will be exempt from tax from 6 April 1988.]

17. For loans taken out from 1 August 1988, tax relief for two or more people borrowing to buy the same property as their only or main residence will be limited to the interest on £30,000 in total for the residence.

18. Relief on new loans for home improvement will be abolished from 6 April 1988. Relief for existing loans [and for loans for the purchase or improvement of let property] is not affected.

19. Relief on new loans for the purchase of residences for dependent relatives and divorced or separated spouses will be abolished from 6 April 1988. Relief for existing loans is not affected.

20. Non-charitable covenants made on or after Budget day by individuals will no longer be effective for tax purposes. The change is estimated to yield £160 million in 1990-91, £175 million in 1991-92, and £[210] million eventually.

21. The limit on charitable donations qualifying for tax relief under payroll giving schemes will be increased to £240 a year from 6 April 1988.

Where do we set limit @ 700,000?

Make 2 Separates Schemes

✓ Must spell out what is cf maintenance let

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22. A new tax regime will be introduced for maintenance payments:

- for payments under new maintenance arrangements, relief will be restricted to payments to a divorced or separated spouse, up to a limit equal to the single allowance. Recipients will not be liable to tax on maintenance payments;

- for existing maintenance arrangements, in 1988-89 the present rules will continue to apply [except that a divorced or separated spouse will be exempt from tax on the first [£2,605] (the single allowance) of maintenance received (after grossing up at the basic rate where tax has been deducted by the payer). From 1989-90, all payments will be made gross and relief for the payer will be limited to the amount which qualified for relief in 1988-89.]

To be decided ✓

The changes are estimated to cost £15 million in 1990-91 and £10 million in 1991-92, and to yield £20 million eventually.

23. The additional rate of income tax charged on the income of discretionary and accumulation trusts will be ~~abolished~~ reduced to 10 per cent from 1988-89].

24. The legislation on Lloyd's reinsurance to close (RIC) will be modified so that it will not apply to Lloyd's members who ceased membership of a syndicate at the end of the underwriting year, and are therefore not members of the syndicate to which the relevant RIC premium is paid. [The legislation will first take effect for the Lloyd's 1985 Account, which closes at the end of 1987. This is the first year to which the 1987 legislation on Lloyd's RIC will apply].

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25. The administrative arrangements for the assessment and collection of tax from members of Lloyds will be reformed. [The legislation will first take effect for the Lloyd's 1986 Account, which closes at the end of 1988].
26. [The entitlement of discretionary share option schemes to approval and to the associated tax relief will be denied and existing approvals will be withdrawn in cases where the company concerned has not introduced an approved all-employee share scheme and does not operate it to the required extent.]
27. Changes will be made to the rules (Section 79 Finance Act 1972) governing unapproved employee share schemes. The present charge (to income tax) on the whole of any growth in value of certain employee-acquired shares is to be replaced in most cases with a new, more narrowly targeted charge that will arise only if and to the extent

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that value is shifted preferentially into the employee shares. This relaxation will also apply to shares in "qualifying" subsidiaries. These changes will take effect from 26 October 1987 when draft Clauses incorporating the proposed changes were published for consultation.

28. Subject to certain conditions, employees will be exempt from tax on any benefit resulting from priority in applying for public offers of shares given to them by virtue of their employment. The change will apply from 23 September 1987.
29. The legislation relating to approved discretionary share option schemes will be changed to enable employees to enter into certain loan arrangements regarding the shares they have under option without prejudicing their eligibility for the tax relief associated with such schemes.
30. The limit below which redundancy and certain other lump sum payments are exempt will be increased from £25,000 to £30,000. The reduced rates of tax which apply to the next £50,000 of such payment will be abolished.
31. Legislation will be introduced to ensure that the Inland Revenue continue to have power to make an income tax assessment, on certain types of income assessable on the "current year" basis, in the course of the year in which the income is received.
32. The "top-slicing" relief which applies to the tax charged on premiums for leases and certain other payments will be withdrawn.

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✓ This was drafted before we saw Mr Taylor's minute of 22 February to Mr Eason.

33. The new system of independent taxation for husbands and wives will apply from 1990-91. The revenue costs in 1990-91 and 1991-92 for income tax are estimated at £[630] and £[970] million respectively. These figures are based on the existing distribution of income between husbands and wives and allow for transitional protection for certain couples. [In addition, there could be further annual revenue costs of some £[350] million resulting from the transfer of investments between spouses, but this estimate is highly uncertain.] For capital gains tax, the prospect of independent taxation may lead some couples to defer disposals until the new arrangements are in place; and from 1990-91 onwards, couples may be expected to transfer assets to take advantage of the availability to each spouse of the annual exempt amount and any unused portion of their basic rate bands. The figure for 1989-90 in table 4.1 reflects the deferral of disposals. Costs for capital gains tax in 1990-91 and 1991-92 are each estimated at £60 million. Those estimates which allow for changes in taxpayers' behaviour are subject to a high degree of uncertainty.

34. A general limit of [£500,000] will be set on the amount of investment in any one company in any period of 12 months qualifying for relief under the Business Expansion Scheme. The estimated yield ^{depends on take up and} is highly uncertain.

35. Relief under the Business Expansion Scheme will be made available for investment in companies providing private rented housing [under the new assured tenancy scheme]. A limit of [£10 million] will apply to qualifying investment in these companies. The estimated revenue cost depends upon take up and is highly uncertain.

??
What is higher limit or shop? /
x Mr
BS minutes

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36. Schedule B will be abolished with effect from 1988-89. With effect from 15 March 1988 (subject to transitional provisions extending to 5 April 1992) the right of occupiers of commercial woodlands to elect to be assessed to tax on their profits or losses under Schedule D will be abolished. The eventual net annual saving is estimated at [£10 million]. [Provision for increased forestry grants will be introduced as from [], building up over this period to an annual increase of £10 million.]
37. [Changes will be made to the tax rules for personal pensions relating to the payment by DHSS of contracting-out rebates.]
38. The rate of tax on refunds of employee pension contributions will be increased from 10 per cent to 20 per cent.
39. Minor amendments are to be made to the 1987 legislation which dealt with exploitation of pensions tax reliefs.
40. Interest will be charged where an employer or contractor delays payment to the Inland Revenue of amounts deducted under the PAYE or subcontractor deduction schemes beyond 19 April immediately following the deduction year. This interest charge will not be introduced before 1992.
41. From expenditure after 15 March 1988 the ceiling above which capital allowances and lease rental payments for cars are restricted will be increased from £8,000 to [£10,000] and the maximum annual writing-down allowance will be increased from £2,000 to £2,500. The cost could build up to £50 million in 1990-91, and to £60 million in 1991-92.

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42. The rules for calculating industrial buildings allowance following a sale and those for transfers of machinery or plant between connected persons will be amended to prevent excessive relief where one person is not chargeable to tax in the United Kingdom. These changes will prevent a potential Exchequer loss of up to £150 million in 1991-92 with a diminishing effect in later years.]

43. The legislation relating to capital allowances for safety expenditure at sports grounds will be amended from 1 January 1988 to take account of changes to the Safety at Sports Grounds Act 1975.

44. Capital allowances on expenditure at certain quarantine premises will be abolished from 16 March 1988.

45. The relief for the costs incurred by a business in entertaining overseas customers ^{or suppliers} will be withdrawn.

46. The base date for capital gains tax and corporation tax on gains will be changed from 6 April 1965 to 31 March 1982. The total cost of rebasing will build up to some £850 million in 1991-92. From 1989-90 onwards, the amount attributable to companies' gains is about three-quarters of the total. The figures take account of the likely effect of this measure on the volume and timing of disposals by individuals and companies.

47. (a) The present flat rate penalty for failure to notify liability to tax will be replaced by a fully mitigable penalty up to the amount of tax unpaid.

(b) The Revenue's power to call for returns of information will be extended to details (where relevant

What is this (v. high) fig?
Cumulative total?
If so, we don't want this. Or the peak year? You, it shd say so.

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for tax) of payments for services by Government Departments, grants or subsidies paid out of public funds and the names of licence holders.

(c) The Revenue's power to call for documents relating to taxpayers suspected of avoidance or evasion will be extended to include the Department of National Savings, and, in order to identify taxpayers suspected of serious default, to documents relating to taxpayers whose identity is not known to the Revenue.

(d) The Revenue will be allowed the same access to records held on computer as it is allowed to records held on paper.

The ~~estimated~~ yield of these measures is based on the unreported tax liabilities which will be uncovered.

an estimate of

48. Changes in the tax rules concerning the conversion of building societies into public limited companies are necessary in order to prevent unintended tax charges arising.
49. As a consequence of the reduction in the basic rate, the rate of advance corporation tax (ACT) for 1988-89 will be 1/3rd of the amount of the distribution. This reduction in ACT will be balanced by an increase in the subsequent liability to mainstream corporation tax.
50. The small companies' rate of corporation tax for the financial year 1988 will be reduced to 25 per cent.
51. [The rules for company residence and migration will be changed. In future companies will be resident for tax purposes if they are incorporated or are centrally managed and controlled here. Companies will be able to migrate if they pay their tax liability, including liability on accrued gains.]

*Contrast with
✓ long explanation,
↳ main chapter!
Right. Much better*

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*BUDGET
What's
this?*

52. The Finance (No 2) Act 1987 repealed part of the definition of an investment trust. The full definition will be reinstated, and the legislation will include provision to ensure that the repeal was never effective.
53. The indexation allowance will be denied or restricted on disposal of certain intra-group debts and shareholdings. This provision counters use of the indexation allowance to create large artificial capital losses which could cause a significant loss of tax.
54. As a result of a recent court ruling, share exchanges by companies in the same group can now give rise to capital gains or losses being taxed or allowed more than once. The legislation will be amended so as to remove that anomaly.
55. Capital allowances in respect of properties let on assured tenancy terms by "approved bodies" will come to an end when the Housing Bill takes effect. Changes will be made to the capital allowances legislation to ensure that relief for past years is not withdrawn and to provide transitional arrangements in respect of expenditure already incurred.
56. Rollover relief will be extended to satellites and spacecraft from 28 July 1987 and to milk and potato quotas from 30 October 1987.
57. From 1988-89, the capital gains of individuals and trusts will be taxed at income tax rates, that is as if they formed the marginal slice of income. The revenue yield in 1990-91 is estimated at £40 million and in 1991-92 at £85 million. The figures take account of the effect of rebasing of gains (item [46] above) and of the likely effect of taxing gains at income tax rates on the volume and timing of disposals.

Why is this so far down? In para 46? More relevant than 46?

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- BUDGET check!
58. The capital gains tax annual exempt amount for 1988-89 will remain at £6,600 for individuals, and £3,300 for most trusts.
59. Retirement relief currently exempts business gains up to £125,000, subject to certain qualifying conditions. From 6 April 1988, half of any business gains between £125,000 and £500,000 will also be exempt, subject to the same conditions.
60. From 4 July 1987, disposals of shares in Building and Co-operative Societies will not qualify for indexation relief.
61. From 6 April 1988, the capital gains tax exemption for homes provided for dependent relatives will cease to be available. There will be special provisions to ensure that exemption continues where a dwelling would have qualified for this exemption on a disposal before 1988-89.
62. The PRT oil allowance for Southern Basin and onshore fields given development consent on or after 1 April 1982 is to be reduced to 100,000 tonnes per chargeable period, with a cumulative total of 2 million tonnes. The yield figures in table 4.1 relate to this proposal only. At the same time, it is proposed to abolish royalty on these fields. These two measures have cumulative cost of around [£40 million] in the first five years [in part because it is estimated that they will accelerate certain developments], but in the long run they are expected to be broadly revenue neutral.
63. For disposals of oil licences in undeveloped areas where the consideration includes a work programme or another licence interest, that work programme or other licence interest will be deemed to have a nil value.

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64. All tariff-related expenditure incurred by an asset owner will be allowed against his PRT liability on tariff income arising from third party use of those assets, even though his principal field has ceased production. No cost will arise until after fields owning assets used by others cease production.
65. The estimated cost of the proposed rate structure in paragraph 4 for 1990-91 is £210 million, measured against the indexed base. For 1991-92 it is £230 million. The estimated full year cost attributable to transfers in 1988-89 is £200 million.
66. The £100,000 exemption limit on transfers to political parties made on or within one year of death is abolished from Budget day.
67. Changes are proposed to stamp duties and the reserve tax on shares in a UK and a non-UK company where the shares are paired and can only be transferred as a unit.
68. Amendments will be made to the civil penalty system so that
- from 16 March, the rate of penalty for late registration will relate to the length of the delay;
 - default interest (to be introduced in late 1989) will not be charged on tax which is also subject to late registration penalty;
 - a penalty for a regulatory offence will only be imposed following issue of a warning letter;

Value added
tax

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- from 16 March, the daily rates of penalty for regulatory offences will be halved and a minimum and maximum level of penalty introduced;
- the third test for serious misdeclaration penalty is to be replaced by a non-automatic penalty which relates to the amount of tax involved;
- VAT registered local authorities and similar bodies will become eligible for repayment supplement and liable to both the serious and the persistent misdeclaration penalties;
- the level of error on a return which excludes eligibility for repayment supplement is to be increased to £250 or 5% of the tax claimed, whichever is the greater;
- from late 1989, adjustments not exceeding £500 in total may be voluntarily declared in the trader's VAT account (such amounts will not normally be liable to either on interest charge or serious misdeclaration penalty).

Do we have to go into such detail? w/h w/h w/h

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69. From 16 March 1988 the registration limits will be increased to £22,100 per annum and £7,500 per quarter.

VAT thresholds

70. The rules for registration of voluntary and intending traders will be simplified and restrictions and conditions removed.

71. The taxing provision relating to confectionery will be brought up-to-date, with the main effect of taxing all cereal bars at the standard rate.

As a main ✓ changes

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72. From [], where a taxable person issues himself with an invoice under the terms of an approved self-billing arrangement, he will be responsible for determining the correct VAT liability.
73. From 1 August 1988, VAT incurred by businesses on entertaining foreign customers will no longer be deductible, to bring it into line with the treatment of VAT on other business entertainment.

*Just that
formulation
also*

Excise duties

74. There will be no changes in the rate of duty on spirits.
75. The duty on typical beer will be increased by [4.7 per cent] equivalent to [1p] a pint (inclusive of consequential VAT).
76. 1 October 1988, beer duty will be charged on the basis of [£0.90] a hectolitre for every degree by which the original gravity of the beer exceeds 1000°.
77. The duty on cider and perry will be increased by [9.7] per cent or [1p] a pint (inclusive of consequential VAT).
78. The duties on still table wine, made-wine and sparkling wine will be increased by [4.7] per cent, equivalent to [4p] on a 75cl bottle of still wine and [6.1p] on a 70cl bottle of sparkling wine (both inclusive of consequential VAT]
79. There will be no change in the rate of duty on fortified wines.
80. Lower strength mixed drinks, not exceeding 5.5 per cent alcohol, will be dutied according to their alcoholic strength on a scale proportionate to table wine duty. This will bring duties on wine-based and similar mixed drinks into line.

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81. The duty on leaded petrol will be increased by [5.5] per cent or [5.6p] a gallon (inclusive of consequential VAT). The duty on unleaded petrol will remain unchanged so that the tax differential in favour of unleaded petrol will rise to [10.6p] a gallon.
82. The duty on derv will be increased by [5.7] per cent, equivalent to [4.9p] a gallon (inclusive of consequential VAT).
83. There will be no change in the rates of duty on gas oil and fuel oil.
84. The specific duties on cigarettes, hand-rolling tobacco and cigars will be increased by [3.7] per cent or [3.4p] a packet of 20 cigarettes and [1.9p] a packet of 5 small cigars (both inclusive of consequential VAT).
85. There will be no change in the duty on pipe tobacco.
86. There will be no change in the duties on cars, light vans, motor cycles, buses, coaches and most lorries.
87. From 16 March 1988 the rates of duty for the heaviest rigid lorries will rise by about 10 per cent bringing them more into line with rates for articulated vehicles of similar gross weight.
88. From 1 June 1988 a new tax class will be introduced for heavy goods vehicles (special types) capable of carrying very long, wide or heavy loads. The rate of VED for these special types will be raised to £1,600. These vehicles cause as much wear and tear as the heaviest HGVs but currently pay a restricted HGV rate (£130).

Vehicle excise
duties

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FROM: COLIN MOWL
DATE: 24 FEBRUARY 1988

CHANCELLOR

cc Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Odling-Smee
Mr Sedgwick
Mr Turnbull
Mr Culpin
Mr S J Davies
Mr Ritchie
Ms C Evans
Mr Cropper
Mr Tyrie
Mr Call

FSBR CHAPTER 6

I attach a draft of FSBR chapter 6.

2. It is consistent with your provisional decisions last Friday on the PSBR totals ie net repayments of £2.9 billion and £3.1 billion in 1987-88 and 1988-89 respectively. The figures for the components are also provisional. We are still discussing the composition of the tax forecast with the revenue departments and will report changes to you. We shall also need to take into account some information that is still coming in, for example on local authority rating decisions.

3. The expenditure figures are also still under review. The draft is based on a planning total outturn in 1987-88 of £146.0 billion, the figure in Mr Sedgwick's submission of 18 February on PSBR Prospects in 1987-88 and 1988-89. The draft of chapter 5 by contrast assumes an outturn of £146.4 billion as in GEP's February assessment (GEP commented then that this figure was likely to prove too high). Both chapters will of course ultimately

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cc into line. Both chapters show the same figure for 1988-89, £156.8 billion, as in the 1988 PEWP.

4. The forecast of general government gross debt interest payments has been increased. The forecast now has interest payments flat between 1987-88 and 1988-89. We think it would be difficult to show an increase.

5. The growth rates of taxes and national insurance contributions (NICs), and general government receipts, along with growth rates of money GDP, are shown below.

	1983-84	1984-85	1985-86	1986-87	% changes	
					1987-88	1988-89 Forecast
<u>Non-oil taxes and NICs</u>						
Actual/Forecast	6.6	6.6	9.2	10.9	10.3	8.2
Before Budget changes	8.1	7.8	9.8	11.7	12.2	10.7
<u>Non-oil general government receipts</u>						
Actual/Forecast	5.8	6.1	8.7	10.9	8.9	7.2
Before Budget changes	7.1	6.3	9.3	11.6	10.6	9.5
<u>Non-oil money GDP</u>	7.8	6.4	11.6	9.9	9.9	7.8
<u>Total taxes and NICs</u>						
Actual/Forecast	7.0	8.8	7.8	5.3	9.8	7.3
Before Budget changes	8.5	9.8	8.3	6.0	11.6	9.8
<u>General Government Receipts</u>						
Actual/Forecast	6.2	8.2	7.5	5.8	8.5	6.4
Before Budget changes	7.9	8.2	8.0	6.4	10.1	8.6
<u>Total money GDP</u>	8.1	7.2	9.6	7.0	10.1	7.2

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6. Before Budget changes, non-oil taxes and NICs have increased more than non-oil money GDP in four out of the last five years (including 1987-88); the exception was 1985-86. On average, before Budget changes, non-oil taxes and NICs have grown about ½ percentage point more than non-oil GDP. The forecast for 1988-89 has non-oil taxes and NICs adjusted for Budget changes increasing by 2½ points more than non-oil GDP.

7. doesn't seem to square with table — ngr: psr reconcile

7. The notable feature of recent years has been the prodigious growth in on-shore corporation tax receipts. Growth has been well into double figures for four years. Outside commentators will know that ICC profits in 1987 grew by over 20 per cent in 1987 by the time that the CSO press release on the national accounts comes out on March 18 with numbers in most cases identical to those in the FSBR. There will be some presumption therefore (with which the proposed numbers are just about consistent) that revenues adjusted for the package should rise noticeably more than money GDP. Many outside commentators may not attempt to adjust the recorded figures for earlier years for Budget changes, in which case they may be more liable to query the forecast. The post-Budget forecast of non-oil taxes may look low relative to GDP compared with past experience.

8. The still provisional forecast for the tax burden is as follows:

	1983-84	1984-85	1985-86	1986-87	1987-88	1988-89
<u>Non-North Sea tax burden</u>						
Actual/Forecast	37.8	37.8	37.0	37.3	37.5	37.6
Before 1988 Budget changes						38.4
<u>Total tax burden</u>						
Actual/Forecast	38.5	39.1	38.4	37.8	37.7	37.8
Before 1988 Budget changes						38.6

Alternative but no doubt more plausible, this could be 37.6

Want to get to 37.5 if at all poss. ngr.

Helpful to get this to 37.7 at a consequence

There is a small rise in the non-oil tax burden in 1988-89 on current figuring. We can consider the precise numbers to show for

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1988-89 when revisions to the figures are complete. The illustrative figures consistent with a £3 billion surplus in table 8 (page 16) of Mr Sedgwick's paper of 18 February showed no increase in the non-oil tax burden. This allocated all of the required adjustment to non-oil taxes, while we are now also adjusting oil taxes and debt interest.

9. The structure of chapter 6 is much the same as last year. But you might note the following, mainly minor, changes:

- the discussion of the alternative ways in which public sector finances can be analysed (paragraph 6.03) is much shorter;
- in chart 6.1 on the structure of receipts and expenditure the total in the left hand panel is now just receipts, rather than receipts and borrowing. It is difficult to include (net) borrowing now that it is negative;
- as you suggested when commenting on chapter 3 we have included a chart (6.2) on the tax burden and ratio of GGE to money GDP. The version included in the body of the text starts from 1978-79, as did the main GGE chart in the PEWP. But we have also included an alternative which starts in 1974-75, giving a reasonable run of years and covering the same period as the PSBR chart in chapter 2;
- the description of the third expenditure item in table 6.4 has been amended to include "cash expenditure on company securities" and is therefore now comprehensive;
- external finance has been added as a memo item to table 6.6;
- in table 6.7 expenditure is now shown as positive. The previous negative sign convention was counter-intuitive and inconsistent with the convention used in virtually all other official statistics;
- similarly Consolidated Fund expenditure in table 6B.1 is now shown as positive.

I suppose this is inevitable

*Stalk
@ 1978-79
Don't like*

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10. Reflecting the latest drafts of the Budget speech we have introduced the term "public sector net debt repayment" (PSDR) into the text. But all the tables retain "public sector borrowing requirement". The PSBR is of course a net borrowing concept, even though the nomenclature does not make this explicit. Moreover it would not be appropriate to make a universal switch to PSDR when PSBR is more relevant for most of recent history.

No need to hurry this PSBR, but money matters for autumn

Conclusion

11. We shall be sending you a final submission on the PSBR and related figures on Wednesday 9 March when the first estimate of the February PSBR will be available. By then we shall need to agree the line to take when asked whether the tax forecasts for the year ahead are central forecasts in the light of economic developments or deliberately "cautious", "prudent" etc.

12. We should be grateful for comments as early as possible on Thursday 25 February so that we can incorporate them in the version to be sent to the printers on Friday.

I have warned them that this deadline is impossible.

Colin Mowl
COLIN MOWL

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The scope of this chapter

6.01 This chapter brings together revenue (discussed in Chapter 4) and spending (in Chapter 5), and provides an analysis and forecast of the public sector's finances in 1988-89 together with estimates of outturn in 1987-88. It also comments on the main features of the public sector's finances in those two years, including the most important changes that have taken place since last year's projections. Table 6.1 is a summary.

Table 6.1 Public expenditure, receipts and borrowing

	£ billion			
	1986-87 Outturn	1987-88 1987 Budget	Latest estimate	1988-89 Forecast
General government expenditure	164.8	173.5	171.6	182.8
General government receipts	160.0	168.8	173.5	184.7
General government borrowing requirement	4.9	4.7	- 2.0	- 1.9
Public corporations' market and overseas borrowing	- 1.5	- 0.8	- 0.9	- 1.2
Public sector borrowing requirement	3.4	3.9	- 2.9	- 3.1

Do you want to do this, in PSBR, or simply refer to negative PSBR?

6.02 There is now estimated to be ~~net~~ ^{a negative} public sector ~~debt~~ ^{summary} requirement, ~~(PSDR)~~ ^{ie a budget surplus,} of about £3 billion in 1987-88, compared with ~~a~~ ^{the} forecast of a ~~public sector borrowing requirement (PSBR)~~ ^{PSBR} of £4 billion made a year ago. This would be the first budget surplus since 1969-70 and only the second since 1952, the earliest year for which PSBR figures are available. ~~There is also forecast to be a~~ ^{budget surplus} ~~net repayment~~ ^{is also forecast} of about £3 billion in 1988-89.

Public sector's finances:

three-fold analysis
much shorter probably better.

6.03 The public sector's finances can be analysed in a number of different ways: by type or activity, by sector and by economic category. The rest of this chapter sets out these three analyses in detail.

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6.04 Table 1.2 analyses the public sector's finances by type or activity. The main receipts of general government (ie. central plus local government) are grouped according to the kind of activity which gives rise to them, while spending is shown by department, as in Chapter 5 and in the public expenditure White Paper. Its bottom line, the PSBR, is derived from those two totals. This derivation is repeated in Table 6.1.

Receipts

in 1987-88
6.05 General government receipts are now projected to exceed the 1987 Budget forecast by about £4³/₄ billion. As Table 1.2 shows, most components of general government receipts are likely to be higher than originally forecast. The main contributors to the extra receipts are income tax (£1 billion), VAT (£1 billion) and North Sea Revenues (£³/₄ billion) and corporation tax (£³/₄ billion).

6.06 Additional income tax receipts are mainly the result of *the stronger growth of the economy & higher incomes.* VAT receipts have increased by more in 1987-88 than would have been expected from the *recorded* ~~currently estimated~~ increase in total consumer spending: *this implies that* either the proportion of total spending *which goes* on goods and services subject to VAT has increased, *that* or estimates of consumer spending in 1987 will be revised up later, ~~as happened last year.~~ The higher than expected oil revenues in 1987-88 are largely the result of a higher *last year* than assumed dollar oil price. ~~Although non-North Sea corporation tax receipts are estimated to be higher than in the 1987 Budget forecast, they are lower than forecast in the 1987 Autumn Statement.~~

6.07 General government receipts are forecast to rise by 6¹/₂ per cent in 1988-89, following an estimated 8¹/₂ per cent increase in 1987-88. This is a little less than the rate of growth

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6-88
further discussed

forecast for money GDP. Without the Budget measures however
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forecast growth in receipts would be about 1½ percentage points
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above that of money GDP.

6.08 Oil revenues, which in the event in 1987-88 were only slightly below the 1986-87 level, are forecast to fall by about £1 billion in 1988-89 ^{as a result of both} [due to] a lower average oil price and lower production. The forecast assumes that ~~sterling~~ [and] oil prices remain close to recent levels. Oil production is assumed to fall in 1988 to a level close to the centre of the Department of Energy's range. A \$1 a barrel difference in the oil price in 1988 would change revenues by about £250 million in 1988-89 and £300 million in a full year. A change of 1 million tonnes in oil production in 1988, spread evenly across fields, would alter revenues by about £40 million in 1988-89 and £45 million in a full year.

6.09 Non-oil receipts are forecast to rise by 7 per cent in 1988-89. As can be seen from Table 1.2 there is within this overall increase:

a 1½ per cent increase in income tax receipts. Without the Budget measures the forecast increase would have been 10 per cent;

a further rise ^{of 3 per cent,} in receipts of corporation tax (including ACT but excluding North Sea mainstream corporation tax).

~~[The 1988-89 increase reflects a provisional estimate of a 25 per cent increase in profits in 1987.]~~

a 16 per cent rise in capital taxes ^{mainly} reflecting rising asset prices in earlier years;

This reflects continued growth
↳ company profits
↳ 1987.

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an 8 per cent increase in VAT, in line with the forecast increase in consumers' expenditure;

a 5½ per cent increase in the excise duties on petrol, tobacco and alcohol, a little below the increase in consumers' expenditure reflecting the trend decline in the share of these items in the total;

a small fall in stamp duty following the fall in stock market prices and turnover.

6.10 Table 6.2 shows taxes (including rates) and national insurance contributions as a percentage of GDP. ~~The non-oil percentage is forecast to increase marginally in 1988-89.~~ Without the Budget measures ~~it would have increased~~ by about one percentage point. *to 1988-89 figure been higher.*

may be amended

in task of

Non-oil taxes have risen slightly as a percentage of non-oil GDP over the last two years, and a further marginal increase is forecast for 1988-89.

Table 6.2 Taxes and national insurance contributions (NICs) as a percentage of GDP

	1982-83	1983-84	1984-85	1985-86	1986-87	1987-88 Latest estimate	1988-89 Forecast
Total taxes and NICs as a share of total money GDP	38.9	38.5	39.1	38.5	37.8	37.7	37.8
Non-oil taxes and NICs as a share of non-oil money GDP	38.2	37.8	37.8	37.0	37.3	37.5	37.6

Expenditure

6.11 General government expenditure is now forecast to be about £171½ billion in 1987-88, £2 billion lower than in the 1987 Budget forecast. *outturn for the* The ~~planning total outturn~~ *in the original plan* is expected to be £2½ billion lower than ~~planned~~ and gross debt interest payments nearly £½ billion lower than forecast. Partly offsetting these is an increase in other national accounts adjustments.

6.12 General government expenditure is expected to rise by 6¼ per cent in 1988-89, to £183 billion. The planning total, at £156.8 billion, *as published* is the same as ~~in~~ the public expenditure

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White Paper (Cm 288) **BUDGET SECRET BUDGET LIST ONLY** **NOT TO BE COPIED** *market*
General government gross debt interest payments in 1988-89 are now forecast to be lower than projected in the White Paper as a result of *the reduction in the PSBR.* ~~lower borrowing and to be at much the same level as expected for 1987-88.~~

Borrowing

6.13 The difference between general government receipts and expenditure is the general government borrowing requirement (GGBR), as shown in Table 6.1. As general government lending to public corporations is included in general government expenditure, the GGBR together with public corporations' market and overseas borrowing, gives the PSBR.

6.14 There was a substantial budget surplus in the first ten months of 1987-88. Excluding privatisation proceeds the PSBR was some £5½ billion lower than in the same period of 1986-87. This reduction in borrowing was almost entirely due to lower central government own account borrowing. Local authority borrowing has been higher than in 1986-87 and public corporations' borrowing little changed. Taking into account the well established pattern of relatively high borrowing in the final two months of the year, the forecast for 1987-88 as a whole is a budget surplus *[or PSBR]* of about £3 billion, or ¾ per cent of ~~money~~ GDP.

X

Further budget surplus
6.15 A *[PSDR]* of £3 billion, or ¾ per cent of ~~money~~ GDP, is ~~also~~ forecast for 1988-89.

Trends in receipts and expenditure

6.16 Chart 6.1 shows trends in taxes and expenditure as percentages of ~~money~~ GDP. *Revenue (from)* ~~The percentage for non-oil taxes and national insurance contributions fell between 1981-82 and 1985-86, but~~ *since then it has been rising.* ~~rose slightly in 1986-87 and again in 1987-88.~~

has risen slightly since then

[It is forecast to rise marginally in 1988-89, ~~to a level below~~ *]*

to be further reduced

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its 1981-82 peak. The ratio of general government expenditure (excluding privatisation proceeds) ^{to GDP} has fallen every year ~~but~~ ^{one} since 1982-83 ~~and~~ ^{is} forecast to fall again in 1988-89.

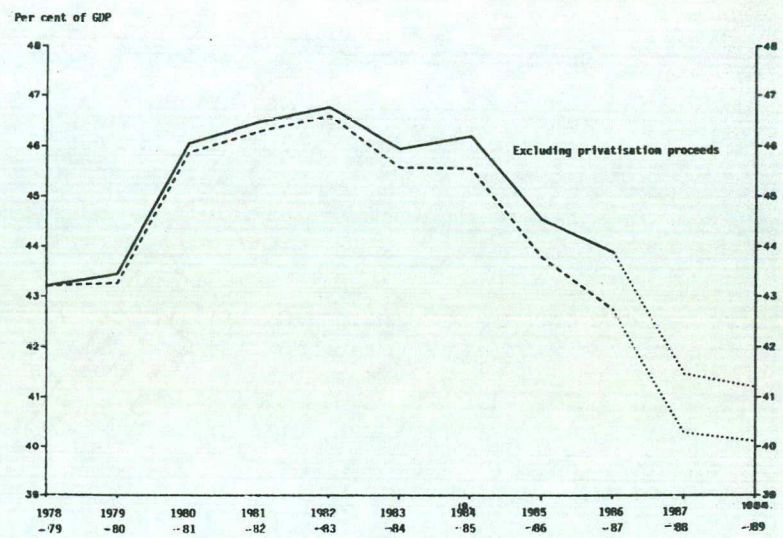
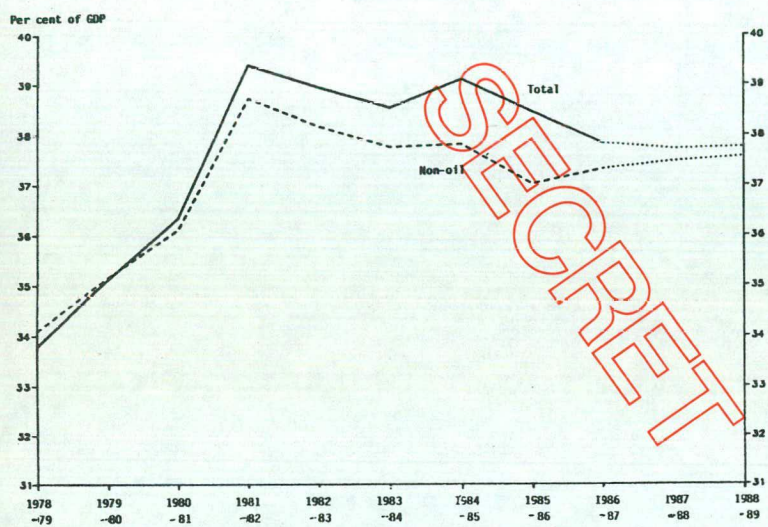
as a percentage of

except for a small rise in 1984-85 as a result of the mines' strike; it

Chart 6.1 Taxes and expenditure ~~relative to~~ GDP

Taxes and national insurance contributions

General government expenditure



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6.17 Chart 6.2 shows the significant changes in the structure of general government receipts and expenditure which have taken place since 1978-79.

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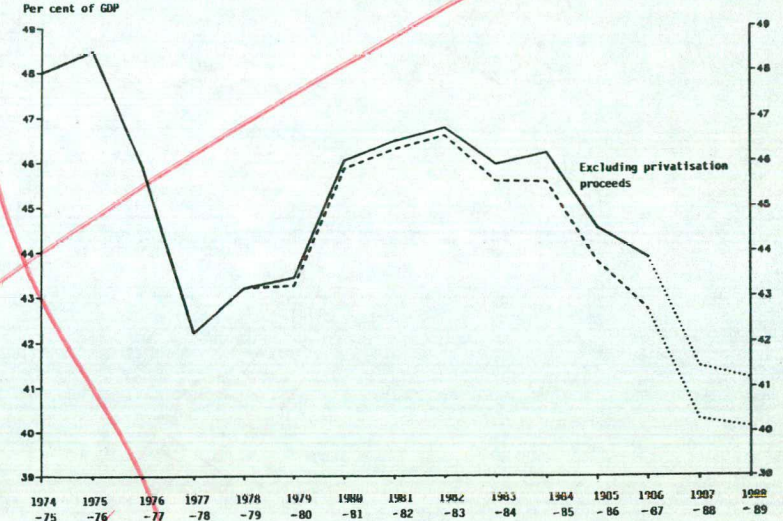
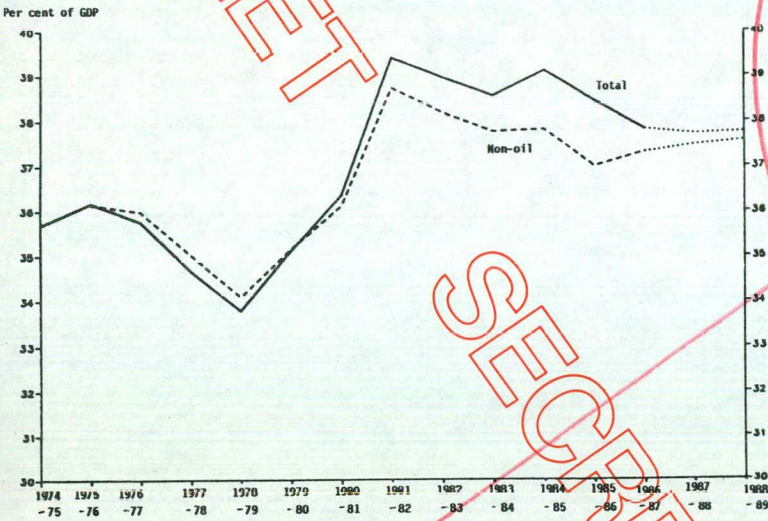
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ALTERNATIVE CHART 6.1

Taxes and national insurance contributions

General government expenditure



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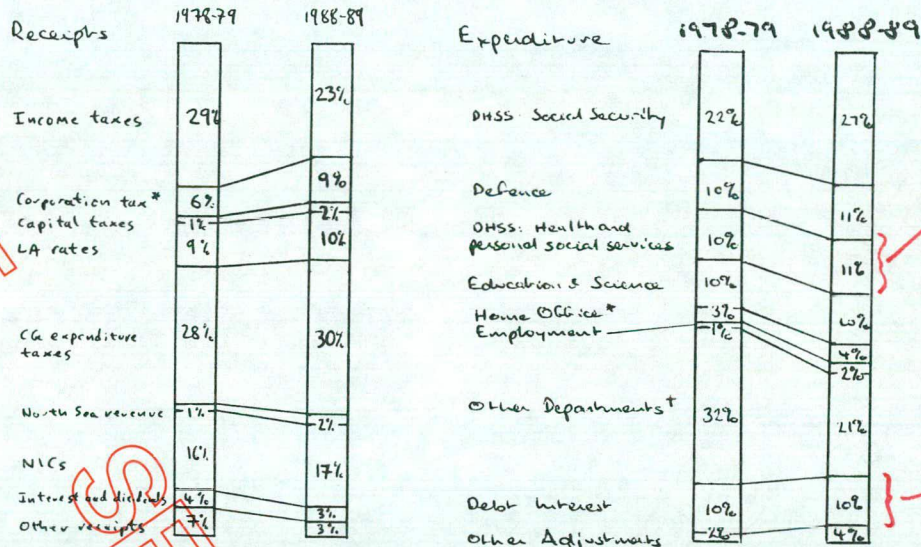
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Chart 6.2 The structure of receipts and expenditure

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Save! We have seen gov't diff figs for them?

Why doesn't that count?

* Excluding North Sea.

* and legal departments

† including Privatisation Proceeds and Reserve

Public sector's finances: analysis by sector

6.18 Table 6.3 shows which authorities or sectors are repaying debt or undertaking ^{net} borrowing in 1987-88 ^{1986-87 and} by central government, local authorities and public corporations.

Table 6.3 Public sector borrowing requirement

	£ billion	
	1986-87 Outturn	1987-88 Latest estimate
1 Central government borrowing on own account	4.5	- 2.8
2 Local authority borrowing from central government		5.2
3 Local authority borrowing from market and overseas	- 5.6	- 4.0
4 Total local authority borrowing	0.2	1.1
5 Public corporations' borrowing from central government		- 0.3
6 Public corporations' borrowing from market and overseas	- 1.5	- 0.9
7 Total public corporations' borrowing	- 1.4	- 1.2
8 Public sector borrowing requirement	3.4	- 2.9
Memorandum item:- Central government borrowing requirement (lines 1+2+5)	10.5	2.1

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6.19 Tables 6.4 to 6.6 show estimated outturns and forecasts of receipts and expenditure in 1987-88 and 1988-89 for each of the three sectors. These tables include some of the analysis by economic category in Table 6.7. Expenditure in 1988-89 does not include an allocation of the Reserve, although the forecast of the PSBR assumes that the Reserve is fully spent.

Central government

6.20 Central government spending includes grants and subsidies to local authorities and public corporations (including nationalised industries), which are included in the receipts of those sectors, shown in Tables 6.5 and 6.6.

Table 6.4 Central government transactions

	£ billion		
	1986-87 Outturn	1987-88 Latest estimate	1988-89 Forecast
<u>Receipts</u>			
Tax and royalties	104.4	115.2	121.7
National insurance and other contributions	26.7	28.8	31.6
Other	10.4	11.2	11.3
Total receipts	141.4	155.2	164.5
<u>Expenditure</u>			
Current expenditure on goods and services	49.4	53.0	55.7
Current grants and subsidies	77.3	80.7	82.8
Interest	16.5	16.9	17.4
Net lending, capital expenditure, and cash expenditure on company securities	2.7	1.8	2.6
Total expenditure	146.0	152.5	158.4**

* Excluding lending to local authorities and public corporations
** Excluding any allocation from the Reserve

Local authorities

6.21 Local authority receipts consist primarily of rate income plus grants from central government. The forecast increase in rate income (net of rate rebates) between 1987-88 and 1988-89

for consistency

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takes account of available information about rate decisions by local authorities, additions to rateable value, and changes to the system of rate rebates introduced by the Social Security Act 1986.

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6.22 The local authority borrowing requirement (LABR) fell sharply in 1986-87 to £¼ billion, from £1¾ billion in 1985-86. The LABR in the first ten months of 1987-88 was higher than in the same period of 1986-87 and it seems likely that borrowing in the year as a whole will be above that in 1986-87, although still well below the levels of ^{earlier} ~~the~~ years immediately prior to that. The estimates of local authority receipts and expenditure do not fully explain the LABR in 1986-87 and 1987-88 (other receipts in table 6.5 and miscellaneous financial transactions in table 6.7 include a balancing item).

Table 6.5 Local authority transactions

	£ billion		
	1986-87 Outturn	1987-88 Latest estimate	1988-89 Forecast
<u>Receipts</u>			
Rates (net of rate rebates) ¹	15.6	17.0	19.2
Rate support grant	11.8	12.6	13.3
Other grants from central government	11.0	12.1	12.2
Other	6.3	5.2	5.6
Total receipts	44.7	46.9	50.4
<u>Expenditure</u>			
Current expenditure on goods and services	31.1	34.1	35.2
Current grants and subsidies	5.4	5.8	6.0
Interest	4.1	4.4	4.5
Net lending and capital expenditure	4.2	3.8	4.4
Total expenditure	44.8	48.1	50.1²
¹ Memo: Rate rebates	1.7	1.8	1.4
² Excluding any allocation from the Reserve			

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Public corporations

6.23 Table 6.6 shows public corporations' transactions. The public corporations' receipts include subsidies and capital grants from central and local government. For the nationalised industries (and the majority of other public corporations) their net external finance, ie. their borrowing plus subsidies and grants, is included in the public expenditure planning total. Public corporations' net external financing requirement, and not their borrowing requirement (PCBR), is the best measure of the public corporations' total contribution to the PSBR, because it ~~also~~ includes, ^{in addition?} as well as borrowing, subsidies and grants provided by the central government which have to be financed from taxation or central government borrowing.

Table 6.6 Public corporations' transactions

	£ billion		
	1986-87 Outturn	1987-88 Latest estimate	1988-89 Forecast
<u>Receipts</u>			
Gross trading surplus (including subsidies)	7.4	7.0	7.4
Other	2.9	2.1	2.2
Total receipts	10.3	9.1	9.6
<u>Expenditure</u>			
Interest, dividends and taxes on income	3.3	3.1	3.8
Net lending and capital expenditure	5.5	4.7	5.7
Total expenditure	8.8	7.9	9.5*
Memo: nationalised industries' external finance	0.4	0.4	0.7
other public corporations' contribution to the planning total	0.8	0.6	0.8

* Excluding any allocation from the Reserve

6.24 Changes in public corporations' income and expenditure from one year to another are affected by privatisations which

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involve re-classifying privatised industries from the public corporations to the private sector in the national accounts. For example, although table 6.6 shows a fall in gross trading surplus in 1987-88, the gross trading surplus of those industries remaining in the public sector rose strongly in 1987-88. The underlying buoyancy of the gross trading surplus is a major reason why the PCBR is estimated to have risen only slightly between 1986-87 and 1987-88, despite the inclusion in the 1986-87 figures of negative net borrowing by corporations now in the private sector.

Public sector's finances: analysis by economic category

6.25 The full analysis of receipts and expenditure by economic category is shown in Table 6.7, with a breakdown between central government, local authorities and public corporations. This analysis, which distinguishes between current and capital transactions (and within the latter between physical and financial investment) shows the derivation of the public sector financial deficit. The financial deficit, unlike the PSBR, is not wholly a measure of cash transactions because certain items above line 24 in Table 6.7, for example some taxes included in lines 1 and 2, are measured on an accruals basis. An accruals adjustment is accordingly made in line 28.

6.26 The unallocated Reserve is assumed to be used up by spending on current items or physical capital formation ie. in transactions that fall above the financial surplus/deficit line. In practice allocations from the Reserve can affect financial transactions (lines 25 to 29).

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Table 6.7 Public sector transactions by sub-sector and economic category

	Line ¹	£ billion				
		1987-88 Latest estimates				
		General government			Public corporations	Public sector
		Central government	Local authorities	Total		
<i>Current and capital receipts</i>						
Taxes on income, and oil royalties	1	59.2	-	59.2	-0.1	59.1
Taxes on expenditure	2	52.4	17.0	69.4	-	69.4
Taxes on capital	3	3.6	-	3.6	-	3.6
National insurance and other contributions	4	28.8	-	28.8	-	28.8
Gross trading surplus	5	-0.6	0.5	-0.1	7.0	6.9
Rent and miscellaneous current transfers	6	0.3	3.0	3.4	0.5	3.9
Interest and dividends from private sector and abroad	7	3.2	0.9	4.1	0.7	4.8
Interest and dividends within public sector	8	5.8	-3.7	2.1	-2.1	-
Imputed charge for non-trading capital consumption	9	1.2	1.6	2.7	-	2.7
Capital transfers from private sector	10	-	-	-	0.1	0.1
Total receipts	11	154.0	19.3	173.2	6.1	179.4
<i>Current and capital expenditure</i>						
Current expenditure on goods and services	12	53.0	34.1	87.1	-	87.1
Subsidies	13	5.2	1.0	6.2	-	6.2
Current grants to personal sector	14	48.2	4.7	53.0	-	53.0
Current grants paid abroad	15	3.6	-	3.6	-	3.6
Current grants within public sector	16	23.7	-23.7	-	-	-
Debt interest	17	16.9	0.6	17.5	0.6	18.1
Gross domestic fixed capital formation	18	3.6	3.8	7.4	4.5	11.9
Increase in stocks	19	-0.1	-	-0.1	0.1	-
Capital grants to private sector	20	1.9	0.6	2.5	0.1	2.6
Capital grants within public sector	21	1.7	-1.0	0.7	-0.7	-
Total expenditure	22	157.7	20.2	177.9	4.6	182.4
Unallocated Reserve	23	-	-	-	-	-
Financial surplus/deficit	24	-3.7	-0.9	-4.6	1.6	-3.0
<i>Financial transactions</i>						
Net lending to private sector and abroad	25	-0.1	0.6	0.5	-0.1	0.4
Cash expenditure on company securities (net) (including privatisation proceeds)	26	5.4	-	5.4	-	5.4
Transactions concerning certain public sector pension schemes	27	0.6	-	0.6	-	0.6
Accruals adjustments	28	0.1	0.1	0.1	-	0.1
Miscellaneous financial transactions	29	0.6	-0.9	-0.3	-0.2	-0.6
Borrowing requirement	30	-2.8	1.1	-1.6	-1.2	-2.9

¹ Relationship between lines: (24) = (11) - (22) + (23)
(30) = -(24 to 29)

no longer show with -ve signs
OK, but some explanation
needed that a financial surplus
is shown as -ve = a financial
surplus + ve (but is
contra-intuitive)

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£ billion ¹						
1988-89 Forecasts						
General government			Public corpora- tions	Public sector		
Line ²	Central govern- ment	Local authori- ties				Total
					<i>Current and capital receipts</i>	
1	62.0	-	62.0	-0.7	61.3	Taxes on income, and oil royalties
2	55.6	19.2	74.8	-	74.8	Taxes on expenditure
3	4.2	-	4.2	-	4.2	Taxes on capital
4	31.6	-	31.6	-	31.6	National insurance and other contributions
5	-0.1	0.5	0.5	7.4	7.9	Gross trading surplus
6	0.4	3.0	3.4	0.6	3.9	Rent and miscellaneous current transfers
7	3.0	0.9	3.8	0.7	4.5	Interest and dividends from private sector and abroad
8	6.1	-4.1	2.0	-2.0	-	Interest and dividends within public sector
9	1.2	1.6	2.8	-	2.8	Imputed charge for non-trading capital consumption
10	-	-	-	0.2	0.2	Capital transfers from private sector
11	163.8	21.1	184.9	6.1	191.0	Total receipts
						<i>Current and capital expenditure</i>
12	55.5	35.2	90.7	-	90.7	Current expenditure on goods and services
13	4.6	0.9	5.6	-	5.6	Subsidies
14	50.5	5.0	55.5	-	55.5	Current grants to personal sector
15	2.9	-	2.9	-	2.9	Current grants paid abroad
16	24.7	-24.7	-	-	-	Current grants within public sector
17	17.4	0.2	17.6	0.9	18.5	Debt interest
18	3.9	4.0	8.0	5.4	13.4	Gross domestic fixed capital formation
19	-	-	-	0.1	0.1	Increase in stocks
20	1.9	0.7	2.6	0.1	2.6	Capital grants to private sector
21	1.5	-0.8	0.7	-0.7	-	Capital grants within public sector
22	163.0	20.6	183.6	5.8	189.4	Total expenditure
23					3.5	Unallocated Reserve
24					-1.9	Financial surplus/deficit
						<i>Financial transactions</i>
25	-0.5	0.3	-0.2	-0.1	-0.3	Net lending to private sector and abroad
26	5.0	-	5.0	-	5.0	Cash expenditure on company securities (net) (including privatisation proceeds)
27	0.6	-	0.6	-	0.6	Transactions concerning certain public sector pension schemes
28	-0.1	-	-0.1	-	-	Accruals adjustments
29	0.3	-0.5	-0.2	-0.2	-0.3	Miscellaneous financial transactions
30					-3.1	Borrowing requirement

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Part A: relationship between tables in Chapter 6, and with Table 1.2; and outturn data

Relationship between
tables

6A.1 Table 6.7 is based on the definitions used to compile the national accounts. In order to show the financial deficit for each sector, lending and other financial transactions are separated from the analysis of receipts and expenditure in lines 1-23 and shown in lines 25-29. These lines show the relationship between the financial deficit (line 24) and the borrowing requirement for each sector (line 30).

6A.2 Tables 6.4-6.6 are summary versions of the sectoral columns of Table 6.7. The information in Table 6.7 is rearranged so that, for example, central government grants to local authorities (which appear as negative expenditure in the local authorities column of Table 6.7, lines 16 and 21) appear as receipts in Table 6.5. Interest paid by local authorities to central government (which appears as negative receipts in the local authorities column of Table 6.7, line 8) appears as expenditure in Table 6.5. Finally, lending and other financial transactions (lines 25-29 of Table 6.7) are included in the receipts and expenditure of Tables 6.4-6.6.

6A.3 Table 1.2 in Chapter 1 uses the same information as Table 6.7, but again rearranges it. To derive general government expenditure, it starts by giving a departmental breakdown of the public expenditure planning total: that includes not only general government expenditure items in the third column of

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Table 6.7 (including the "financial transactions" in lines 25-26), but also borrowing or capital expenditure by public corporations in the fourth column. General government expenditure as shown in Table 1.2 is then obtained by adding general government debt interest from the third column of Table 6.7 and the national accounts adjustments already included in Table 6.7, and deducting public corporations' borrowing from the market and from overseas.

6A.4 Alternatively, general government expenditure in Table 1.2 (and Table 2.4) can be obtained as the sum of lines 22, 23, 25 and 26 (third column) in Table 6.7 and on-lending to public corporations in Table 6.3.

6A.5 To derive general government receipts, Table 1.2 takes the receipts shown in the third column of Table 6.7 (lines 11, 27, 28 and 29) and rearranges them according to the type of activity which gives rise to them. For example, oil revenues comprise North Sea corporation tax and petroleum revenue tax (included in "taxes on income" in Table 6.7) plus oil royalties. The sub total "total taxes and royalties" is the same as the first line of Table 2.5 in Chapter 2.

Outturn data

6A.6 Outturns for the PSBR and the statutory central government accounts (as in Tables 6B.1-4 in Part B of the Annex) are compiled monthly and published by press notice 12 working days after the end of the month and then in more detail in Tables 2.5 and 3.12 to 3.16 of the following issue of Financial Statistics. Details of the PSBR on national accounts definitions, as in Table 6.7, are compiled quarterly and published in sections 2 to 5 of Financial Statistics three months after the end of the quarter.

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6A.7 The first outturn for the PSBR in 1987-88 will accordingly be published on April 20. The first national accounts outturns for 1987-88 will appear in the June issue of Financial Statistics, including supplementary Table 13 which is based on Table 6.7.

Part B: central government transactions

Commentary on the tables

6B.1 The tables in Part B of this Annex are confined to central government transactions, and are based on the statutory funds and accounts. Their relationship to the accounts of central government on a national accounts basis (as in Table 6.4) is described in the Financial Statistics Explanatory Handbook (1987 edition, p38). The receipts and payments in the Part B tables are all shown on a cash basis, not accrued. Table 1.2, however, shows the main categories of taxes on an accrued basis as in the national accounts: for instance the item "income tax" in Table 1.2 differs slightly from "income tax" in Table 6B.3.

Table 6B.1 Summary of central government transactions

	£ billion 1987-88 Latest estimate
<u>Consolidated Fund</u>	
Revenue (Table 6B.3)	123.0
Expenditure (Table 6B.2)	121.2
<u>National Loans Fund (Table 6B.4)</u>	
Receipts	16.7
Payments	21.6
Surplus transferred from Consolidated Fund	1.8
Total net borrowing by the National Loans Fund	3.1
Surplus on other funds and accounts (net)	1.0
Central government borrowing requirement* (Table 6.3)	2.1

* Including borrowing for on-lending to local authorities and public corporations

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Table 6B.2 Consolidated Fund expenditure

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	£ million 1987-88 latest estimate
Supply issues ¹	105,190
Standing services	
Payment to the National Loans Fund in respect of service of the national debt	9,800
Northern Ireland - share of taxes etc	2,220
Payments to the European Communities	3,890
Other services	100
Total standing services	16,010
Total Consolidated Fund expenditure	121,200

¹ Supply Issues are monies paid from the Consolidated Fund to departments' cash accounts with the Paymaster General for spending on Supply. Supply Expenditure (see Table 5.4) equates closely to total Supply Issues in most years, although there may sometimes be slight timing differences between the two.

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Table 6B.3 .4 National Loans Fund receipts and payments

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£ million
1987-88
Latest
estimate

Receipts

Interest on loans, profits of the Issue Department of the Bank of England, etc	6,920
Service of the National Debt - balance met from the Consolidated Fund	9,800
Total receipts	16,720

Payments

Service of the National Debt:	
interest	16,550
management and expenses	170
Total service of the National Debt	16,720

Loans to:

nationalised industries	- 320
other public corporations	- 160
local authorities	5,190
private sector and within central government	180
Total National Loans Fund lending*	4,890

Consolidated Fund surplus	1,840
Total payments	20,610

* On-lending to local authorities and public corporations in Table 6.3 includes, in addition to National Loans Fund lending, net lending from other funds and accounts (mainly Supply Issues in Table 6B.2).

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COPY NO 1 OF 29

From: J ODLING-SMEE

25th February 1988

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir Peter Middleton
Mr Anson
Sir Terence Burns
Mr Scholar
Mr Culpin
Mr Sedgwick
Mr Turnbull
Mrs Butler
Mr S Davies
Mr Mowl
Miss Sinclair
Ms Evans
Mr Hudson
Mr Cropper
Mr Tyrie
Mr Call

Mr Battishill)
Mr Isaac) IR
Mr Painter)

Mr Unwin)
Mr Knox) C&E

FSBR CHAPTER 1

I attach a draft of Chapter 1 of the FSBR.

2. It follows the style of last year's except that we have expanded the description of the measures in the stub of Table 1.1 to make it more informative. You will want to consider whether you like this presentation.

3. The other important decision relates to the order of the measures in Table 1.1 and the degree of aggregation. We have put the excise duties much lower down than usual, and they could be moved up. Otherwise, there are clearly plenty of alternative ways of ordering the other measures, including the various components of

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income tax. On income tax in particular, do you agree that the order of the rates and allowances changes should, as shown, follow the Scorecard order, and if so that items 1-8 of Table 4.1 should be revised to follow the same order? This would mean, among other things, that item 1 (basic rate) in the existing version of Table 4.1 would become item 6.

4. Table 1.1 includes the footnote you requested on student grants and forestry.

5. You will want to indicate which tax measures to mention in paragraph 1.05. You could have a short list and exclude the items in square brackets. Or you could go for a longer selection.

6. All figures are subject to revision. Those in Table 1.1 are consistent with those in the draft of Table 4.1 which you have. Those in Table 1.2 are consistent with those in the drafts of Chapters 5 and 6 you received yesterday (which were not exactly consistent with each other). We shall, of course, ensure that all figures are eventually fully consistent.

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J ODLING-SMEE

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1. THE BUDGET

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1.01 The objective of the Government's economic policy is to defeat inflation and to maintain a ^{vigorous} dynamic and enterprising economy, ~~and hence the conditions for~~ ^{with} sustained growth of output and employment.

1.02 The Financial Statement and Budget Report (FSBR) supplements the Chancellor's Budget Statement. It presents the Medium-Term Financial Strategy (MTFS); describes developments in the economy over the past year; provides forecasts to mid-1989; sets out the tax proposals in the Budget; summarises the Government's spending plans; and ^{gives forecast of} ~~shows the position of~~ the public finances for the year ahead.

The Medium Term Financial Strategy

1.03 Chapter 2 describes the MTFS, which provides the framework for the Government's economic policy. Monetary and fiscal policies are designed to keep the growth of money GDP on a downward trend over the medium term, so bringing down inflation. The MTFS is complemented by ^{supply side} policies, including new measures in the Budget, ~~to~~ ^{designed to} encourage enterprise, efficiency and flexibility and thus the growth of output and employment.

The economy

with the largest fall in unemployment since the War.

1.04 Chapter 3 describes the main developments in the economy in 1987 and the prospect until mid-1989. The economy grew strongly in 1987, ~~and unemployment fell at a post-war record rate.~~ ^{a further} ~~GDP is forecast to grow by 3% in 1988, with business investment growing by 8½%.~~ ^{partially strong growth in} Inflation should remain low and unemployment continue to fall.

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Tax measures

1.05 Chapter 4 sets out the tax proposals in the Budget. They continue the Government's programme of tax reduction and reform. They include the independent taxation of husband and wife, an increase in personal allowances, a reduction of 2p in the basic rate of income tax, the abolition of rates of income tax above 40% [and an increase in the higher rate threshold, the alignment of the rates of capital gains tax with income tax rates, the removal of the tax liability on inflationary capital gains before 1982, and the abolition of some income tax reliefs]. The measures are summarised in Table 1.1.

and the introduction in 1990-91, a

an increase
all the higher

I suggest

Other measures include reforms of capital gains tax, inheritance tax and the tax treatment of maintenance and cohabitation, and

Public expenditure

1.06 Chapter 5 summarises the Government's spending plans. Public expenditure is planned over the medium term to grow less rapidly than the economy as a whole, permitting some further reduction in the burden of taxation.

as set out in the Public Expenditure White Paper. This chapter also provides the latest estimate of the outlook for public expenditure planning total in 1987-88.

Public sector finances

1.07 Chapter 6 presents the complete financial picture for the public sector. The budget is expected to show a surplus of £3 billion in 1987-88, the first surplus since 1969-70. A surplus of £3 billion is also forecast for 1988-89. This takes account of the tax proposals in the Budget which are expected to reduce revenues by £4 billion, over and above the net cost of indexing tax rates and allowances. Table 1.2 shows the main components of general government receipts and expenditures.

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direct → indirect

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Table 1.1 The Budget measures¹

	£ million 1988-89	Changes from a non-indexed base	Changes from an indexed base	yield(+)/cost(-) 1989-90 Changes from an indexed base
Income tax				
personal allowances double indexed	-1395	-685	-940	
basic rate reduced to 25p ²	-2500	-2500	-3100	
basic rate limit increased to £20,000	-300	-220	-420	
higher rates above 40p abolished	-835	-780	-1670	
life assurance premium relief reduced	-	-	+70	
company cars valuation for tax purposes doubled	+230	+230	+330	
income threshold for fringe benefits increased to £10,000	-50	-50	-50	
£30,000 mortgage interest relief ceiling applied to residence	+5	+5	+20	
relief on new home improvement loans abolished	+80	+80	+200	
relief on new non-charitable covenants abolished ³	+20	+20	+45	
changes in rules for maintenance payments	-20	-20	-20	
Capital gains tax				
annual exemption frozen at £6,600	-	-	+10	
gains charged at income tax rates	+70	+70	+40	
capital gains rebased to 1982	-	-	-75	
Independent taxation of husband and wife ⁴	*	*	-30	
Inheritance tax				
single rate of 40% above threshold of £110,000	-110	-90	-180	
Corporation tax				
capital gains rebased to 1982	-25	-25	-265	
small companies' rate reduced to 25p	*	*	-50	
Business expansion scheme				
investment ceiling of £½ million per company	*	*	+25	
extension to private rented housing	*	*	-40	
Forestry removed from income/corporation tax ³	*	*	-5	
Excise duties increased overall broadly in line with inflation. Changes imply the following price increases:	+550	+10	-20	
VED and unleaded petrol unchanged; leaded petrol up 5½p a gallon				
cigarettes up 3½p for twenty, pipe tobacco unchanged				
table wine up 4p a bottle; beer and cider up 1p a pint; spirits and fortified wines unchanged				
Other tax changes	+70	+60	+40	
Total	-4210	-3895	-6085	

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- 1 These measures and the basis of the costings shown are described in detail in Chapter 4.
- 2 Figures include the effect of the consequential change in the rate of advance corporation tax.
- 3 Figures are net of the cost of consequential public expenditure measures, shown in Chapter 5. Gross revenue effects are shown in Table 4.1.
- 4 The cost of independent taxation, which is introduced in 1990-91, is shown in the Annex to Chapter 4.

- = nil. * - negligible.

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Table 1.2 The finances of the public sector¹

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	£ billion			£ billion		
	1987-88		1988-89	1987-88		1988-89
	1987 Budget ²	Latest Estimate	Forecasts	1987 Budget ²	Latest Estimate	Forecasts
RECEIPTS						
Income tax	40.0	41.0	41.8			
Corporation ³ tax excluding North Sea ⁴	13.5	14.0	17.3			
Capital taxes	3.3	3.6	4.2			
Expenditure taxes:						
VAT	23.3	24.3	26.2			
local authority rates	16.9	17.0	19.2			
petrol, derv, etc	7.8	7.7	8.4			
spirits, beer, wine, etc	4.3	4.3	4.4			
cigarettes and other tobacco	4.9	4.8	4.9			
stamp duties	2.1	2.5	2.2			
other	8.5	8.8	9.5			
Total expenditure taxes	67.8	69.4	74.8			
North Sea revenues:						
North Sea corporation tax ⁴	1.4	1.4	1.5			
petroleum revenue tax	1.7	2.2	1.3			
oil royalties	0.8	1.0	0.7			
Total North Sea	3.9	4.6	3.5			
Other ⁵	-0.8	-0.6	-0.7			
Total taxes and royalties	127.8	131.9	140.9			
National insurance and other contributions	28.5	28.8	31.6			
Interest and dividend receipts	5.7	6.2	5.8			
Gross trading surpluses and rent	3.3	3.0	3.6			
Other	3.5	3.7	2.8			
General government receipts	168.8	173.6	184.7			
EXPENDITURE						
DHSS - social security	46.0	[46.3]	48.5			
DHSS - health and personal social services	19.1	[19.7]	20.7			
Defence	18.8	[18.7]	19.2			
Education and science	16.6	[17.1]	18.0			
Scotland, Wales and Northern Ireland	16.0	[16.4]	17.1			
Other departments	33.6	[33.2]	34.9			
Privatisation proceeds	-5.0	[-5.0]	-5.0			
Reserve	3.5		3.5			
Public expenditure planning total	148.6	[146.4]	156.8			
General government gross debt interest	17.9	[17.5]	[17.5]			
Other adjustments	7.0	[8.1]	[8.5]			
General government expenditure	173.5	[171.6]	[182.8]			

Expenditure, receipts and borrowing

	£ billion		
	1987-88		1988-89
	1987 Budget ²	Latest Estimate	Forecasts
General government expenditure	173.5	171.6	182.8
General government receipts	168.8	173.6	184.7
General government borrowing requirement	4.7	-2.0	-1.9
Public corporations' market and overseas borrowing	-0.8	-0.9	-1.2
Public sector borrowing requirement	3.9	-2.9	-3.1

¹ In these and other tables, constituent items may not add up to totals because of rounding

² On current definitions

³ Including advance corporation tax but excluding corporation tax on capital gains

⁴ Before advance corporation tax set off. See footnote³ to Table 6B.3

⁵ Adjustments for advance corporation tax set off against North Sea corporation tax plus accruals adjustment.

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Income tax

So do with the changes

personal allowances	-1395
basic rate	-2800
higher rate thresholds	-300
higher rates	-835
car scales	+230
PIA limit	-50
home improvement loans	+80
covenants and maintenance	-
> LAPR	-
Independent taxation	*
Capital gains tax	-
relating	-
rates	+70
Inheritance tax	-110
Corporation tax	0
capital gains	-25
small companies rate	*
Excise duties	
oils	-
VED	7550
tobacco	-
alcohol	-
Other tax changes	0
TOTAL	-4210

do not make group separately

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Mr Cropper
Mr Call

CHANCELLOR

BUDGET SPEECH

I have now had a chance to read through Andrew Hudson's draft of 19 February carefully. I think it is excellent. We are nearly there already! The attached Annex gives some detailed drafting points which you can probably leave Andrew to handle and many of which I think he's spotted.

I have one general point about the conclusion. As I have mentioned before, the speech is in danger of having a little too much finality about it. The rates, everything at 25% or 40%, give that impression, even though this is diluted a little by your commitment to 20 pence.

Might it be worth having a paragraph or two in the peroration which make three related points:

- i. The task of tax reform and simplification is by no means complete. The objectives of further simplicity, further reductions in taxation when they are prudent, and the further removal of distortions to economic activity will guide us in our third term and beyond.

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ii. It is increasingly accepted that these principles accord with the wishes of people and the needs of the economy.

They are in stark contrast to the principles which lay behind the tax system we inherited, driven by misplaced notions of social engineering, and a misunderstanding about the relationship between the tax system and productiveness of the economy. Those principles led to the hopeless complexity, the absurdly high rates, the distortions and the injustices of the tax system of a decade ago.

iii. The budget announces both tax reductions and tax reform. But these measures, important though they are, do not stand alone. They form part of and complement the further set of supply side measures set out in our Manifesto. Taken together these measures offer the best prospect of sustaining the virtuous circle in our third term and beyond: of reducing taxes while maintaining yield, and of reducing the burden on individuals and businesses which spur further investment and growth.

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~~BUDGET SECRET: BUDGET LIST ONLY~~**BUDGET SECRET
BUDGET LIST ONLY****NOT TO BE COPIED****ANNEX: SOME DETAILED SUGGESTIONS ON 19 FEBRUARY DRAFT**

(Underlinings are drafting suggestions)

B6. Third sentence 'and our supply side policies have reduced the burdens which held British industry and individual enterprise in check for far too long'.

B7. I would itemise the number of years over which new jobs have been created. I think it is five.

B11. Last sentence. I would either remove 'balanced growth is set to continue', or explain what is meant. At present it reads as if, despite a shift in the balance between consumption and investment, somehow, that same balanced growth is set to continue!

B13. Line 4. Rather than 'inflation ... crept up to just under 4.5%', I would say simply 'inflation ... rose to just under 4.5%'.

0v7
B16. Penultimate line. Rather than 'as British firms start to repeat their success as exporters' I would say 'as British firms build on their success as exporters ...'.

D3. Line 5. Instead of saying that the borrowing requirement has vanished I would point out that it has been replaced by the 'public sector debt repayment'.

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F7. Rather than say that we're abolishing the married man's allowance, I think it might be better to say that we are replacing it. During the election we made much of Labour's commitment to abolish the married man's allowance. I would have thought it better not to give them even a chink of light.

G15. On Section 482 the main bull point to get across is that we are removing the criminal penalty.

H2. At present the text reads 'I have argued that CGT should apply only to real gains, and not paper gains'. I think paper gains means accruals. I would replace the word paper with inflationary.

K13. I would itemise the yield individually for maintenance payments and covenants. It is important to stress that we're not getting or losing much from the maintenance reform.

M24. I would shorten this considerably. I don't think we can justify the removal of MIR for home improvement loans on the grounds that it is a kick in the teeth for double-glazers.

M38. If we raise the basic rate threshold by 10% we slip the higher rate move to £20,000 (also 10%) through on the rails, and make it a little less a sore thumb.

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Thanks. I will look at that with AA: I will look at that with

ASAP on HON. Mr. FROM: A BOTTRILL

DATE: 26 February 1988

- 1. MR SEDGWICK
- 2. CHANCELLOR

with the visible trade figures having

been poor in recent

months there is a cash led

standing of the AS forecast for the current

account in 1988, i.e. a deficit of £3½%,

notwithstanding the much better recorded

outcome on invisibles.

- cc Sir P Middleton
- Sir T Burns
- Mr Odling-Smee
- Mr Sedgwick
- Mr Owen
- Mr Young

Circulation Monday 11.30 am

- Mr Hudson
- Miss C Evans

P.N.J. 26.11

FSBR: CURRENT BALANCE OF PAYMENTS FORECAST

We are re-examining the forecast for the current balance of payments in the light of the January trade figures and the substantial revisions to the invisibles data for the past. This process is not complete since we do not have the final detail of either set of figures but you may wish to be aware of our preliminary assessment of the consequences for the forecasts to be published in the FSBR.

Visible trade

2. The visible trade deficit for 1987 has been revised down by £0.2 billion, but the January figures are worse than expected. We are inclined to discount heavily the January trade figures, particularly for exports. The figures, however, do suggest that export prices may have been rather higher than we had expected, and we have made some minor adjustments to both prices and volumes. The forecasts for the total value of non-oil exports is slightly higher but the increase in non-oil export volumes in 1988 is now 5 per cent instead of 5½ per cent with prices increasing a little faster and the terms of trade better. Table 1 compares the new figures with those contained in Table 3.3 of the draft FSBR circulated by Mr Sedgwick on 18 February.

P.S. It is esp. taking new estimates for 1987 is necessary. What is forecast for 1987? In last current FSBR -1 (of our forecast -2.2) Improving visible trade, exports in part 2. Mr.

See also table on next page Mr.

Table 1: Visible trade

(per cent changes on previous year)

Previous FSBR draft in brackets

	Total goods			Non-oil goods		
	Export volume	Import volume	Terms of trade	Export volume	Import volume	Terms of trade
1987	5½ (5½)	7½ (7½)	1 (1)	7 (7)	8½ (8½)	1 (1)
1988	3½ (3½)	7 (7)	1 (1)	5 (5½)	6½ (6½)	1½ (1)

3. The implications of the January trade figures for imports are worth taking more seriously. The rise in non-oil import volumes contrasts with the falls between December and January observed in six out of the previous seven years. It gives us less confidence that the level of imports in the first quarter as a whole will be as low as previously forecast and we have adjusted the forecast accordingly. We have retained broadly the same forecast growth for non-oil import volumes in 1988 as a whole but the high starting point now implies very little growth through the year. Outside commentators may remark on this.

Invisibles

4. The revisions to invisibles are still preliminary since the CSO and its contributors are still checking the information on 1987Q4 and previous periods. We know, too, that Shell's results for the final quarter of 1987 will not be published until 3 March. Nevertheless, on the information so far to hand the invisibles out-turn for both 1987 and previous years is likely to be substantially better than expected.

Table 2: Invisibles balances

(£ billion)

Previous FSBR draft in brackets

	Services	IPD	Transfers	Total
1986	6 (5)	5 (4½)	-2 (-2)	8½ (7½)
1987	6 (5½)	6 (5)	-3½ (-3½)	8½ (7)
1988	6 (5½)	6 (5)	-3½ (-3½)	9½ (7½)

The 1988 figs don't add up:
 present figs $6 + 6 - 3\frac{1}{2} = 9\frac{1}{2}$
 previous draft $5\frac{1}{2} + 5 - 3\frac{1}{2} = 7\frac{1}{2}$
 PSE explain

after seasonal adjustment!

RE
 11/10
 11/10
 11/10
 11/10

5. The reasons for the changes include an upward revision to insurance companies' net underwriting earnings for the past as a result of discovery of a reporting error by a major company. This has contributed to an improvement in the services surplus for 1986 and 1987 of rather more than £½ billion a year. The surplus on interest, profits and dividends has also been revised up by £½ billion for 1988 and almost £1 billion for 1987. The revisions include higher direct investment earnings abroad by UK companies and lower payments abroad by UK subsidiaries of foreign companies and banks. In addition, UK residents' earnings from bank deposits abroad are now estimated to be higher partly as a result of inclusion of Swiss trustee accounts which were previously not captured.

6. The net effect of these changes is to increase the invisibles surplus by about £1½ billion in 1987 and reduce the estimated current deficit for that year to slightly less than £1 billion compared to the £2½ billion deficit contained in the latest trade figures press notice.

Table 3: Current balance of payments

	(£ billion)				Current balance
	Manufactures	Oil	Other goods	Invisibles	
1986	-5½ (-5½)	4 (4)	-7 (-7)	8½ (7½)	½ (-1)
1987	-6½ (-6½)	4 (4)	-7½ (-7)	8½ (7)	-1 (-2½)
1988	-8½ (-8½)	2½ (3)	-6½ (-6½)	9½ (7½)	-3 (-4½)

7. The impact of these changes on the forecast for the current balance for 1988 are shown in table 3. The trade balances on manufactures and non-manufactures would show no change from our previous views. The oil surplus, however, seems likely to be a little lower as a result of our move to a \$15 a barrel assumption. This slightly worse out-turn for the oil surplus would tend to offset part of the improvement in invisibles.

8. We think that in the light of the very recent figures for imports in particular and notwithstanding the better out-turn for invisibles it would be prudent in public presentation to show a change in the current deficit between 1987 and 1988 no smaller than the £2 billion we proposed originally. An alternative that takes prudence a bit further would be to stick to the Autumn Statement forecast of a current deficit of £3½ billion in 1988. The same figure could be used for 1989 H1 at an annual rate in Table 3.12 of Chapter 3 of the FSBR.

ABottrill

A BOTTRILL

COPY NO: 11

OF: 12

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REF NO: ACSA/17

FROM: A C S ALLAN

DATE: 26 February 1988

MISS SINCLAIR

cc PS/Financial Secretary
 Sir P Middleton
 Mr Scholar
 Mr Culpin
 Mr Odling-Smee
 Miss C Evans
 PS/IR
 Mr P R H Allen - C&E

FSBR CHAPTER 4

The Chancellor was most grateful for your minute of 22 February and the draft of Chapter 4.

I attach a marked-up copy of the pages on which the Chancellor had comments.

There are one or two other points:

- i. The Chancellor was content with the section on independent taxation. He would prefer it to be boxed and kept on one page.
- ii. He would prefer to use the same wording as last year in the first part of the introduction to the Annex to table 4.1 (discussed in your new paragraph 4).
- iii. Is it necessary to include the paragraph about measures announced and implemented before Budget day (entertainments and gifts etc) in the introduction to the Annex?
- iv. The Chancellor noted that the ordering of the items produced a large gap between CGT re-basing and CGT rates, both in the Table and in the Annex. He would prefer them next to each other, or at least much closer together.

ACSA
 A C S ALLAN

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4 The Budget tax proposals

4.01 The main tax changes proposed in the Budget are summarised below. A full list of changes is given in Table 4.1

Income tax

4.02 The basic rate of income tax will be reduced to 25 per cent. ^{P4.02A} There will be a single higher rate of income tax of 40 per cent, ~~The scale of charge will be:~~

Rate of tax per cent	Taxable income £
25	1-20,000
40	above 20,000

*which will apply
to taxable income
over £20,000.*

4.03 The main income tax personal allowances will be increased by twice the amounts due under the statutory indexation provisions (based on the increase of 3.7 per cent in the RPI in the year to December 1987). This will mean that:

the single person's and wife's earned income allowances will rise from £2,425 to £2,605;

the married allowance will rise from £3,795 to £4,095;

the age allowance for those aged 65 to 79 will rise from £2,960 to £3,180 (single) and from £4,675 to £5,035 (married);

the age allowance for those aged 80 or over will rise from £3,070 to £3,310 (single) and from £4,845 to £5,205 (married);

the income limit for age allowance will rise from £9,800 to £10,600;

the additional personal allowance and widow's bereavement allowance will rise from £1,370 to £1,490.

4.04 The housekeeper allowance, dependent relative allowance and the allowance for the services of a son or daughter will be abolished.

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4.05 From [6 April 1989] onwards a couple will not be entitled to more than one additional personal allowance.

Life assurance premium relief

4.06 The rate of premium relief for life assurance policies taken out before 14 March 1984 will be reduced to [12½ per cent] from 6 April 1989.

Benefits in kind

4.07 Car benefit scale charges for 1988-89 will be set at twice their 1987-88 levels [and for 1989-90 they will be increased by ^{at least} 10 per cent above the 1988-89 levels]

(the "PIID" limit)

4.08 The gross income threshold above which employees are liable to tax on certain benefits will be raised from £8,500 to £10,000.

? A car parking

4.09 The exemptions from tax for luncheon vouchers up to the value of 15p per day, and for the benefit of meals provided at less than cost by an employer in a canteen or dining room not available to staff generally will be withdrawn from 6 April 1989.

Mortgage interest relief
Very convoluted - needs simplifying

4.10 For loans taken out from 1 August 1988, tax relief for two or more people borrowing to buy the same property as their only or main residence will be limited to the interest on £30,000 in total for the residence. Relief on new loans for home improvements and new loans for the purchase of residences for dependent relatives and divorced or separated spouses will be abolished from 6 April 1988.

The tax treatment of covenants will be reformed and simplified.

Covenants

and income from such covenants made after Budget day will not be taxable in the hands of the recipient.

4.11 Non-charitable covenants made by individuals on or after Budget day will no longer attract tax relief. ~~Relief for covenants made before Budget Day will continue.~~ There will be parallel changes in the student grant system (see paragraph 5[]). Covenants to charities will not be affected, nor will non-charitable covenants made before Budget day.

Charitable giving

4.12 The limit on charitable donations qualifying for tax relief under the payroll giving scheme will be increased to £240 a year from 1988-89.

doubled from £120

Maintenance payments

4.13 The tax treatment of maintenance payments will be reformed. Under new maintenance arrangements recipients will not be liable to tax on the payments; relief for those making payments will be restricted to payments to a divorced or separated spouse, up to a limit of

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Employee share schemes

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[£2,005]. Transitional provisions will be introduced to protect existing maintenance arrangements.

Needs better explanation

Trusts

Capital gains

4.14 [From 6 April 1989, options granted under an approved discretionary share option scheme will only qualify for tax relief if the company also operates an approved all-employee share or share option schemes.]

4.15 Following consultation last year, the scope of the income tax charge on unapproved employee share schemes under Section 79 of the 1972 Finance Act will be reduced.

4.16 The additional rate of income tax on discretionary trusts will be [abolished from 1988-89/ reduced to ¹⁰ per cent for 1988-89.]

4.17 The capital gains tax annual exempt amount will remain at £6,600 in the case of individuals and £3,300 in the case of most trusts.

4.18 The base date for capital gains will be brought forward from 6 April 1965 to 31 March 1982. The present indexation provisions will continue to apply to gains accruing from 31 March 1982. The proposal will also apply to companies' gains.

4.19 Gains, after deduction of the exempt amount and allowing for rebasing to 1982 and indexation, will be added to income and taxed at income tax rates (as if they were the marginal slice of income).

4.20 From 6 April, 50 per cent of any gains between £125,000 and £500,000 will qualify for retirement relief, subject to the general conditions for the relief.

Inheritance tax

4.21 From Budget Day the threshold will be increased from £90,000 to ^{£110,000} ~~£107,000~~. Chargeable transfers above this amount will be taxed at a single rate of 40 per cent. *The £100,000 limit on the amount that can be given to a political party without incurring inheritance tax will be abolished.*

for inheritance tax
~~4.22 The limit on the amount which can be given to a political party without incurring IHT will be removed.~~

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Business tax

4.23 The ~~small companies~~ rate of corporation tax will be reduced to 25 per cent. The rate of advance corporation tax (ACT) will go down automatically to 1/3 as a consequence of the reduction in the basic rate of income tax.

4.24 The main rate of corporation tax for the financial year 1988 will be 35 per cent.

4.25 ~~The ceiling above which capital allowances on cars are restricted will be increased from £8,800 to [£10,000] for expenditure after 15 March 1988.]~~

In common with other business entertainment,

4.26 ~~The~~ cost of entertaining overseas ^{businessmen} ~~customers~~ will no longer be an allowable business expense for tax purposes. This change will take effect from Budget Day, except for commitments entered into before that date. From 1 August 1988 the VAT paid by businesses on this entertainment will no longer be deductible.

Too flat: needs expanding

4.27 A number of changes will be made to prevent tax charges arising on the conversion of building societies into public limited companies.

Business Expansion Scheme

4.28 The Business Expansion Scheme will be changed to permit relief on investment in companies providing private rented housing.

4.29 A general limit of [] will be set on relief under the Business Expansion Scheme for investment in any one company in any period of twelve months, with a higher limit of [] for investment in companies providing private rented housing *or shipping*

^

Lloyd's

4.30 Changes will be made to the present administrative arrangements for taxing members of Lloyd's.

4.31 The legislation on Lloyd's reinsurance to close will be modified to give relief to Lloyd's members who leave syndicates at the end of the underwriting year.

Forestry

4.32 Income from the occupation of commercial woodlands will be removed from the scope of Income Tax and Corporation Tax. [See paragraph [5.] for details of the proposed increase in grants for forestry.]

Is this essential here?

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Oil taxation

4.33 Oil allowances for Petroleum Revenue Tax (PRT) will be reduced to 100,000 tonnes per chargeable period for all Southern Basin and onshore fields given development consent on or after 1 April 1982. (At the same time the Secretary of State for Energy proposes to abolish royalty payments for these fields.)

4.34 A new capital gains relief will be provided for disposals of oil licence interests in undeveloped areas wherever the consideration includes a work programme or another licence interest.

Company residence and migration

Shorten considerably

4.35 Section 482(1) (a) and (b) of the Taxes Act will be repealed with effect from Budget Day. In future companies will not need to apply to the Treasury for consent to move their residence abroad for tax purposes. The proposed new arrangements will:

extend the definition of UK company residence, so that companies either incorporated in the UK, or centrally managed and controlled here, will be deemed to be resident here for tax purposes;

require UK incorporated companies wishing to change their residence to change the country of their incorporation and to pay any tax arising on doing so; and

require UK resident companies not incorporated here wishing to change their residence to provide for the payment of their tax (including tax on accrued gains) before they do so.

Keith Report

4.36 Following recommendations of the Keith Committee, a number of changes will be made to encourage people to notify the Inland Revenue if they are liable to tax. These include the introduction of a tax-g geared penalty for failing to notify liability. There will be changes to the information powers of the Inland Revenue to help identify those who fail to notify liability to tax.

4.37 Legislation will be introduced to charge interest where payment to the Inland Revenue of income tax deducted by employers is delayed beyond the end of the tax year. The interest charge will be implemented when the necessary Inland Revenue computer systems

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are in place. There will be parallel social security legislation to extend the interest charge to late payment of Class I or Class IV National Insurance contributions.]

VAT

4.38 From 16 March 1988 the registration limits will become £22,100 per annum and £7,500 per quarter.

4.39 The VAT civil penalty system, introduced in 1985, has been reviewed and various amendments are proposed. These include the introduction of a time-related penalty for late registration; the halving of daily penalties; changes to the rules about eligibility to repayment supplement; and changes to the rules for persons who persistently misdeclare their liability.

4.40 The provision for applying VAT to confectionery will be ~~brought up to date~~ ^{amended} with the main effect of taxing all cereal bars at the standard rate.

Excise duties

4.41 The duty on beer, light wine and sparkling wine will rise by the equivalent of [1p] on a typical pint of beer, [4p] on a bottle of table wine and a little over [6p] on a bottle of sparkling wine (all inclusive of ~~consequential~~ VAT). The duties on spirits and fortified wines will remain unchanged. The minimum duty charge for beer will be abolished and provision will be made for restructuring the duties on low strength mixed drinks.

4.42 The duty on leaded petrol will be increased by the equivalent of [just over 5½p] a gallon (inclusive of ~~consequential~~ VAT). The duty on unleaded petrol will remain unchanged. The duty on derv will rise by the equivalent of [just under 5p] a gallon.

4.43 The specific duties on cigarettes, hand-rolling tobacco and cigars will rise by the equivalent of [over 3p] on a packet of 20 cigarettes and [nearly 2p] on a packet on 5 small cigars. The duty on pipe tobacco will remain unchanged.

Could this be omitted?

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Table 4.1 Direct effects of changes in taxation

£ million

Estimated effect on receipts in:
1988-89

1989-90

Changes from a non-indexed base Changes from an indexed base Changes from an indexed base

See Annex 4
Paragraph numbers

INLAND REVENUE

Income tax

1	Reduction of 2p in basic rate	-2120	-2120	-2900
2	Abolition of higher rates of income tax above 40p	-835	-780	-1670
3	Increase in single allowance of £100 and married allowance of £300	-1235	-610	-835
4	Increase in additional personal allowance and widow's bereavement allowance of £120	-15	-5	-10
5	Increase in age allowance of £220 (single) and £240 (married) for those aged 65 to 79	-110	-55	-70
6	Increase in age allowance of £240 (single) and £260 (married) for those aged 80 and over	-20	-10	-10
7	Increase in income limit for age allowance of £500	-15	-5	-15
8	Increase in basic rate limit of £2,100 to £2,000	-300	-220	-420
9	Abolition of minor personal allowances	+10	+10	+10
10	Restriction on additional personal allowance for unmarried couples	-	-	+5
11	Reduction in relief on life assurance premiums	-	-	+70
12	Fringe benefits - car scale	+250	+250	+250
13	Fringe benefits - income threshold	-50	-50	-50
14	Fringe benefits - car parking space	+	+	+
15	Fringe benefits - luncheon vouchers and employer subsidised meals	-	-	-
16	Fringe benefits - sports facilities	-	-	-
17	Mortgage interest relief ceiling applied to residents	+5	+5	+20
18	Abolition of tax relief on new home purchase mortgages	+50	+50	+200
19	Abolition of tax relief on new loans for wives for dependent relatives, divorced and separated spouses	+	+	+
20	Abolition of tax relief on new coverment	+45	+45	+100
21	Payroll giving to charities - increase in relief limit to £100 a year	+	+	+
22	Change in rules for maintenance payments	-20	-20	-20
23	Change in additional rate on discretionary allowances	-	-	-
24	Lloyd's reinsurance to close - relief on premiums	+	+	+
25	Lloyd's: reform of administrative expenses	-	-	+
26	Link between approved discretionary employee share schemes and approved employee share schemes	-	-	-
27	Unapproved employee share schemes	+	+	+
28	Employee priority in public offer of shares	+	+	+
29	Approved 1984 employee share schemes	+	+	+
30	Redundancy payments: top-slicing	+	+	+
31	Assessing procedure for Schedule D	+	+	+
32	Withdrawal of "top-slicing" relief for interest on bank and building society loans, etc.	+	+	+

Income tax and capital gains tax

33	Independent taxation of income and chargeable assets, gains of husband and wife	+	+	-
34	Business Expansion Scheme - limit on relief	+	+	+
35	Business Expansion Scheme - private company shares	+	+	-

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Looks v odd, requires footnote to tax table

← must say a bit more

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Table 4.1 Direct effects of changes in taxation

£ million

Estimated effect on receipts in:
1988-89

1989-90

Changes from a non-indexed base	Changes from an indexed base	Changes from an indexed base
---------------------------------	------------------------------	------------------------------

See Annex A Paragraph numbers

Income tax and corporation tax

? should be +10

36 Forestry - removal of commercial woodlands from scope of tax	-	-	+
37 (Personal pensions - minor changes)	-10	-10	-5
38 Refunds of employee pension contributions	+15	+15	+15
39 Occupational pensions - minor amendments	-	-	-
40 End of year interest on PAYE and subcontractors' deductions	-	-	-
41 Capital allowances - motor cars	*	*	30
42 Capital allowances - exempt persons	-	-	-
43 Capital allowances - safety at sports grounds	*	*	*
44 Capital allowances - abolition of quarantine business relief	*	*	*
45 Withdrawal of relief for entertaining expenses business businessmen	*	*	+5

Income tax, corporation tax and capital gains tax

46 Rebasing capital gains to March 1982	-25	-25	-140
47 Keith Committee administrative changes	+10	+10	+20

split into 2, one for CT and one for CGT, each in appropriate section

Income tax, corporation tax, capital gains tax and stamp duties

48 Conversion of building societies into public limited companies - changes in tax rules	-	-	-
--	---	---	---

Corporation tax

49 Reduction in rate of ACT to 1/3 rd of the amount of the distribution	-180	-180	-
50 Reduction in small companies' rate to 21 per cent	*	*	-5
51 Company residence and migration - new rules	-	-	-
52 Definition of an investment trust	-	-	-
53 Indexation allowance - intra-group transfers	-	-	-
54 Intra-group share exchanges	-	-	-
55 Capital allowances - assured tenancies	-	-	-

Corporation tax and capital gains tax

56 Rollover relief ^{for} satellites, space or projects	*	*	-
--	---	---	---

these are very far apart: more natural to have them closer / next to each other

Capital gains tax

57 Charging gains of individuals and trusts	-	-	-
58 Annual exempt amount	-	-	-
59 Retirement relief	-	-	-
60 Building and Co-operative society shares	*	*	-
61 Homes provided for dependent relatives	-	-	-

* = Negligible - = Nil

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Table 4.1 Direct effects of changes in taxation

£ million

Estimated effect on receipts in:
1988-89

1989-90

See Annex 4
Paragraph numbers

Changes from a non-indexed base Changes from an indexed base Changes from an indexed base

Oil taxation

62	Reduction in PRT oil allowances for certain fields	+30	+30	+30
63	New capital gains relief for certain oil licence disposals	-5	-5	-5
64	Petroleum revenue tax relief for certain tariff related costs	-	-	-

Inheritance tax

65	Changes to rates and bands <i>Increase in threshold and change to flat rate</i>	-110	-90	-130
66	Abolition of limit on gifts to political parties	*	*	*

Stamp duties

67	Stamp duty and reserve tax on paired shares	-	-	-
----	---	---	---	---

TOTAL INLAND REVENUE -4760 -3895 -5127

CUSTOMS AND EXCISE

Value added tax

68	Keith Committee - review of civil penalties	*	*	*
69	Increase in registration limits	*	*	*
70	Revised registration requirements	*	*	*
71	<u>Change in liability of certain confectioners</u>	+5	+5	+5
72	Revision of approved self-billing arrangements	+5	+5	+5
73	Revised treatment of business entertainment for overseas customers	*	*	*

Excise duties

74	No change in rate of spirits duty	-	+20	+20
75	Increase in rate of beer duty	+50	+50	+50
76	Abolition of minimum duty charge for beer	*	*	*
77	Increase in rate of duty on cider and perry	+5	+5	+5
78	Increase in rate of duty on light wine and made-wine duties	+20	+20	+20
79	No change in rates of duty on fortified wines	-	-	-
80	Revised duty regime for low strength alcohol drinks	*	*	*
81	Increase in rate of duty on leaded petrol etc	-275	-275	-275
82	Increase in rate of duty on perry	-75	-75	-75
83	No change in rates of minor oil duties	-	-	-
84	Increase in rates of duties on cigarettes, hand-rolling tobacco and cigars	-100	-100	-100
85	No change in rate of duty on pipe tobacco	-	*	*

separate line for 'no change' in duty on unleaded petrol

TOTAL CUSTOMS AND EXCISE +565 +110 +675

* = Negligible - = nil

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8. The basic rate limit will rise from £17,900 to £20,000. The increase is ~~£1,400 more than~~ the amount due under statutory indexation.

three times

9. The housekeeper allowance, dependent relative allowance and the allowance for the services of a son or daughter will be abolished.

10. From [6 April 1989] an unmarried couple will not be entitled to more than one additional personal allowance.

11. Following the reductions in the basic rate of income tax in successive Budgets, the rate of relief for life assurance premiums on policies taken out before 14 March 1984 will be reduced to [12.5] per cent from 6 April 1989. The starting date is to allow life offices time to make the necessary preparations.

from 15 per cent to

12. For 1988-89 the scale for taxing car benefits in respect of company cars provided for directors and for higher paid employees will be double the 1987-88 levels. The previously announced scales for 1988-89 will not apply. Costs are measured from these previously announced scales. [A further increase of 10 per cent will be made for 1989-90.] [No change is proposed for 1988-89 and 1989-90 to the scale charges for car fuel benefit also used for VAT purposes.]

not less than

13. For 1988-89 the rate of remuneration at which an employee is regarded as higher-paid and liable to tax in respect of certain benefits received by reason of his employment is to be increased from £8,500 to £10,000.

(the 'PIID limit')

14. [The provision of a car parking space for the use of directors or higher-paid employees ~~on premises occupied by the employer~~] will be exempt from tax from 6 April 1988.]

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15. [The extra-statutory concession exempting from tax luncheon vouchers up to the value of 15p a day will be withdrawn with effect from 6 April 1989. The exemption from tax of the benefit of subsidised meals provided by an employer for directors and higher-paid employees in a canteen or dining room which is not open to the staff generally will also be withdrawn from the same date.]

16. [The benefit to employees of sports facilities provided on premises occupied by the employer and available to the staff generally will be exempt from tax from 6 April 1988.]

17. For loans taken out from 1 August 1988, tax relief for two or more people borrowing to buy the same property as their only or main residence will be limited to the interest on £30,000 in total for the residence.

18. Relief on new loans for home improvement will be abolished from 6 April 1988. Relief for existing loans [and for loans for the purchase or improvement of let property] is not affected.

19. Relief on new loans for the purchase of residences for dependent relatives and divorced or separated spouses will be abolished from 6 April 1988. Relief for existing loans is not affected.

20. Non-charitable covenants made on or after Budget day by individuals will no longer be effective for tax purposes. The change is estimated to yield £160 million in 1990-91, £175 million in 1991-92, and £210 million eventually.

21. The limit on charitable donations qualifying for tax relief under payroll giving schemes will be increased to £240 a year from 6 April 1988.

Should there be a note somewhere saying the MIR limit will be set at £30,000 or isn't that necessary?

make into 2 separate sentences

Must spell out further - cf maintenance below.

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22. A new tax regime will be introduced for maintenance payments:

- for payments under new maintenance arrangements, relief will be restricted to payments to a divorced or separated spouse, up to a limit equal to the [single allowance]. Recipients will not be liable to tax on maintenance payments;

still under discussion

- for existing maintenance arrangements, in 1988-89 the present rules will continue to apply except that a divorced or separated spouse will be exempt from tax on the first [£2,605] (the single allowance) of maintenance received (after grossing up at the basic rate where tax has been deducted by the payer). From 1989-90, all payments will be made gross and relief for the payer will be limited to the amount which qualified for relief in 1988-89.

[The changes are estimated to cost £15 million in 1990-91 and £10 million in 1991-92, and to yield £20 million eventually.]

from 18 per cent

23. The additional rate of income tax charged on the income of discretionary and accumulation trusts will be ~~abolished~~, reduced to 10 per cent from 1988-89].

24. The legislation on Lloyd's reinsurance to close (RIC) will be modified so that it will not apply to Lloyd's members who ceased membership of a syndicate at the end of the underwriting year, and are therefore not members of the syndicate to which the relevant RIC premium is paid. [The legislation will first take effect for the Lloyd's 1985 Account, which closes at the end of 1987. This is the first year to which the 1987 legislation on Lloyd's RIC will apply].

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This was drafted before we saw Mr Taylor's minute of 22 February to Mr Eason.

33. The new system of independent taxation for husbands and wives will apply from 1990-91. The revenue costs in 1990-91 and 1991-92 for income tax are estimated at £[630] and £[970] million respectively. These figures are based on the existing distribution of income between husbands and wives and allow for transitional protection for certain couples. [In addition, there could be further annual revenue costs of some £[350] million resulting from the transfer of investments between spouses, but this estimate is highly uncertain.] For capital gains tax, the prospect of independent taxation may lead some couples to defer disposals until the new arrangements are in place; and from 1990-91 onwards, couples may be expected to transfer assets to take advantage of the availability to each spouse of the annual exempt amount and any unused portion of their basic rate bands. The figure for 1989-90 in table 4.1 reflects the deferral of disposals. Costs for capital gains tax in 1990-91 and 1991-92 are each estimated at £60 million. Those estimates which allow for changes in taxpayers' behaviour are subject to a high degree of uncertainty.

34. A general limit of [£500,000] will be set on the amount of investment in any one company in any period of 12 months qualifying for relief under the Business Expansion Scheme. The estimated yield ^{depends on take up and} is highly uncertain.

35. Relief under the Business Expansion Scheme will be made available for investment in companies providing private rented housing [under the new assured tenancy scheme]. A limit of (£10 million) will apply to qualifying investment in these companies. The estimated revenue cost depends upon take up and is highly uncertain.

?
Include also higher limit for shipping and other BES measures.

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42. The rules for calculating industrial buildings allowance following a sale and those for transfers of machinery or plant between connected persons will be amended to prevent excessive relief where one person is not chargeable to tax in the United Kingdom. These changes will prevent a potential Exchequer loss of up to £150 million in 1991-92 with a diminishing effect in later years.]
43. The legislation relating to capital allowances for safety expenditure at sports grounds will be amended from 1 January 1988 to take account of changes to the Safety at Sports Grounds Act 1975.
44. Capital allowances on expenditure at certain quarantine premises will be abolished from 16 March 1988.
45. The relief for the costs incurred by a business in entertaining overseas ^{businessmen} ~~customers~~ will be withdrawn.
46. The base date for capital gains tax and corporation tax on gains will be changed from 6 April 1965 to 31 March 1982. The total cost of rebasing will build up to ^{a great} some £850 million in 1991-92. From 1989-90 onwards, the amount attributable to companies' gains is about three-quarters of the total. The figures take account of the likely effect of this measure on the volume and timing of disposals by individuals and companies.
47. (a) The present flat rate penalty for failure to notify liability to tax will be replaced by a fully mitigable penalty up to the amount of tax unpaid.
- (b) The Revenue's power to call for returns of information will be extended to details (where relevant

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for tax) of payments for services by Government Departments, grants or subsidies paid out of public funds and the names of licence holders.

(c) The Revenue's power to call for documents relating to taxpayers suspected of avoidance or evasion will be extended to include the Department of National Savings, and, in order to identify taxpayers suspected of serious default, to documents relating to taxpayers whose identity is not known to the Revenue.

(d) The Revenue will be allowed the same access to records held on computer as it is allowed to records held on paper.

The ~~estimated~~ yield of these measures is based on the unreported tax liabilities which will be uncovered. ^{an estimate of}

48. Changes in the tax rules concerning the conversion of building societies into public limited companies are necessary in order to prevent unintended tax charges arising.
49. As a consequence of the reduction in the basic rate, the rate of advance corporation tax (ACT) for 1988-89 will be 1/3rd of the amount of the distribution. This reduction in ACT will be balanced by an increase in the subsequent liability to mainstream corporation tax.
50. The small companies' rate of corporation tax for the financial year 1988 will be reduced to 25 per cent.
51. [The rules for company residence and migration will be changed. In future companies will be resident for tax purposes if they are incorporated or are centrally managed and controlled here. Companies will be able to migrate if they pay their tax liability, including liability on accrued gains.]

This, shorter, version is much preferable to longer version in main chapter.

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What is this?

52. The Finance (No 2) Act 1987 repealed part of the definition of an investment trust. The full definition will be reinstated, and the legislation will include provision to ensure that the repeal was never effective.
53. The indexation allowance will be denied or restricted on disposal of certain intra-group debts and shareholdings. This provision counters use of the indexation allowance to create large artificial capital losses which could cause a significant loss of tax.
54. As a result of a recent court ruling, share exchanges by companies in the same group can now give rise to capital gains or losses being taxed or allowed more than once. The legislation will be amended so as to remove that anomaly.
55. Capital allowances in respect of properties let on assured tenancy terms by "approved bodies" will come to an end when the Housing Bill takes effect. Changes will be made to the capital allowances legislation to ensure that relief for past years is not withdrawn and to provide transitional arrangements in respect of expenditure already incurred.
56. Rollover relief will be extended to satellites and spacecraft from 28 July 1987 and to milk and potato quotas from 30 October 1987.
57. From 1988-89, the capital gains of individuals and trusts will be taxed at income tax rates, that is as if they formed the marginal slice of income. The revenue yield in 1990-91 is estimated at £40 million and in 1991-92 at £85 million. The figures take account of the effect of rebasing of gains (item [46] above) and of the likely effect of taxing gains at income tax rates on the volume and timing of disposals.

Long way from 46.

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Do we really
need to go
into all
this detail?

- from 16 March, the daily rates of penalty for regulatory offences will be halved and a minimum and maximum level of penalty introduced;
- the third test for serious misdeclaration penalty is to be replaced by a non-automatic penalty which relates to the amount of tax involved;
- VAT registered local authorities and similar bodies will become eligible for repayment supplement and liable to both the serious and the persistent misdeclaration penalties;
- the level of error on a return which excludes eligibility for repayment supplement is to be increased to £250 or 5% of the tax claimed, whichever is the greater;
- from late 1989, adjustments not exceeding £500 in total may be voluntarily declared in the trader's VAT account (such amounts will not normally be liable to either an interest charge or serious misdeclaration penalty).

X

69. From 16 March 1988 the ^{VAT threshold} ~~registration limits~~ will be increased to £22,100 per annum and £7,500 per quarter.

70. The rules for registration of voluntary and intending traders will be simplified and restrictions and conditions removed.

X

71. The taxing provision relating to confectionery will be ^{amended} ~~brought up to date~~, with the main effect of taxing all cereal bars at the standard rate.

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good formulation,
usable elsewhere.

Excise duties

72. From [], where a taxable person issues himself with an invoice under the terms of an approved self-billing arrangement, he will be responsible for determining the correct VAT liability.
73. From 1 August 1988, VAT incurred by businesses on entertaining foreign customers will no longer be deductible, to bring it into line with the treatment of VAT on other business entertainment.
74. There will be no changes in the rate of duty on spirits.
75. The duty on typical beer will be increased by [4.7 per cent] equivalent to [1p] a pint (inclusive of consequential VAT).
76. 1 October 1988, beer duty will be charged on the basis of [£0.90] a hectolitre for every degree by which the original gravity of the beer exceeds 1000^o.
77. The duty on cider and perry will be increased by [9.7] per cent or [1p] a pint (inclusive of consequential VAT).
78. The duties on still table wine, made-wine and sparkling wine will be increased by [4.7] per cent, equivalent to [4p] on a 75cl bottle of still wine and [6.1p] on a 70cl bottle of sparkling wine (both inclusive of consequential VAT]
79. There will be no change in the rate of duty on fortified wines.
80. Lower strength mixed drinks, not exceeding 5.5 per cent alcohol, will be dutied according to their alcoholic strength on a scale proportionate to table wine duty. This will bring duties on wine-based and similar mixed drinks into line.

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OF: 12

REF NO: ACSA/17

FROM: A C S ALLAN

DATE: 26 February 1988

MISS SINCLAIR

cc PS/Financial Secretary
Sir P Middleton
Mr Scholar
Mr Culpin
Mr Odling-Smee
Miss C Evans
PS/IR
Mr P R H Allen - C&E

FSBR CHAPTER 4

The Chancellor was most grateful for your minute of 22 February and the draft of Chapter 4.

I attach a marked-up copy of the pages on which the Chancellor had comments.

There are one or two other points:

- i. The Chancellor was content with the section on independent taxation. He would prefer it to be boxed and kept on one page.
- ii. He would prefer to use the same wording as last year in the first part of the introduction to the Annex to table 4.1 (discussed in your new paragraph 4).
- iii. Is it necessary to include the paragraph about measures announced and implemented before Budget day (entertainments and gifts etc) in the introduction to the Annex?
- iv. The Chancellor noted that the ordering of the items produced a large gap between CGT re-basing and CGT rates, both in the Table and in the Annex. He would prefer them next to each other, or at least much closer together.

ACSA
A C S ALLAN

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NOT TO BE COPIED**4 The Budget tax proposals**

4.01 The main tax changes proposed in the Budget are summarised below. A full list of changes is given in Table 4.1

Income tax

4.02 The basic rate of income tax will be reduced to 25 per cent. There will be a single higher rate of income tax of 40 per cent, ~~The scale of charge will be:~~ P4.02A

Rate of tax per cent	Taxable income £
25	1-20,000
40	above 20,000

*which will apply
to taxable income
over £20,000.*

4.03 The main income tax personal allowances will be increased by twice the amounts due under the statutory indexation provisions (based on the increase of 3.7 per cent in the RPI in the year to December 1987). This will mean that:

the single person's and wife's earned income allowances will rise from £2,425 to £2,605;

the married allowance will rise from £3,795 to £4,095;

the age allowance for those aged 65 to 79 will rise from £2,960 to £3,180 (single) and from £4,675 to £5,035 (married);

the age allowance for those aged 80 or over will rise from £3,070 to £3,310 (single) and from £4,845 to £5,205 (married);

the income limit for age allowance will rise from £9,800 to £10,600;

the additional personal allowance and widow's bereavement allowance will rise from £1,370 to £1,490.

4.04 The housekeeper allowance, dependent relative allowance and the allowance for the services of a son or daughter will be abolished.

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4.05 From [6 April 1989] an unmarried couple will not be entitled to more than one additional personal allowance.

**Life assurance
premium relief**

4.06 The rate of premium relief for life assurance policies taken out before 14 March 1984 will be reduced to [12½ per cent] from 6 April 1989.

**Benefits in
kind**

4.07 Car benefit scale charges for 1988-89 will be set at twice their 1987-88 levels [and for 1989-90 they will be increased by ^{at least} 10 per cent above the 1988-89 levels].

4.08 The gross income threshold above which employees are liable to tax on certain benefits will be raised from £8,500 to £10,000.

(the "PIID" limit)

4.09 The exemptions from tax for luncheon vouchers up to the value of 15p per day, and for the benefit of meals provided at less than cost by an employer in a canteen or dining room not available to staff generally will be withdrawn from 6 April 1989.

? A car parking

**Mortgage
interest relief**

Very convoluted
- needs simplifying

4.10 For loans taken out from 1 August 1988, tax relief for two or more people borrowing to buy the same property as their only or main residence will be limited to the interest on £30,000 in total for the residence. Relief on new loans for home improvements and new loans for the purchase of residences for dependent relatives and divorced or separated spouses will be abolished from 6 April 1988.

The tax treatment of covenants will be reformed and simplified.

Covenants

4.11 Non-charitable covenants made by individuals on or after Budget day will no longer attract tax relief. Relief for covenants made before Budget Day will continue. There will be parallel changes in the student grant system (see paragraph 5[]). Covenants to charities will not be affected, nor will non-charitable covenants made before Budget day.

and income from such covenants made after Budget day will not be taxable in the hands of the recipient.

**Charitable
giving**

4.12 The limit on charitable donations qualifying for tax relief under the payroll giving scheme will be increased to £240 a year from 1988-89.

doubled from £120

**Maintenance
payments**

4.13 The tax treatment of maintenance payments will be reformed. Under new maintenance arrangements recipients will not be liable to tax on the payments; relief for those making payments will be restricted to payments to a divorced or separated spouse, up to a limit of

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[£2,605]. Transitional provisions will be introduced to protect existing maintenance arrangements.

Employee share schemes

4.14 [From 6 April 1989, options granted under an approved discretionary share option scheme will only qualify for tax relief if the company also operates an approved all-employee share or share option schemes.]

Needs better explanation

4.15 Following consultation last year, the scope of the income tax charge on unapproved employee share schemes under Section 79 of the 1972 Finance Act will be reduced.

Trusts

4.16 The additional rate of income tax on discretionary trusts will be [~~abolished from 1988-89~~/reduced to ¹⁰ per cent for 1988-89.]

Capital gains

4.17 The capital gains tax annual exempt amount will remain at £6,600 in the case of individuals and £3,300 in the case of most trusts.

gains made before that date will no longer be liable to tax.

4.18 The base date for capital gains will be brought forward from 6 April 1965 to 31 March 1982. The present indexation provisions will continue to apply to gains accruing from 31 March 1982. The proposal will also apply to companies' gains.

4.19 Gains, after deduction of the exempt amount and allowing for rebasing to 1982 and indexation, will be added to income and taxed at income tax rates (as if they were the marginal slice of income).

4.20 From 6 April, 50 per cent of any gains between £125,000 and £500,000 will qualify for retirement relief, subject to the general conditions for the relief.

Inheritance tax

4.21 From Budget Day the threshold will be increased from £90,000 to ^{for inheritance tax} ~~£107,000~~ ^{£110,000}. Chargeable transfers above this amount will be taxed at a single rate of 40 per cent. *The £100,000 limit on the amount that can be given to a political party without incurring inheritance tax will be abolished.*

~~4.22 The limit on the amount which can be given to a political party without incurring IHT will be removed.~~

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Business tax

4.23 The ~~small companies'~~ rate of corporation tax will be reduced to 25 per cent. The rate of advance corporation tax (ACT) will go down automatically to $\frac{1}{3}$ as a consequence of the reduction in the basic rate of income tax.

4.24 The main rate of corporation tax for the financial year 1988 will be 35 per cent.

4.25 ~~[The ceiling above which capital allowances on cars are restricted will be increased from £8,800 to [£10,000] for expenditure after 15 March 1988.]~~

In common with other business entertainment,

4.26 The cost of entertaining overseas ^{businessmen} customers will no longer be an allowable business expense for tax purposes. This change will take effect from Budget Day, except for commitments entered into before that date. From 1 August 1988 the VAT paid by businesses on this entertainment will no longer be deductible.

4.27 A number of changes will be made to prevent tax charges arising on the conversion of building societies into public limited companies.

Too flat: needs expanding

Business Expansion Scheme

4.28 The Business Expansion Scheme will be changed to permit relief on investment in companies providing private rented housing.

4.29 A general limit of [] will be set on relief under the Business Expansion Scheme for investment in any one company in any period of twelve months, with a higher limit of [] for investment in companies providing private rented housing ^{or shipping}

Lloyd's

4.30 Changes will be made to the present administrative arrangements for taxing members of Lloyd's.

4.31 The legislation on Lloyd's reinsurance to close will be modified to give relief to Lloyd's members who leave syndicates at the end of the underwriting year.

Forestry

4.32 Income from the occupation of commercial woodlands will be removed from the scope of Income Tax and Corporation Tax. (See paragraph [5.] for details of the proposed increase in grants for forestry.)

Is this essential here?

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Company taxation

4.33 Oil allowance for Petroleum Revenue Tax (PRT) will be reduced to 100,000 tonnes per chargeable period for all Southern Basin and onshore fields given development consent on or after 1 April 1982. (At the same time the Secretary of State for Energy proposes to abolish royalty payments for these fields.)

4.34 A new capital gains relief will be provided for disposals of oil licence interests in undeveloped areas wherever the consideration includes a work programme or another licence interest.

Company residence and migration

4.35 Section 482(1) (a) and (b) of the Taxes Act will be repealed with effect from Budget Day. In future companies will not need to apply to the Treasury for consent to move their residence abroad for tax purposes. The proposed new arrangements will:

extend the definition of UK company residence, so that companies either incorporated in the UK, or centrally managed and controlled here, will be deemed to be resident here for tax purposes;

require UK incorporated companies wishing to change their residence to change the country of their incorporation and to pay any tax arising on doing so; and

require UK resident companies not incorporated here wishing to change their residence to provide for the payment of their tax (including tax on accrued gains) before they do so.

Shorten considerably

Keith Report

4.36 Following recommendations of the Keith Committee, a number of changes will be made to encourage people to notify the Inland Revenue if they are liable to tax. These include the introduction of a tax-g geared penalty for failing to notify liability. There will be changes to the information powers of the Inland Revenue to help identify those who fail to notify liability to tax.

4.37 Legislation will be introduced to charge interest where payment to the Inland Revenue of income tax deducted by employers is delayed beyond the end of the tax year. The interest charge will be implemented when the necessary Inland Revenue computer systems

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are in place. [There will be parallel social security legislation to extend the interest charge to late payment of Class I or Class IV National Insurance contributions.]

VAT

4.38 From 16 March 1988 the registration limits will become £22,100 per annum and £7,500 per quarter.

4.39 The VAT civil penalty system, introduced in 1985, has been reviewed and various amendments are proposed. These include the introduction of a time-related penalty for late registration; the halving of daily penalties; changes to the rules about eligibility to repayment supplement; and changes to the rules for persons who persistently misdeclare their liability.

4.40 The provision for applying VAT to confectionery will be ~~brought up-to-date~~ ^{amended} with the main effect of taxing all cereal bars at the standard rate.

Excise duties

4.41 The duty on beer, light wine and sparkling wine will rise by the equivalent of [1p] on a typical pint of beer, [4p] on a bottle of table wine and a little over [6p] on a bottle of sparkling wine (all inclusive of consequential VAT). The duties on spirits and fortified wines will remain unchanged. The minimum duty charge for beer will be abolished and provision will be made for restructuring the duties on low strength mixed drinks.

4.42 The duty on leaded petrol will be increased by the equivalent of [just over 5½p] a gallon (inclusive of consequential VAT). The duty on unleaded petrol will remain unchanged. The duty on derv will rise by the equivalent of [just under 5p] a gallon.

4.43 The specific duties on cigarettes, hand-rolling tobacco and cigars will rise by the equivalent of [over 3p] on a packet of 20 cigarettes and [nearly 2p] on a packet on 5 small cigars. The duty on pipe tobacco will remain unchanged.

Could this be omitted?

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Table 4.1 Direct effects of changes in taxation

£ million

Estimated effect on receipts in:
1988-89 1989-90

See Annex 4
Paragraph numbers

Changes from a non-indexed base Changes from an indexed base Changes from an indexed base

INLAND REVENUE

Income tax

1	Reduction of 2p in basic rate	-2120	-2120	-2900
2	Abolition of higher rates of income tax above 40p	-835	-780	-1670
3	Increase in single allowance of £180 and married allowance of £300	-1235	-610	-835
4	Increase in additional personal allowance and widow's bereavement allowance of £120	-15	-5	-10
5	Increase in age allowance of £220 (single) and £340 (married) for those aged 65 to 79	-110	-55	-70
6	Increase in age allowance of £240 (single) and £360 (married) for those aged 80 and over	-20	-10	-10
7	Increase in income limit for age allowance of £800	-15	-5	-15
8	Increase in basic rate limit of £2,100 to £20,000	-300	-220	-420
9	Abolition of minor personal allowances	+10	+10	+10
10	Restriction on additional personal allowance for unmarried couples	-	-	+5
11	Reduction in relief on life assurance premiums	-	-	+70
12	Fringe benefits - car scale	+230	+230	+330
13	Fringe benefits - income threshold	-50	-50	-50
14	Fringe benefits - car parking space	*	*	*
15	Fringe benefits - luncheon vouchers and employer subsidised meals	-	-	[]
16	Fringe benefits - sports facilities	*	*	*
17	Mortgage interest relief ceiling applied to residence	+5	+5	+20
18	Abolition of tax relief on new home improvement loans	+80	+80	+200
19	Abolition of tax relief on new loans for homes for dependent relatives, divorced and separated spouses	*	*	*
20	Abolition of tax relief on new covenants	+45	+45	+105
21	Payroll giving to charities - increase in donation limit to £240 a year	*	*	*
22	Change in rules for maintenance payments	-20	-20	-20
23	Change in additional rate on discretionary trusts	[-5]	-5	[-10]
24	Lloyd's reinsurance to close - relief for leavers	*	*	*
25	Lloyds: reform of administrative arrangements	-	-	*
26	Link between approved discretionary and all-employee share schemes	-	-	-
27	Unapproved employee share schemes	*	*	*
28	Employee priority in public offer of shares	*	*	*
29	Approved 1984 employee share option schemes - restricted shares	*	*	*
30	Redundancy payments: top-slicing	*	*	*
31	Assessing procedure for Schedule D	-	-	-
32	Withdrawal of "top-slicing" relief for tax charged on premiums for leases, etc	*	*	*

Income tax and capital gains tax

33	Independent taxation of income and chargeable capital gains of husband and wife	*	*	-30
34	Business Expansion Scheme - limit on relief	*	*	+25
35	Business Expansion Scheme - private rented housing	*	*	-40

* = Negligible - = Nil

looks v odd, & requires footnote to tax table

must say a bit more

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Table 4.1 Direct effects of changes in taxation

£ million

See Annex 4
Paragraph numbers

Estimated effect on receipts in:		1989-90
1988-89	1989-90	
Changes from a non-indexed base	Changes from an indexed base	Changes from an indexed base

Income tax and corporation tax

? should be +10

36 Forestry - removal of commercial woodlands from scope of tax	-	-	*
37 Personal pensions - minor changes	[-10	-10	-5]
38 Refunds of employee pension contributions	+15	+15	+15
39 Occupational pensions - minor amendments	-	-	-
40 End of year interest on PAYE and subcontractors deductions	-	-	-
41 Capital allowances - motor cars	*	*	30
42 Capital allowances - exempt persons	-	-	-
43 Capital allowances - safety at sports grounds	*	*	*
44 Capital allowances - abolition of quarantine premises relief	*	*	*
45 Withdrawal of relief for entertaining overseas customers - businessmen	*	*	+5

Income tax, corporation tax and capital gains tax

46 Rebasing capital gains to March 1982	-25	-25	-340
47 Keith Committee administrative changes	+10	+10	+20

split into 2, one for CT and one for CGT, each in appropriate section

Income tax, corporation tax, capital gains tax and stamp duties

48 Conversion of building societies into public limited companies - changes in tax rules	-	-	-
--	---	---	---

Corporation tax

49 Reduction in rate of ACT to 1/3 rd of the amount of the distribution	-380	-380	-200
50 Reduction in small companies' rate to 25 per cent	*	*	-50
51 Company residence and migration - new rules	-	-	-
52 Definition of an investment trust	-	-	-
53 Indexation allowance - intra-group transactions	-	-	-
54 Intra-group share exchanges	-	-	-
55 Capital allowances - assured tenancies relief	-	-	-

Corporation tax and capital gains tax

56 Rollover relief ^{for} satellites, spacecraft, milk and potato quotas	*	*	-5
--	---	---	----

these are very far apart: more natural to have them closer / next to each other

Capital gains tax

57 Charging gains of individuals and trusts at income tax rates	+70	+70	+40
58 Annual exempt amount	-	-	+10
59 Retirement relief	-	-	+10
60 Building and Co-operative society shares	*	*	*
61 Homes provided for dependent relatives	-	-	*

* = Negligible - = Nil

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Table 4.1 Direct effects of changes in taxation

		£ million		
		Estimated effect on receipts in:		
		1988-89	1989-90	
See Annex 4 Paragraph numbers		Changes from a non-indexed base	Changes from an indexed base	Changes from an indexed base
Oil taxation				
62	Reduction in PRT oil allowances for certain fields	+30	+30	+30
63	New capital gains relief for certain oil licence disposals	-5	-5	-5
64	Petroleum revenue tax relief for certain tariff related costs	-	-	-
Inheritance tax				
65	Changes to rates and bands <i>Increase in threshold and change to flat rate</i>	-110	-90	-180
66	Abolition of limit on gifts to political parties	*	*	*
Stamp duties				
67	Stamp duty and reserve tax on paired shares	-	-	-
TOTAL INLAND REVENUE		-4760	-3895	-6020
CUSTOMS AND EXCISE				
Value added tax				
68	Keith Committee - review of civil penalties	*	*	*
69	Increase in registration limits	*	*	*
70	Revised registration requirements	*	*	*
71	Change in liability of certain confectionery	+5	+5	+10
72	Revision of approved self-billing arrangements	+5	+5	+5
73	Revised treatment of business entertainment for overseas customers	*	*	*
Excise duties				
74	No change in rate of spirits duty	-	-25	-30
75	Increase in rate of beer duty	+80	+20	+20
76	Abolition of minimum duty charge for beer	*	*	*
77	Increase in rate of duty on cider and perry	+5	+5	+5
78	Increase in rate of duty on light wine and made-wine duties	+20	+5	+10
79	No change in rates of duty on fortified wines	-	-5	-5
80	Revised duty regime for low strength mixed drinks	*	*	*
81	Increase in rate of duty on leaded petrol etc	+275	+80	+50
82	Increase in rate of duty on derv	+75	+25	+30
83	No change in rates of minor oil duties	-	-5	-5
84	Increase in rates of duties on cigarettes, hand-rolling tobacco and cigars	+100	-	-
85	No change in rate of duty on pipe tobacco	-	*	*
TOTAL CUSTOM AND EXCISE		+565	+110	+90

* = Negligible - = Nil

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8. The basic rate limit will rise from £17,900 to £20,000. The increase is ~~£1,400 more than~~ the amount due under statutory indexation. ↑
three times
9. The housekeeper allowance, dependent relative allowance and the allowance for the services of a son or daughter will be abolished.
10. From [6 April 1989] an unmarried couple will not be entitled to more than one additional personal allowance.
11. Following the reductions in the basic rate of income tax in successive Budgets, the rate of relief for life assurance premiums on policies taken out before 14 March 1984 will be reduced to [12.5] per cent from 6 April 1989. The starting date is to allow life offices time to make the necessary preparations. from 15 per cent to
12. For 1988-89 the scale for taxing car benefits in respect of company cars provided for directors and for higher paid employees will be double the 1987-88 levels. The previously announced scales for 1988-89 will not apply. Costs are measured from these previously announced scales. [A further increase of 10 per cent will be made for 1989-90.] [No change is proposed for 1988-89 and 1989-90 to the scale charges for car fuel benefit also used for VAT purposes.] not less than
13. For 1988-89 the rate of remuneration at which an employee is regarded as higher-paid and liable to tax in respect of certain benefits received by reason of his employment is to be increased from £8,500 to £10,000. (the 'PIID limit')
14. [The provision of a car parking space for the use of directors or higher-paid employees ~~on premises occupied by the employer~~] will be exempt from tax from 6 April 1988.]

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15. [The extra-statutory concession exempting from tax luncheon vouchers up to the value of 15p a day will be withdrawn with effect from 6 April 1989. The exemption from tax of the benefit of subsidised meals provided by an employer for directors and higher-paid employees in a canteen or dining room which is not open to the staff generally will also be withdrawn from the same date.]

16. [The benefit to employees of sports facilities provided on premises occupied by the employer and available to the staff generally will be exempt from tax from 6 April 1988.]

17. For loans taken out from 1 August 1988, tax relief for two or more people borrowing to buy the same property as their only or main residence will be limited to the interest on £30,000 in total for the residence.

18. Relief on new loans for home improvement will be abolished from 6 April 1988. Relief for existing loans [and for loans for the purchase or improvement of let property] is not affected.

19. Relief on new loans for the purchase of residences for dependent relatives and divorced or separated spouses will be abolished from 6 April 1988. Relief for existing loans is not affected.

20. Non-charitable covenants made on or after Budget day by individuals will no longer be effective for tax purposes. The change is estimated to yield £160 million in 1990-91, £175 million in 1991-92, and £[210] million eventually.

21. The limit on charitable donations qualifying for tax relief under payroll giving schemes will be increased to £240 a year from 6 April 1988.

Should there be a note somewhere saying the MIR limit will be set at £30,000 or isn't that necessary?

make into 2 separate sentences

Must spell out further - cf maintenance below.

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22. A new tax regime will be introduced for maintenance payments:

- for payments under new maintenance arrangements, relief will be restricted to payments to a divorced or separated spouse, up to a limit equal to the single allowance. Recipients will not be liable to tax on maintenance payments;

still under discussion

for existing maintenance arrangements, in 1988-89 the present rules will continue to apply except that a divorced or separated spouse will be exempt from tax on the first [£2,605] (the single allowance) of maintenance received (after grossing up at the basic rate where tax has been deducted by the payer). From 1989-90, all payments will be made gross and relief for the payer will be limited to the amount which qualified for relief in 1988-89.

[The changes are estimated to cost £15 million in 1990-91 and £10 million in 1991-92, and to yield £20 million eventually.]

23. The additional rate of income tax charged on the income of discretionary and accumulation trusts will be ~~abolished~~, reduced to 10 per cent from 1988-89].

from 18 per cent

24. The legislation on Lloyd's reinsurance to close (RIC) will be modified so that it will not apply to Lloyd's members who ceased membership of a syndicate at the end of the underwriting year, and are therefore not members of the syndicate to which the relevant RIC premium is paid. [The legislation will first take effect for the Lloyd's 1985 Account, which closes at the end of 1987. This is the first year to which the 1987 legislation on Lloyd's RIC will apply].

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This was drafted before we saw Mr Taylor's minute of 22 February to Mr Eason.

33. The new system of independent taxation for husbands and wives will apply from 1990-91. The revenue costs in 1990-91 and 1991-92 for income tax are estimated at £[630] and £[970] million respectively. These figures are based on the existing distribution of income between husbands and wives and allow for transitional protection for certain couples. [In addition, there could be further annual revenue costs of some £[350] million resulting from the transfer of investments between spouses, but this estimate is highly uncertain.] For capital gains tax, the prospect of independent taxation may lead some couples to defer disposals until the new arrangements are in place; and from 1990-91 onwards, couples may be expected to transfer assets to take advantage of the availability to each spouse of the annual exempt amount and any unused portion of their basic rate bands. The figure for 1989-90 in table 4.1 reflects the deferral of disposals. Costs for capital gains tax in 1990-91 and 1991-92 are each estimated at £60 million. Those estimates which allow for changes in taxpayers' behaviour are subject to a high degree of uncertainty.

34. A general limit of [£500,000] will be set on the amount of investment in any one company in any period of 12 months qualifying for relief under the Business Expansion Scheme. The estimated yield ^{depends on take up and} is highly uncertain.

35. Relief under the Business Expansion Scheme will be made available for investment in companies providing private rented housing [under the new assured tenancy scheme]. A limit of [£10 million] will apply to qualifying investment in these companies. The estimated revenue cost depends upon take up and is highly uncertain.

?
Include also higher limit for shipping and other BES measures.

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42. The rules for calculating industrial buildings allowance following a sale and those for transfers of machinery or plant between connected persons will be amended to prevent excessive relief where one person is not chargeable to tax in the United Kingdom. These changes will prevent a potential Exchequer loss of up to £150 million in 1991-92 with a diminishing effect in later years.]
43. The legislation relating to capital allowances for safety expenditure at sports grounds will be amended from 1 January 1988 to take account of changes to the Safety at Sports Grounds Act 1975.
44. Capital allowances on expenditure at certain quarantine premises will be abolished from 16 March 1988.
45. The relief for the costs incurred by a business in entertaining overseas ^{businessmen} ~~customers~~ will be withdrawn.
46. The base date for capital gains tax and corporation tax on gains will be changed from 6 April 1965 to 31 March 1982. The total cost of rebasing will build up to some ^{a peak of} £850 million in 1991-92. From 1989-90 onwards, the amount attributable to companies' gains is about three-quarters of the total. The figures take account of the likely effect of this measure on the volume and timing of disposals by individuals and companies.
47. (a) The present flat rate penalty for failure to notify liability to tax will be replaced by a fully mitigable penalty up to the amount of tax unpaid.
- (b) The Revenue's power to call for returns of information will be extended to details (where relevant

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for tax) of payments for services by Government Departments, grants or subsidies paid out of public funds and the names of licence holders.

(c) The Revenue's power to call for documents relating to taxpayers suspected of avoidance or evasion will be extended to include the Department of National Savings, and, in order to identify taxpayers suspected of serious default, to documents relating to taxpayers whose identity is not known to the Revenue.

(d) The Revenue will be allowed the same access to records held on computer as it is allowed to records held on paper.

The ~~estimated~~ yield of these measures is based on the unreported tax liabilities which will be uncovered. ^{an estimate of}

48. Changes in the tax rules concerning the conversion of building societies into public limited companies are necessary in order to prevent unintended tax charges arising.
49. As a consequence of the reduction in the basic rate, the rate of advance corporation tax (ACT) for 1988-89 will be 1/3rd of the amount of the distribution. This reduction in ACT will be balanced by an increase in the subsequent liability to mainstream corporation tax.
50. The small companies' rate of corporation tax for the financial year 1988 will be reduced to 25 per cent.
51. [The rules for company residence and migration will be changed. In future companies will be resident for tax purposes if they are incorporated or are centrally managed and controlled here. Companies will be able to migrate if they pay their tax liability, including liability on accrued gains.]

This, shorter, version is much preferable to longer version in main chapter.

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What is this?

52. The Finance (No 2) Act 1987 repealed part of the definition of an investment trust. The full definition will be reinstated, and the legislation will include provision to ensure that the repeal was never effective.
53. The indexation allowance will be denied or restricted on disposal of certain intra-group debts and shareholdings. This provision counters use of the indexation allowance to create large artificial capital losses which could cause a significant loss of tax.
54. As a result of a recent court ruling, share exchanges by companies in the same group can now give rise to capital gains or losses being taxed or allowed more than once. The legislation will be amended so as to remove that anomaly.
55. Capital allowances in respect of properties let on assured tenancy terms by "approved bodies" will come to an end when the Housing Bill takes effect. Changes will be made to the capital allowances legislation to ensure that relief for past years is not withdrawn and to provide transitional arrangements in respect of expenditure already incurred.
56. Rollover relief will be extended to satellites and spacecraft from 28 July 1987 and to milk and potato quotas from 30 October 1987.
57. From 1988-89, the capital gains of individuals and trusts will be taxed at income tax rates, that is as if they formed the marginal slice of income. The revenue yield in 1990-91 is estimated at £40 million and in 1991-92 at £85 million. The figures take account of the effect of rebasing of gains (item [46] above) and of the likely effect of taxing gains at income tax rates on the volume and timing of disposals.

Long way from 46.

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Do we really
need to go
into all
this detail?

- from 16 March, the daily rates of penalty for regulatory offences will be halved and a minimum and maximum level of penalty introduced;
- the third test for serious misdeclaration penalty is to be replaced by a non-automatic penalty which relates to the amount of tax involved;
- VAT registered local authorities and similar bodies will become eligible for repayment supplement and liable to both the serious and the persistent misdeclaration penalties;
- the level of error on a return which excludes eligibility for repayment supplement is to be increased to £250 or 5% of the tax claimed, whichever is the greater;
- from late 1989, adjustments not exceeding £500 in total may be voluntarily declared in the trader's VAT account (such amounts will not normally be liable to either on interest charge or serious misdeclaration penalty).

69. From 16 March 1988 the ^{VAT threshold} ~~registration limits~~ will be increased to £22,100 per annum and £7,500 per quarter.

70. The rules for registration of voluntary and intending traders will be simplified and restrictions and conditions removed.

71. The taxing provision relating to confectionery will be ^{amended} ~~brought up to date~~, with the main effect of taxing all cereal bars at the standard rate.

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72. From [], where a taxable person issues himself with an invoice under the terms of an approved self-billing arrangement, he will be responsible for determining the correct VAT liability.

73. From 1 August 1988, VAT incurred by businesses on entertaining foreign customers will no longer be deductible, to bring it into line with the treatment of VAT on other business entertainment.

*good formulation,
usable elsewhere.*

Excise duties

74. There will be no changes in the rate of duty on spirits.

75. The duty on typical beer will be increased by [4.7 per cent] equivalent to [1p] a pint (inclusive of consequential VAT).

76. 1 October 1988, beer duty will be charged on the basis of [£0.90] a hectolitre for every degree by which the original gravity of the beer exceeds 1000°.

77. The duty on cider and perry will be increased by [9.7] per cent or [1p] a pint (inclusive of consequential VAT).

78. The duties on still table wine, made-wine and sparkling wine will be increased by [4.7] per cent, equivalent to [4p] on a 75cl bottle of still wine and [6.1p] on a 70cl bottle of sparkling wine (both inclusive of consequential VAT]

79. There will be no change in the rate of duty on fortified wines.

80. Lower strength mixed drinks, not exceeding 5.5 per cent alcohol, will be dutied according to their alcoholic strength on a scale proportionate to table wine duty. This will bring duties on wine-based and similar mixed drinks into line.

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FROM: A C S ALLAN

DATE: 26 February 1988

MR MOWL

cc PS/Financial Secretary
Sir P Middleton
Sir T Burns
Mr Scholar
Mr Culpin
Mr Odling-Smee
Mr Sedgwick
Mr Turnbull
Miss C Evans

FSBR CHAPTER 6

The Chancellor was grateful for your minute of 24 February and the draft of Chapter 6. I attach a marked-up copy of the pages on which he had comments.

The other points he made were:

i. He could not reconcile the last sentence of your paragraph 6 (saying that the forecast for 1988/89 has non oil taxes and NTCs adjusted for Budget change increasing by $2\frac{1}{2}$ points more than non-oil GDP) with the figures in the table in your paragraph 5. The figures there seem to be 2.9% before Budget changes, and 0.4% after Budget changes.

ii. He would wish if at all possible to publish a figure for the non-North Sea tax burden in 1988-89 identical to that in 1987-88. This would mean shading the present provisional forecast for 1988-89 down from 37.6 to 37.5; at the same time it would be helpful to shade down the forecast of the total tax burden in 1988-89 from 37.8 to 37.7, the same as in 1987-88. Alternatively, but no doubt more problematic, would be to shade up the 1987-88 estimates.

iii. He was grateful for the charts on the tax burden and ratio of GGE to money GDP; he prefers the version starting in 1978-79.

iv. He agrees with your proposed change to the sign convention in table 6.7. But he felt some explanation was

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needed of the convention that a financial surplus is shown as negative and a financial deficit as positive, which is counter-intuitive.

v. He did not feel he wanted to carry through to the FSBR the term 'public sector net debt repayment' (PSDR).

vi. On chart 6.2, why does the proportion of expenditure on debt interest not come down between 1978/79 and 1988-89 (it is shown as 10% in both years)? He also wonders whether the figures for health (growing from 10% to 11%) may not cause confusion, since we have used figures on a different basis (ie as proportions of departmental spending) quite widely in other contexts - eg chart 1.10 of the PEWP.

ACSA

A C S ALLAN

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The scope of this chapter

6.01 This chapter brings together revenue (discussed in Chapter 4) and spending (in Chapter 5), and provides an analysis and forecast of the public sector's finances in 1988-89 together with estimates of outturn in 1987-88. It also comments on the main features of the public sector's finances in those two years, including the most important changes that have taken place since last year's projections. Table 6.1 is a summary.

Table 6.1 Public expenditure, receipts and borrowing

	£ billion			
	1986-87 Outturn	1987-88 1987 Budget	Latest estimate	1988-89 Forecast
General government expenditure	164.8	173.5	171.6	182.8
General government receipts	160.0	168.8	173.5	184.7
General government borrowing requirement	4.9	4.7	- 2.0	- 1.9
Public corporations' market and overseas borrowing	- 1.5	- 0.8	- 0.9	- 1.2
Public sector borrowing requirement	3.4	3.9	- 2.9	- 3.1

6.02 There is now estimated to be ~~not~~ ^{a negative} public sector ~~net~~ ^{borrowing} requirement, ~~ie a budget surplus,~~ ^{ie a budget surplus,} ~~repayment (PSBR)~~ of about £3 billion in 1987-88, compared with ~~the~~ ^{PSBR} a forecast of a ~~public sector borrowing requirement (PSBR)~~ of £4 billion made a year ago. This would be the first budget surplus since 1969-70 and only the second since 1952, the earliest year for which PSBR figures are available. ~~There is also forecast~~ ^{is also forecast} to be a net repayment of about £3 billion in 1988-89.

Public sector's finances:

three-fold analysis

6.03 The public sector's finances can be analysed in a number of different ways: by type or activity, by sector and by economic category. The rest of this chapter sets out these three analyses in detail.

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Public sector's finances: analysis by type or activity
6.04 Table 1.2 analyses the public sector's finances by type or activity. The main receipts of general government (ie. central plus local government) are grouped according to the kind of activity which gives rise to them, while spending is shown by department, as in Chapter 5 and in the public expenditure White Paper. Its bottom line, the PSBR, is derived from those two totals. This derivation is repeated in Table 6.1.

Receipts

In 1987-88

6.05 General government receipts are now projected to exceed the 1987 Budget forecast by about £4¾ billion. As Table 1.2 shows, most components of general government receipts are likely to be higher than originally forecast. The main contributors to the extra receipts are income tax (£1 billion), VAT (£1 billion), ~~and~~ North Sea Revenues (£¾ billion), and corporation tax (£¾ billion).

6.06 Additional income tax receipts are mainly the result of *the stronger growth of the economy & higher incomes.* VAT receipts have increased by more in 1987-88 than would have been expected from the *recorded* currently estimated increase in total consumer spending: *this implies* either *that* the proportion of total spending on goods and services subject to VAT has increased, *which goes* or *that* estimates of consumer spending in 1987 *may* will be revised up later, *last year.* as happened last year. The higher than expected oil revenues in 1987-88 are largely the result of a higher *dollar oil price* than assumed *last year.* dollar oil price. ~~Although non-North Sea corporation tax receipts are estimated to be higher than in the 1987 Budget forecast, they are lower than forecast in the 1987 Autumn Statement.~~

6.07 General government receipts are forecast to rise by 6½ per cent in 1988-89, following an estimated 8½ per cent increase in 1987-88. This is a little less than the rate of growth

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(to be discussed)

6.08 Oil revenues, which in the event in 1987-88 were only slightly below the 1986-87 level, are forecast to fall by about £1 billion in 1988-89 ^{as a result of with} ~~due to~~ a lower average oil price and lower production. The forecast assumes that ~~sterling and~~ oil prices [remain close to recent levels] Oil production is assumed to fall in 1988 to a level close to the centre of the Department of Energy's range. A \$1 a barrel difference in the oil price in 1988 would change revenues by about £250 million in 1988-89 and £300 million in a full year. A change of 1 million tonnes in oil production in 1988, spread evenly across fields, would alter revenues by about £40 million in 1988-89 and £45 million in a full year.

6.09 Non-oil receipts are forecast to rise by 7 per cent in 1988-89. As can be seen from Table 1.2 there is within this overall increase:

a 1 1/2 per cent increase in income tax receipts. Without the Budget measures the forecast increase would have been 10 per cent;

of [] per cent

a further rise in receipts of corporation tax (including ACT but excluding North Sea mainstream corporation tax).

~~[The 1988-89 increase reflects a provisional estimate of a 25 per cent increase in profits in 1987.]~~

a 16 per cent rise in capital taxes, ^{mainly} reflecting rising asset prices in earlier years;

This reflects continued growth in company profits in 1987.

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a 5½ per cent increase in the excise duties on petrol, tobacco and alcohol, a little below the increase in consumers' expenditure reflecting the trend decline in the share of these items in the total;

a small fall in stamp duty following the fall in stock market prices and turnover.

6.10 Table 6.2 shows taxes (including rates) and national insurance contributions as a percentage of GDP. ~~The non-oil percentage is forecast to increase marginally in 1988-89. Without the 1988-89 figure it would have increased by about one percentage point higher.~~

Non-oil taxes have risen slightly as a percentage of non-oil GDP in each of the last two years, and [a further marginal increase] is forecast for 1988-89.

Table 6.2 Taxes and national insurance contributions (NICs) as a percentage of GDP

	1982-83	1983-84	1984-85	1985-86	1986-87	1987-88 Latest estimate	1988-89 Forecast
Total taxes and NICs as a share of total money GDP	38.9	38.5	39.1	38.5	37.8	37.7	37.8
Non-oil taxes and NICs as a share of non-oil money GDP	38.2	37.8	37.8	37.0	37.3	37.5	37.6

Expenditure

6.11 General government expenditure is now forecast to be about £171½ billion in 1987-88, £2 billion lower than in the 1987 Budget forecast. ^{outturn for the} The ~~planning total~~ ^{in the original plans} ~~outturn~~ is expected to be £2½ billion lower than ~~planned~~ and gross debt interest payments nearly £½ billion lower than forecast. Partly offsetting these is an increase in other national accounts adjustments.

6.12 General government expenditure is expected to rise by 6¾ per cent in 1988-89, to £183 billion. The planning total, at £154 billion, ^{published} ~~is~~ ^{as in} The public expenditure

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White Paper 1988-89
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payments in 1988-89 are now forecast to be lower than projected in the White Paper as a result of ^{the marked reduction in the PSBR,} lower borrowing and to be ~~at much the same level as expected for 1987-88.~~

Borrowing

6.13 The difference between general government receipts and expenditure is the general government borrowing requirement (GGBR), as shown in Table 6.1. As general government lending to public corporations is included in general government expenditure, the GGBR together with public corporations' market and overseas borrowing, gives the PSBR.

6.14 There was a substantial budget surplus in the first ten months of 1987-88. Excluding privatisation proceeds the PSBR was some £2 billion lower than in the same period of 1986-87. This reduction in borrowing was almost entirely due to lower central government own [^] account borrowing. Local authority borrowing has been higher than in 1986-87 and public corporations' borrowing little changed. Taking into account the well established pattern of relatively high borrowing in the final two months of the year, the forecast for 1987-88 as a whole is a budget surplus ~~for 1987-88~~ of about £3 billion, or 3/4 per cent of ~~money~~ GDP.

^

X
X

further budget surplus
6.15 A ~~PSBR~~ [^] of £3 billion, or 3/4 per cent of ~~money~~ GDP, is ~~also~~ forecast for 1988-89.

Trends in receipts and expenditure

6.16 Chart 6.1 shows trends in taxes and expenditure as percentages of ~~money~~ GDP. ^{Revenues from non-oil taxes as a percentage of non-oil GDP} ~~The percentage for non-oil taxes~~ and national insurance contributions fell between 1981-82 and 1985-86, but ^{since then it has been rising.} ~~rose slightly in 1986-87 and again in 1987-88.~~

to be further discussed

[It is forecast to rise marginally in 1988-89.] ~~to a level below~~

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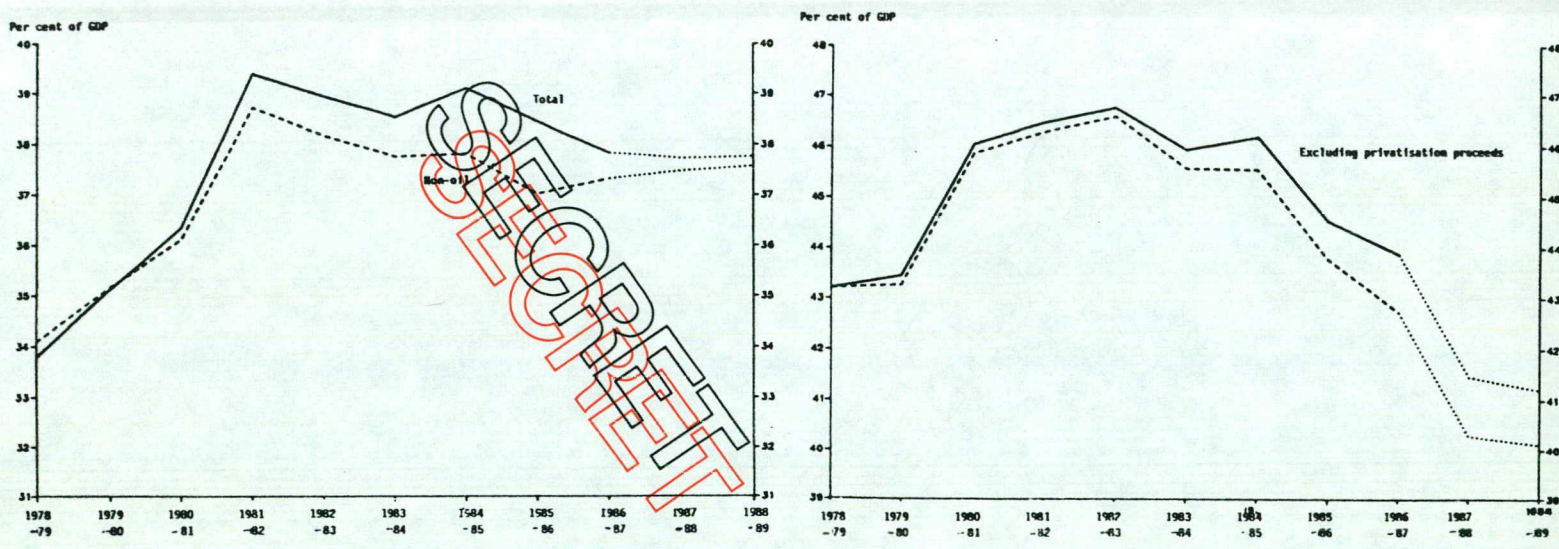
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~~its share of general government expenditure~~
~~(excluding privatisation proceeds)~~ has fallen every year but
~~one~~ since 1982-83 and is forecast to fall again in 1988-89.
every year
except for a small rise in 1984-85 as a result of the miners' strike; it

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Chart 6.1 Taxes and expenditure relative to GDP

Taxes and national insurance contributions
General government expenditure
as a percentage of



6.17 Chart 6.2 shows the significant changes in the structure of general government receipts and expenditure which have taken place since 1978-79.

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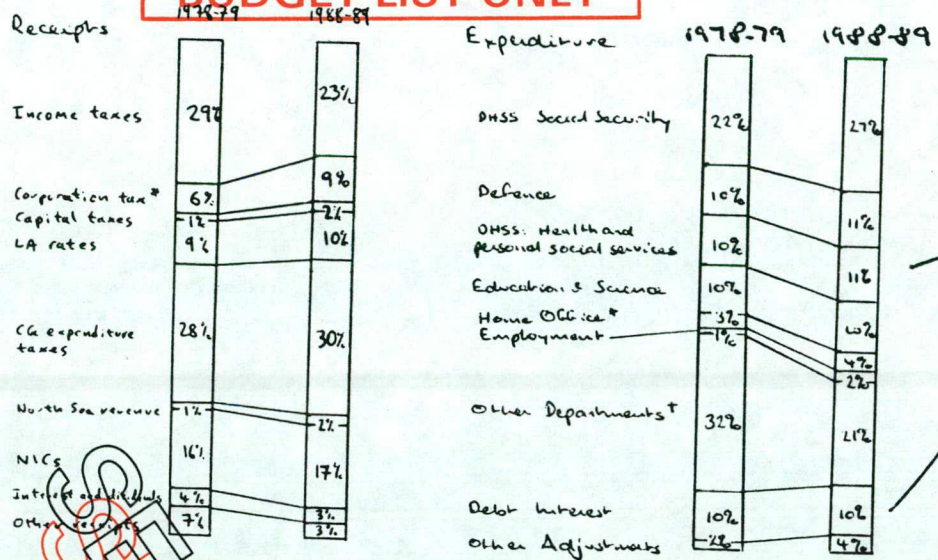
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Chart 6.2 The structure of receipts and expenditure

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SEE COVER NOTE

* Excluding North Sea

† and legal departments
‡ including Privatisation Proceeds and Reserve

Public sector's finances: analysis by sector

6.18 Table 6.3 shows which authorities or sectors are repaying debt or undertaking ^{net} borrowing in 1987-88 ^{1986-87 and} by central government, local authorities and public corporations.

Table 6.3 Public sector borrowing requirement

	£ billion	
	1986-87 Outturn	1987-88 Latest estimate
1 Central government borrowing on own account	4.5	- 2.8
2 Local authority borrowing from central government	5.9	5.2
3 Local authority borrowing from market and overseas	- 5.6	- 4.0
4 Total local authority borrowing	0.2	1.1
5 Public corporations' borrowing from central government	0.1	- 0.3
6 Public corporations' borrowing from market and overseas	- 1.5	- 0.9
7 Total public corporations' borrowing	- 1.4	- 1.2
8 Public sector borrowing requirement	3.4	2.9
Memorandum item:- Central government borrowing requirement (lines 1+2+5)	10.5	

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6.19 Tables 6.4 to 6.6 show estimated outturns and forecasts of receipts and expenditure in 1987-88 and 1988-89 for each of the three sectors. These tables include some of the analysis by economic category in Table 6.7. Expenditure in 1988-89 does not include an allocation of the Reserve, although the forecast of the PSBR assumes that the Reserve is fully spent.

Central government

6.20 Central government spending includes grants and subsidies to local authorities and public corporations (including nationalised industries), which are included in the receipts of those sectors, shown in Tables 6.5 and 6.6.

Table 6.4 Central government transactions

	£ billion		
	1986-87 Outturn	1987-88 Latest estimate	1988-89 Forecast
<u>Receipts</u>			
Tax and royalties	104.4	115.2	121.7
National insurance and other contributions	26.7	28.8	31.6
Other	10.4	11.2	11.3
Total receipts	141.4	155.2	164.5
<u>Expenditure</u>			
Current expenditure on goods and services	49.4	53.0	55.7
Current grants and subsidies	77.3	80.7	82.8
Interest	16.5	16.9	17.4
Net lending, capital expenditure, and cash expenditure on company securities	2.7	1.8	2.6
Total expenditure	146.0	152.5	158.4²

¹ Excluding lending to local authorities and public corporations
² Excluding any allocation from the Reserve

[for consistency]

Local authorities

6.21 Local authority receipts consist primarily of rate income plus grants from central government. The forecast increase in rate income (net of rate rebates) between 1987-88 and 1988-89

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takes account of a certain information about rate rebates by local authorities, additions to rateable value, and changes to the system of rate rebates introduced by the Social Security Act 1986.

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6.22 The local authority borrowing requirement (LABR) fell sharply in 1986-87 to £¼ billion, from £1¼ billion in 1985-86. The LABR in the first ten months of 1987-88 was higher than in the same period of 1986-87 and it seems likely that borrowing in the year as a whole will be above that in 1986-87, although still well below the levels of ^{earlier} ~~the~~ years, ~~immediately prior to~~ ~~that~~. The estimates of local authority receipts and expenditure do not fully explain the LABR in 1986-87 and 1987-88 (other receipts, in table 6.5 and miscellaneous financial transactions in table 6.7 include a balancing item).

Table 6.5 Local authority transactions

	£ billion		
	1986-87 Outturn	1987-88 Latest estimate	1988-89 Forecast
<u>Receipts</u>			
Rates (net of rate rebates) ¹	15.6	17.0	19.2
Rate support grant	11.8	12.6	13.3
Other grants from central government	11.0	12.1	12.2
Other	6.3	5.2	5.6
Total receipts	44.7	46.9	50.4
<u>Expenditure</u>			
Current expenditure on goods and services	31.1	34.4	35.2
Current grants and subsidies	5.4	5.8	6.0
Interest	4.1	4.7	4.5
Net lending and capital expenditure	4.2	3.8	4.4
Total expenditure	44.8	48.1	50.1²

¹ Memo: Rate rebates

1.7

1.8

1.4

² Excluding any allocation from the Reserve

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Public corporations

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Table 6.6 shows public corporations' transactions. The public corporations' receipts include subsidies and capital grants from central and local government. For the nationalised industries (and the majority of other public corporations) their net external finance, ie. their borrowing plus subsidies and grants, is included in the public expenditure planning total. Public corporations' net external financing requirement, and not their borrowing requirement (PCBR), is the best measure of the public corporations' total contribution to the PSBR, because it ~~also~~ includes, ^{in addition} ~~as well as~~ borrowing, subsidies and grants provided by the central government which have to be financed from taxation or central government borrowing.

Table 6.6 Public corporations' transactions

	£ billion		
	1986-87 Outturn	1987-88 Latest estimate	1988-89 Forecast
<u>Receipts</u>			
Gross trading surplus (including subsidies)	7.4	7.0	7.4
Other	2.9	2.1	2.2
Total receipts	10.3	9.1	9.6
<u>Expenditure</u>			
Interest, dividends and taxes on income	3.3	3.1	3.8
Net lending and capital expenditure	5.5	4.7	5.7
Total expenditure	8.8	7.9	9.5¹
Memo: nationalised industries' external finance	0.4		0.7
other public corporations' contribution to the planning total	0.8		0.8

¹ Excluding any allocation from the Reserve

6.24 Changes in public corporations' income and expenditure from one year to another are affected by privatisations which

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