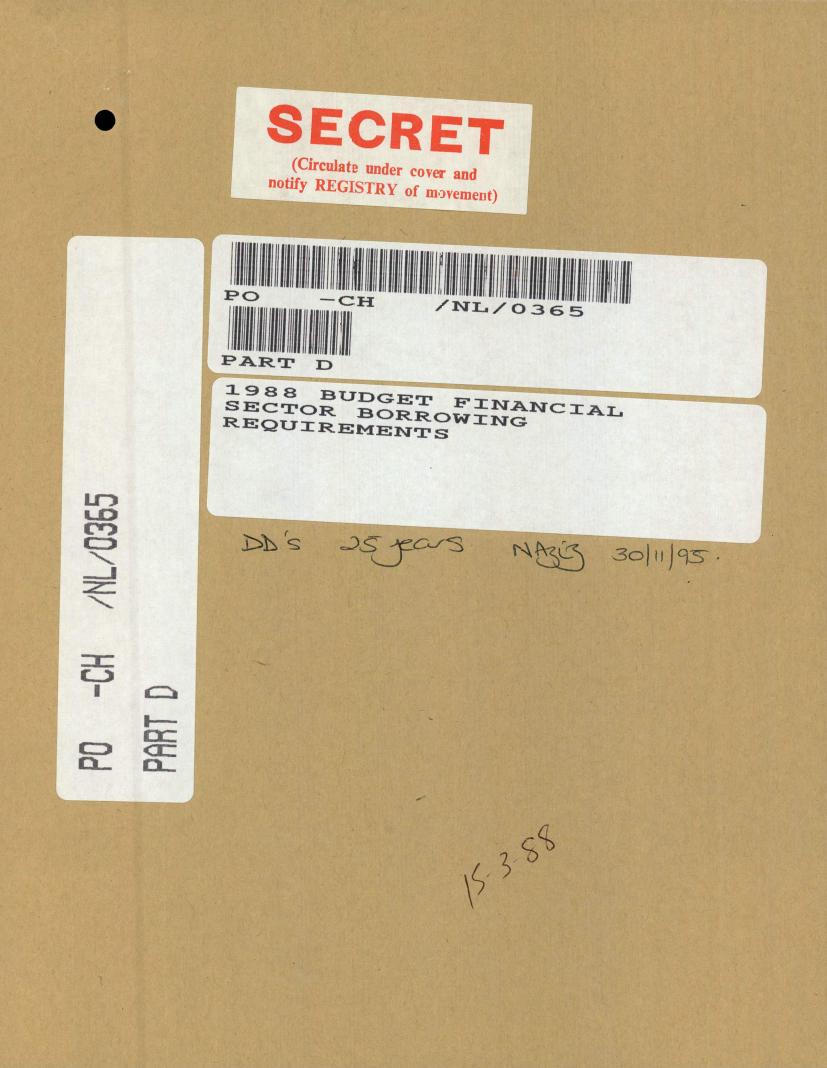
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FROM: COLIN MOWL DATE: 10 March 1988

MR RITCHIE

cc PPS/Chancellor PS/CST Sir P Middleton Sir T Burns Mr Anson Mr Scholar Mr Odling-Smee Mr Sedgwick Mr Turnbull Mr Culpin Mr S J Davies Mr Pickford Mr R I G Allen Mrs R J Butler Ms C Evans Ms Simpson Mr Hudson Mr Franklin Mrs Todd Ms Chapman Mr Cropper Mr Tyrie

Mr Call

Mr Calder - IR Mr R P H Allen - C&E

PSBR FIGURES IN THE BUDGET

The Chancellor has decided to publish the following PSBR figures in the FSBR:

	1987-88	1988-89
£ billion	- 3.1	- 3.2
% of money GDP	34	34

They will appear in tables 6.1, 6.3 and 6.7 exactly as above ie. rounded to the nearest £0.1 billion. Following the precedent of last year in which PSBRs of £4.1 billion and £3.9 billion were described as "about £4 billion", this year's figures will be described in the text of chapter 6 as net repayments of "about £3 billion". In table 3.12 they will be rounded to the nearest f_2 billion ie. - £3 billion in both years. In table 2.6, which rounds to the nearest £1 billion, they will also be shown as -£3 billion.

-Coli Moul

COLIN MOWL



COPY NO 7 OF 18

FROM: A C S ALLAN DATE: 10 March 1988

MR SEDGWICK

cc PS/Chief Secretary Sir P Middleton Sir T Burns Mr Anson Mr Scholar Mr Culpin Mr Odling-Smee Mr Turnbull Mr S J Davies Mr Hibberd Mr Mowl Ms C Evans Mr Franklin Mr Ritchie Mrs Todd

THE PSBR IN 1987-88 AND 1988-89: FINAL FIGURES FOR THE FSBR

The Chancellor was grateful for your minute of 9 March. He wishes to publish PSBRs of £-3.1 billion for 1987-88 and £-3.2 billion for 1988-89.

ACSA

A C S ALLAN

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COPY NO 200F 20

FROM: A C S ALLAN DATE: 10 March 1988

S J DAVIES

PS/Chief Secretary CC PS/Financial Secretary PS/Economic Secretary Sir P Middleton Sir T Burns Sir G Littler Mr Anson Mr Scholar Mr Odling-Smee Mr Peretz Mr Sedgwick Mr Turnbull Mr R I G Allen Mr Pickford Miss C Evans Miss Simpson Mr Cropper

FSBR: CHAPTER 2

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The Chancellor was grateful for your minute of 9 March. He had the following comments on the text etc:

- (i) He wants to reflect further on the wording of the very end of paragraph 2.03 (which currently reads "with inflation at around 4 per cent"); I shall let you know during the course of the afternoon if he wishes to change this.
- (ii) He notes that the Q4 figures for money GDP and output need to be added to chart 2.1.
- (iii) The attached redraft of paragraphs 2.09 to 2.11 should be used.
 - (iv) The layout of page 9 is ugly. He would prefer chart 2.2 to be shrunk a little.



- (v) He prefers the years to be labelled as in chart 2.4, but with the spaces in, eg, "79-80" closed up. This format should be used for chart 2.5.
- (vi) The heading to chart 2.5 should be "Public Sector Borrowing Requirement" only, and not "and privatisation proceeds".
- (vii) In paragraph 2.16, the figure for the PSBR for 1988-89 should be type-set with a minus sign not a dash.
- (viii) In paragraph 2A.5, the last sentence should read "...oil revenues in 1988-89 are now forecast to be lower than projected a year ago". (ie omitting "somewhat").

Mpw PP. ACSALLAN psl/l6A

MONETARY POLICY

2.09 Interest rate decisions are based on a continuous and comprehensive assessment of monetary conditions so as to ensure downward pressure on inflation.

2.10 Industry has benefitted from the greater stability of exchange rates over the past year, and the Government will continue to pursue a policy of exchange rate stability, with the rate against the Deutschmark being of particular importance. This provides an important financial discipline, which both ensures that increases in domestic costs will not be accommodated by a lower exchange rate, and at the same time unpins the declining path of money GDP growth and inflation.

2.10 Achieving these objectives requires a reduction in monetary growth over the medium-term ...

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FROM: A C S ALLAN DATE: 10 March 1988

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COPY NO 14 OF 15

Sir P Middleton CC Sir T Burns Mr Odling-Smee Mr Peretz Mr Sedgwick Mr R I G Allen Mr Pickford Miss Simpson Mr Hudson Mr Allum Miss C Evans

CHAPTER 3 OF THE FSBR: THE INDUSTRY ACT FORECAST

The Chancellor was grateful for your minute of 9 March. He was content with the various points in your cover note, except that he wishes paragraph 3.08 to begin "Sterling has shown considerable stability against the Deutschmark over the past year".

On further reflection, and after seeing the briefing on the 2. Q4 balance of payments figures, he now wishes to show a current account deficit of £4 billion in 1988, based on a smaller This will mean consequential invisibles surplus, of $\pounds 8\frac{1}{2}$ billion. amendments to paragraphs 3.07 and 3.30 and to Tables 3.4 and 3.12. The deficit should be described as "less than 1 per cent of GDP".

I attach a copy of the pages on which he had drafting 3. comments.



A C S ALLAN





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BUDGET	SECRET
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3 The economy; recenter NOT TO BE COPIED developments and prospects to mid-1989

Summary

3.01 Growth should be around 3 per cent in 1988, close to the average rate over the last six years, but significantly below the $4\frac{1}{4}$ per cent growth in 1987. Inflation is expected to remain low and there are good prospects for a further fall in unemployment.

Assumptions

3.07 The forecast assumes that fiscal and monetary policies are operated within the framework of the Medium Term Financial Strategy. It assumes that North Sea oil prices and sterling remain close to recent levels.

Demand and activity

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3.02 The economy grew strongly in 1987, with GDP growth of $4\frac{1}{4}$ per cent and manufacturing output growth of $5\frac{1}{2}$ per cent. Domestic demand grew 0.2by just under 4 per cent, the same as in 1986. It is expected to grow at a similar rate in 1988, with slightly slower growth of consumer spending being offset by markedly faster growth of investment. GDP is forecast to grow by 3 per cent ($3\frac{1}{2}$ per cent for non-oil GDP).

Inflation

3.03 RPI inflation averaged just over 4 per cent in 1987. It fell to 3¹/₄ per cent in January 1988, but is forecast to return to 4 per cent in the fourth quarter of 1988.

Labour market

3.04 Employment has risen strongly over the past year, with unemployment falling by half a million—the largest decline since the war. Unemployment should continue to fall this year.

World economy 3.05 GNP in the main industrial economies grew by about 3 per cent last year. Some slackening in growth is likely in 1988 particularly in the United States, and growth in the main industrialised countries in aggregate could ease slightly to $2\frac{1}{2}$ per cent. Industrial production picked up strongly during 1987. Associated with this were faster growth in trade in manufactures and some recovery in industrial materials prices. World trade in manufactures appears to have grown by about $5\frac{1}{2}$ per cent in 1987 and should grow by a similar amount this year.

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UK trade and current account RETA O NOT TO BE COPIE

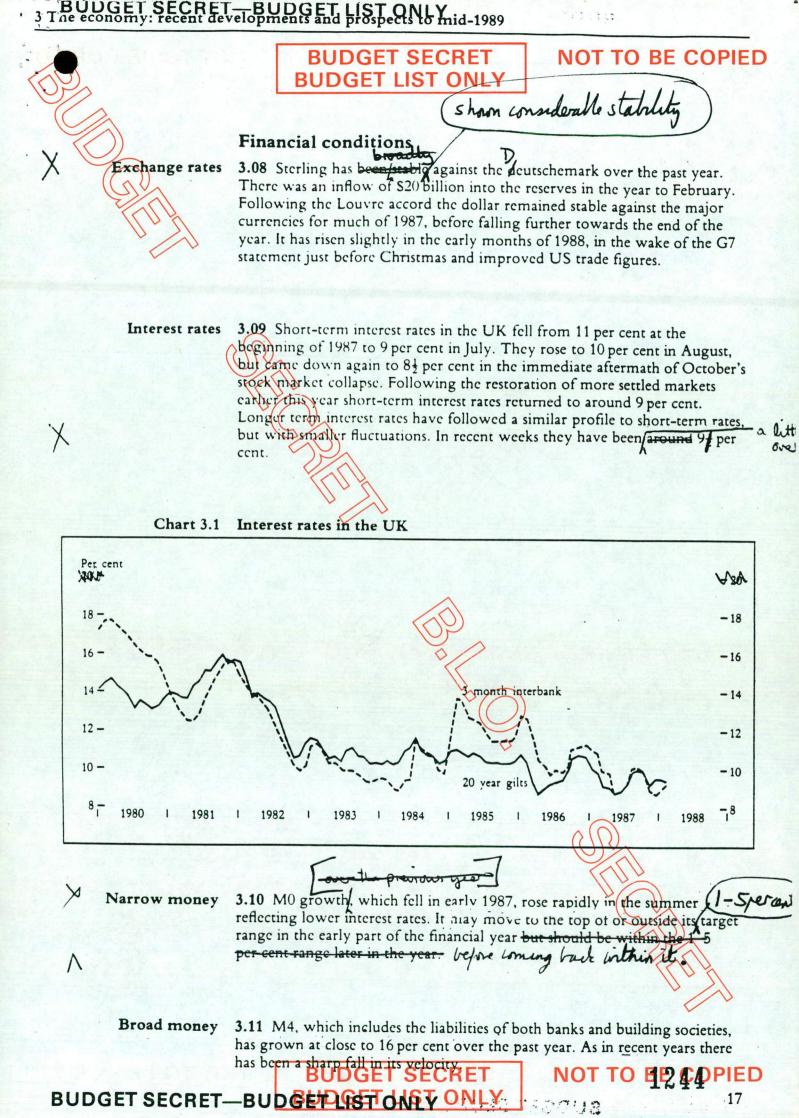
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be helped by stronger commodity prices, and hence export earnings. Total world trade in 1988 is forecast to continue to grow at close to the rate experienced in 1987.

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UK trade and the balance of payments

Relative costs and prices

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3.22 UR sinit labour costs in manufacturing rose only slightly in 1987, at a similar rate to the average in the other major economies, with rapid productivity growth largely offsetting a continuing high level of pay increases. Despite some appreciation of sterling against the dellar the UK's cost competitiveness remains clearly more favourable than in 1984 and 1985 before the fall in world oil prices. The maintenance of competitiveness in the scar ahead will depend on success in continuing to restrain unit cost increases

Table 3.2

the

The exchange rate and cost competitiveness

S-O	Sterling index (1975 = 100)	Relative unit labour costs ¹ (1980 = 100) (Centre over
1985 Q4	80	88
1986 Q4	68	71
1987 Q4	75	80

Ratio of UK manufacturing sector's costs to those overseas.

Trade volumes (goods 3.23 Non-oil export volumes rose by 7 per cent in 1987. Manufactured other than oil) exports rose particularly strongly, reflecting renewed growth in world trade and the UK's strong competitive position. Non-oil export volumes are forecast to rise in 1988 by a further 5 per cent.

(CurA 3.5)

3.24 The UK increased its share of world trade in manufactures slightly in 1987. Its volume share has remained broadly stable since 1981, in marked contrast to the previous long-term decline. This improved performance is forecast to continue in 1988.

Table 3.3 Visible trade

	Per cent c	Per cent changes on previous year					
	All goods				oil		
	Export volume	Import volume	Terms of trade ¹	Export volume	Import Volume	Terms of trade ¹	
1986	3 1	61	-5	4	0	-1	
1987	5 1	71	1	7	87	2	
1988 Forecast	31/2	$6\frac{1}{2}$	1/2	5	61	1	
10		A CONTRACT OF MALE					

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Ratio of UK export average values to import average values.

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3.25 Non-oil import volumes fell unexpectedly in early 1987, but rose during the rest of the year, and were 82 per cent higher than in 1986. The increases were widespread, with higher imports of materials and capital goods reflecting the strong growth of UK production, stocks and investment. Consumer goods imports also rose in response to the rise in consumer spending. The volume of imports is forecast to rise less rapidly through the year ahead as output growth slows.

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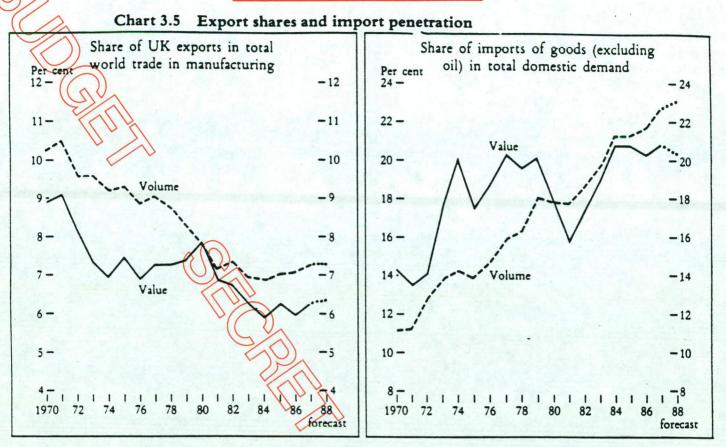
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Oil trade 3.26 There was a surplus in oil trade of $\pounds 4$ billion in 1987, little changed from 1986. Higher oil prices and a fall in domestic demand for oil more than offset a decline in North Sea production. In 1988 oil production is likely to be below its 1987 level and close to the centre of the Department of Energy's projected output range while domestic demand for oil may rise modestly. The oil trade surplus is expected to fall by $\pounds 1\frac{1}{2}$ billion, to about $\pounds 2\frac{1}{2}$ billion.

Trade prices and the
terms of trade3.27 The terms of trade, which fell in 1986 as oil prices declined, improved
again in 1987 as oil prices firmed and as sterling's appreciation offset some
rise in world commodity prices in the latter part of the year. Little further
change in the terms of trade is assumed during the rest of 1988.

Invisibles and overseas assets 3.28 The latest estimate for the surplus on invisibles in 1987, at £8 billion, is slightly below the outturn in 1986, with increased transfers to the European Community only partly offset by higher net earnings from services and from the UK's net overseas assets. The invisible surplus seems likely to rise in 1988 partly because of lower net payments abroad by North Sea oil companies.

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3.29 The value of the UK's stock of net overseas assets is estimated provisionally to have been about \pounds 90 billion at the end of 1987, some \pounds 20 billion down on end-1986. This decline is largely due to the fall in world equity markets and in the sterling value of UK assets in North America following the fall in the US dollar.

Current account



3.30 The current account deficit is estimated to have been $\pounds 1 \pounds$ billion in 1987, the improvement over the forecast in last year's FSBR being due to the unexpected strength of exports of manufactures. A deficit of $\pounds 2$ billion (per cent of GDP) is forecast for 1988, largely as a result of the projected decline in the oil surplus. The deficit on non-oil trade is forecast to show little further change from the level in the second half of 1987.

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Table 3.4 Current account

Manufactures				
Manufactures	Oil	Other goods	Invisibles	Current balance
$-5\frac{1}{2}$	4	-7	81	0
$-6\frac{1}{2}$	4	$-7\frac{1}{2}$	8	· -1+
$-8\frac{1}{2}$	21	$-6\frac{1}{2}$	181/2	-26
	$-6\frac{1}{2}$	$-6\frac{1}{2}$ 4	$ \begin{array}{cccccccccccccccccccccccccccccccccccc$	$\begin{array}{cccccccccccccccccccccccccccccccccccc$

Demand and activity

3.31 The UK economy grew by 4¼ per cent in 1987. Growth was strong throughout the economy manufacturing output rose by 5½ per cent, construction output by 8 per cent and output of the service industries by 5½ per cent.

Personal sector expenditure

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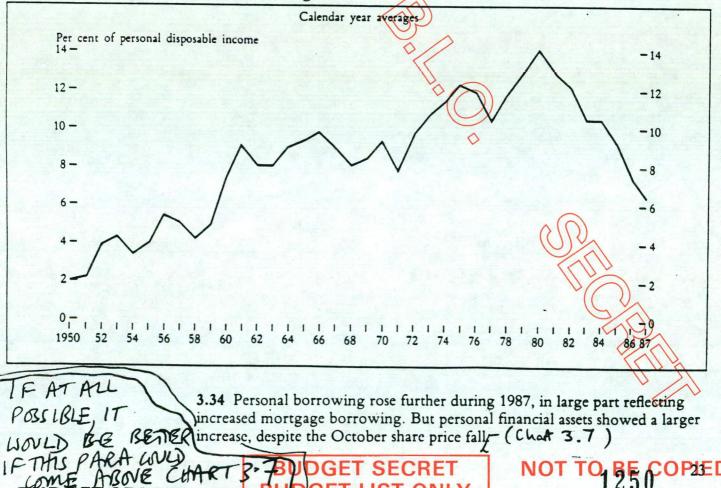
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3.32 Consumers' expenditure is now estimated to have risen by 5 per cent in 1987, slightly less than in 1986. The growth in consumer spending was faster than the 31 per cent growth in real personal disposable income, and the savings ratio once again fell.

3.33 A number of factors could account for the decline in the savings ratio in recent years. Inflation has been at a low level not experienced since the 1960s. Recent increases in real house prices and in equity prices up to October 1987 may also have contributed. Finally employers have taken socalled "holidays" on their contributions to employees' pension funds; which these score as reduced personal saving.

Chart 3.6 Personal savings ratio

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3.37 Current estimates suggest that manufacturing investment grew by 6 3½ per cent last year, while total non-oil business investment grew by 7 per cent. The latest DTI Investment Intentions Survey suggested a strong pick-C in manufacturing investment growth, to about 11 per cent in 1988. The January CBI Industrial Trends Survey, the first full enquiry since the fall in share prices, confirms that prospect, with a near record balance of manufacturing firms expecting to increase investment. On the basis of the DTI Survey, further steady growth, of about 6 per cent, is expected in nonmanufacturing business investment. This outlook for company investment is consistent with the recent and prospective buoyancy in output, real profitability, and company finances, and it will add to industrial capacity. North Sea investment fell by about ∠½ billion in 1987 and is expected to show little change in 1988.

Table 3.5 Gross fixed domestic capital formation

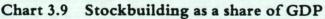
	L billion at	Per cent changes	on previous year	
	1980 prices	1986	1987	Forecast 1988
Business ¹	29.8	-3	41	8 1
of which (i) non-oil business (ii) manufacturing	27·8 7·1	$-2 -5\frac{1}{2}$	6 1 31	$\frac{8\frac{1}{2}}{11\frac{1}{2}}$
Private dwellings ²	9.6	64	\$61/2	2
General government	7.0	51	$-\frac{2}{12}$	Í
Total fixed investment	46.4	0	3 1	6

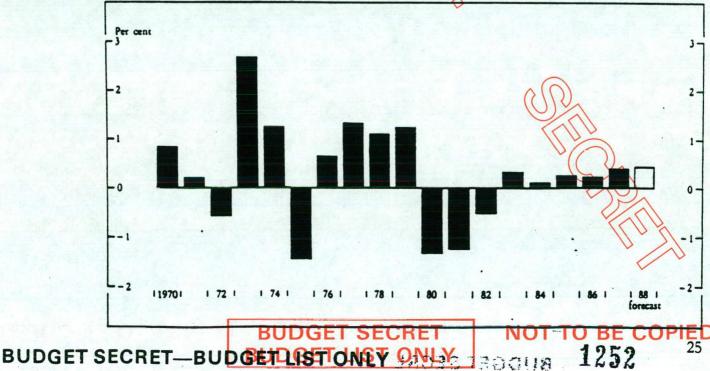
¹Includes investment by public corporations.

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²Includes purchase less sales of land by persons, companies and public corporations, other than purchases of council houses.

3.38 Despite a rise in stocks in 1987 stock-output and stock-sales ratios continued their trend decline of the last eight years. These downward trends are expected to continue in 1988, though, as last year, there is still likely to be modest stockbuilding.





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and activity

3.39 GDP growth is likely to moderate to around 3 per cent (3½ per cent excluding oil) in 1988, close to the average rate tince 1991. Domestic demand is forecast to rise at around the same rate in 1988 as in 1987; some slowdown in consumer spending should be offset by buoyant investment. But declining North Sea output (and lower oil exports) may reduce GDP growth by ½ m per cent, rather more than in 1987. Manufacturing output is expected to rise faster than non-oil GDP in 1988, as it did in 1987.

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Table 3.6

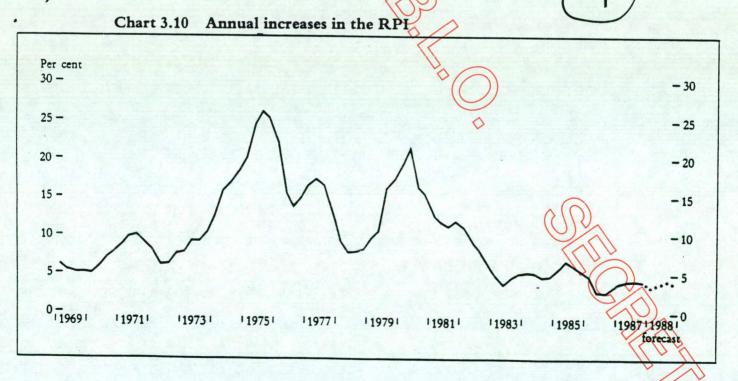
e 3.6 Domestic demand and GDP

	Per cent cha	anges on a ye	ar earlier
	1987	Forecasts	i
~		1988	1989 H1
Domestic demand	4	4	21
Exports of goods and services1	$5\frac{1}{2}(6\frac{1}{2})$	3 (4)	21 (5) 31/2
Imports of goods and services1	$7\frac{1}{2}(8\frac{1}{2})$	6(6)	51 45 (44)51
GDP ¹ ²	$4\frac{1}{4}(4\frac{3}{4})$	$3(3\frac{1}{2})$	$2\frac{1}{2} (4)^{3 \frac{1}{2}}$ $5\frac{1}{2} (4)^{5 \frac{1}{2}}$ $2\frac{1}{2} (3)$
Manufacturing production	51	5	21
Non-oil shown in brackets.			And the second

² Average measure

Inflation

3.40 The annual rate of inflation as measured by the RPI was 4.1 per cent in 1987Q4, in line with the forecasts in the 1987 FSBR and Autumn Statement. The average rate for 1987 as a whole was 4.2 per cent. Last year was the first time in 23 years that inflation was lower than the growth SDP, which is now estimated at 4.3 per cent.



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3.41 Pay settlements in manufacturing industry recorded by the CBI show a fall of about 1 percentage point between the 1985-86 and 1986-87 pay rounds. There was a similar picture in the services sector. Average earnings,

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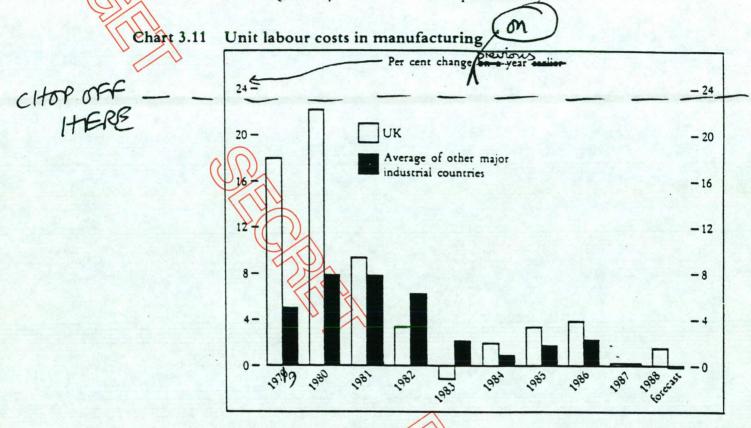
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boosted by record overtime working in manufacturing, rose by 8 per cent. But unit labour costs in manufacturing were broadly unchanged in 1987, reflecting a sharp increase in labour productivity.



Prospects

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3.42 It is difficult to discern a reliable trend in recent private sector pay settlements. They have been markedly lower than the recent high growth in earnings, which reflects record overtime working and bonus payments. Recent data suggest that settlements may turn out a little higher in 1988 than in 1987, but overtime working (and overtime earnings) should fall as economic growth moves back closer to trend.

3.43 In 1987 rapid growth in productivity meant that manufacturing unit labour costs rose only fractionally, in line with other major industrial countries. Continued growth in underlying productivity should mean that manufacturing unit labour costs grow only slowly in 1988, though in other major industrialised countries no unit labour cost growth at all is forecast.

	Table 3.7	Costs in manufa	acturing	V(O)		
×		Per cent changes on previous year				
	Unit labour costs	Cost of materials and fuel ¹	Estimated total unit costs ²	Output prices ¹		
1986		4	-11	- +	4	
1987		\$V2	5	11	41/2	
1988 Forecast		2	×-21/2	1/	41/2	

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3.44 Manufacturers' profit margins rose significantly in 1987 for the third year in succession. There may be further increases in 1988 if producers take some advantage of falling import costs to raise profits, as they did in 1986. Over the longer term, high profitability should lead to continued growth in investment, capacity and productivity. Together these should enhance prospects for controlling industrial costs.

3.45 Inflation has come down during the first quarter of 1988, aided by lower import costs and recent cuts in mortgage interest rates. It may edge up a little, partly as a result of the Budget proposals and the effects of local authority rate increases. There will also be some real increases in nationalised industry prices following a decline in real terms over the past three years. The RPI is forecast to rise by 4 per cent in the year to the fourth quarter of 1988. With substantial cuts in income tax, the tax and price index (TPI) is likely to rise more slowly than the RPI during 1988. By the fourth quarter of 1980 it is likely to be 13/1 per cent higher than a year earlier.

Table 3.8 Retail prices index

		Per cent changes on	n a year earlier	
	Weight in 1987		Forecasts	
		1987 Q4	1988 Q4	1989 Q2
Food	16 1	34	2	\$ 21/2
Nationalised industries	6 .	21	61	
Housing	15	7	63/4	5 1 2481/4
Other	$62\frac{1}{2}$	31 0	$3\frac{1}{2}$	31
Total	100	4	4	4

3.46 The GDP deflator measures the price of domestic value added principally unit labour costs and profits per unit of output. It does not include import prices. The GDP deflator at market prices is estimated to have risen by 5 per cent in 1987–88 (a little faster than expected in the Autumn Statement), following an increase of $3\frac{1}{2}$ per cent in 1986–87. The higher rate of increase in 1987–88 is accounted for by a recovery in North Sea profits, which had fallen by over 50 per cent in 1986–87 following the sharp fall in oil prices. The GDP deflator is new forecast to rise by $4\frac{1}{2}$ per cent in 1988–89.

Productivity and the labour market

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3.47 Preliminary estimates suggest that the employed labour force in Great Britain rose sharply during 1987; in the year to September 1987 it is estimated to have risen by 453,000. Self-employment has grown particularly strongly, as many more people have taken advantage of the opportunities offered by the buoyant economic climate. Total employment has now risen by over $1\frac{1}{2}$ million since March 1983.

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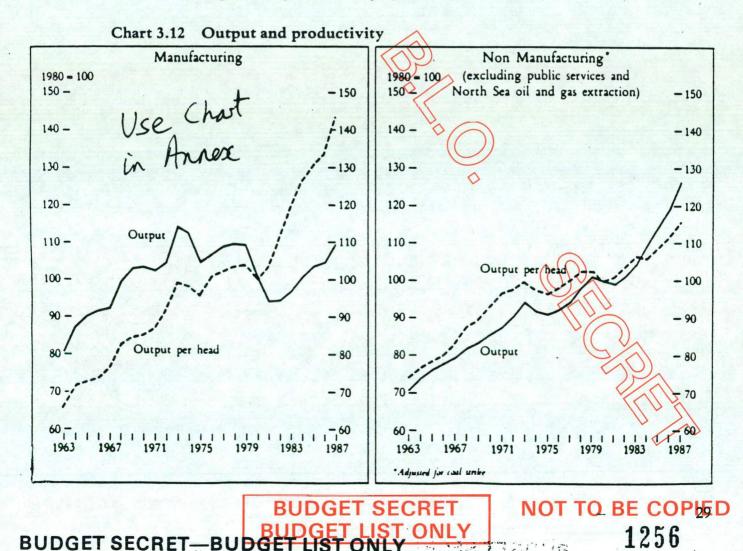
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X Table 3.9	Changes -	BUDGET S BUDGET LIS		ΝΟΤ ΤΟ) BE COPIEI
	Thousands,	change in GB Geaso	onally adjusted		
R	Employees in employment		Self- employed	HM Forces	Employed labour force
	Male	Female			
September 1984 to September 1985	+ 55	+ 200	+ 90	-3	+ 343
September 1985 to September 1986	- 82	+ 150	+ 71	-3	+136
September 1986 to September 1987	+ 25	+ 225	+ 2071	-4	+ 453

¹ Figures for self-employment after June 1987 are projections based on self-employment growth over the previous six years.

3.48 Productivity has also been growing strongly. In 1987 manufacturing productivity rose by almost 7 per cent. In the year to 1987Q3 (the latest period for which comparable data are available) UK manufacturing productivity rose faster than in any other major industrial country. It has now risch by an average of 4 per cent per annum since 1979. Underlying growth in labour productivity in manufacturing industry may now be higher than in the 1960s. This has been accompanied recently by a substantial improvement in capital productivity. Non-manufacturing output per hour has risen by about 2 per cent a year since 1979, and by about 2¹/₂ per cent a year since 1983. Output per head has grown less than this, as a result of the large rise in part-time employment.



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Table 3.1	0 Output	per head of t	he employed	labour force	/	
$\langle \rangle$	Per cent ch	anges			1	Por san
	Annual ave	nual averages		1984 Q4 ³	1985 Q4	1986 Q4
	1964-73	1973-79	1979-87	to 1985 Q4	to 1986 Q4	to 1987 Q4 ²
Manufacturing	37	1	4	24	61	61
Non-manufacturing ¹	3	1	11	34 3/4	31	37
Whole economy	21	11	2	23/4	31	31
Non-North Sea economy	23	· 1	2	241	37	31

¹Excludes public services and North Sea oil and gas extraction.

²Partly forecast.

3 Figures for 1984 Q4 are adjusted for the extruded effect of the coal strike

Unemployment 3.49 Seasonally adjusted adult unemployment in the UK has fallen in each of the last eighteen months. It has now come down by almost 650,000 since July 1986. Over the same period long term unemployment (over one year's duration) has fallen by around 250,000. The improved trend in unemployment has been mainly the result of strong growth of output and employment. Unemployment should continue to fall in the year ahead. But excessive pay settlements could threaten further progress.

Forecast and outturn

3.50 Table 3.11 compares the main elements of the forecast published in the 1987 FSBR with the outturn or latest estimate.

(D)	1987 ESBD	or Katest	Average
	FSBR forecast	estimate/	errors from past forecasts
Total gross domestic product (per cent change between 1986 and 1987)	3	41	3
RPI/per cent increase between the fourth quarters of 1986 and 1987)		4	14
Money GDP (per cent change between 1986–87 and 1987–88)	✓ 7½	9 1	1+
Current account of the balance of payments in (1987, £ billion)	$-2\frac{1}{2}$	-1+	3
PSBR, financial-year (1987-88, £ billion)	4	11-3	\$4

3.51 Inflation in the fourth quarter of 1987 was in line with the forecast made a year ago while the current account deficit is now estimated to have been rather smaller than forecast. Although the data on which the latest estimates of GDP in 1987 are based are still very uncertain, it is clear that both money and real GDP growth have been stronger than forecast. The PSBR in 1987–88 is likely to turn out about $\mathcal{L}[7]$ billion lower than last year's forecast. This error—which is slightly higher than average errors on past forecasts—reflects a combination of lower than expected general government expenditure and, in particular, higher than forecast tax revenues. This is discussed in more detail in Chapter 6.

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3.52 This year's forecast is summarised in Table 3.12.

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BUDGET SECRET BUDGET LIST ONLY 3 The economy: recent developments and prospects to mid-1989

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Table 3.12 The prospects: summary

	Forecast		Average errors	
	1986 to 1987	1987 to 1988	from past forecasts ¹	
<u>In</u>	per cent changes		percentage points	
Output and expenditure at constant 1980 prices				
Domestic demand	4	4	1	
of which:			Y Death	
consumers' expenditure general government consumption	5 0	211/2	1	
fixed investment	31	6	21	
change in stockbuilding (as per cent of				
level of GDP)	Xo	0	12	
Exports of goods and services	5 1	3 6 1/2	17	
Imports of goods and services Gross domestic product: total	41	3	24	
manufacturing	20 51 71 41 51 51	5	$1\frac{1}{4}$ $2\frac{1}{4}$ $\frac{3}{4}$ $1\frac{1}{2}$	
Inflation				
Retail prices index	per cent changes			
1987 Q4 to 1988 Q4	4	- Partie - Strandsong	11	
1988 Q2 to 1989 Q2	4		11 11 11	
Deflator for GDP at market prices	per cent changes of	per cent changes on a year earlier		
Financial year 1987–88	5		1 3 1 3	
Financial year 1988–89	4	12	14	
Money GDP at market prices	L billion ²			
Financial year 1987–88		(93)	1	
Financial year 1988-89	457	$(7\frac{1}{2})$	11/2	
Balance of payments on current account	£ billion			
1988		-4	$3\frac{1}{2}$ $4\frac{1}{2}$	
1989 first half (at an annual rate)		2-4	$4\frac{1}{2}$	
PSBR	\mathcal{L} billion ³			
Financial year 1987–88		3	1 (1%)	
Financial year 1988–89	-3		4 \$ (12%)	

figure) between forecast and outturn over the last ten years.

² Per cent change on previous financial fear in brackets; average error shown relates to the forecast of the percentage change. ³ Per cent of GDP at market prices shown in brackets.

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CONFIDENTIAL



FROM: A C S ALLAN DATE: 10 March 1988

MR ODLING-SMEE

cc PS/Chief Secretary PS/Financial Secretary PS/Paymaster General PS/Economic Secretary Sir P Middleton Sir T Burns Mr Scholar Mr Sedgwick Mr R I G Allen Mr S Davies Mr Hibberd Mr Mowl Mr Pickford Miss C Evans Mr Cropper Mr Tyrie Mr Call

FSBR: TABLE 3.12

The Chancellor was grateful for your minute of 9 March with the alternative version of Table 3.12. He was not entirely happy with how that came out, and at this stage would prefer to stick to last year's format.

A C S ALLAN

psl/21A



COPY NO. 17 OF 18.

FROM: A C S ALLAN DATE: 10 March 1988

cc PS/Financial Secretary Sir P Middleton Sir T Burns Mr Scholar Mr Culpin Mr Odling-Smee Mr R I G Allen Mr Pickford Mr Riley Miss Simpson Miss C Evans Mr Hudson PS/IR MR P R H Allen - C&E

FSBR: CHAPTER 4

MISS SINCLAIR

The Chancellor was most grateful for your minute of 9 March, and agrees with the points in your covering note. I attach a copy of the pages on which he had comments.

2. He had a few separate comments on the redrafted paragraphs on CGT (paragraphs 30-32 in the Annex)

- (i) Do the costings in paragraph 31 assume annual indexation of the exempt amount? They should.
- (ii) It looks odd to give figures for 1990-91 and 1991-92 for the measures in paragraphs 31 and 32, but not for the measure in paragraph 30. Do we need these figures at all?
- (iii) He feels it is absurd to include the sentence "Estimates of cost take account of the likely effect of this measure on the volume and timing of disposals." <u>three</u> times especially in the context of the reduction in the exempt slice. He feels it should be included just once; to govern the entire CGT package.

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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 main income tax personal allowances and the limit of the basic rate band 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 Desember 1987). This will mean that:

the single person's and wife's carned income allowances will rise by $\pounds 180$ from $\pounds 2423$ to $\pounds 2605$;

the married allow ance will rise by £300 from £3795 to £4095;

the additional personal allowance and widow's bereavement allowance will rise by $\pounds 120$ from $\pounds 1$ 370 to $\pounds 1$ 490;

the age allowance for those aged 65 to 79 will rise by £220 from £2960 to £3180 (single) and by £360 from £4675 to £5035 (married);

the age allowance for those aged 80 and over will rise by £240 from $\pounds 3\,070$ to £3310 (single) and by £360 from £4845 to £5205 (married);

the income limit for age allowance will rise by $\pounds 800$ from $\pounds 9800$ to $\pounds 10600$.

4.03 The dependent relative allowance, of up to £145 the housekeeper allowance of £100 and the allowance for the services of a son or daughter of will be abolished.

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

ATTS the basic rate limit will rise from £17 900 to £19 300 of taxable income.

4.06 The basic rate of income tax will be reduced to 23 perdent.

4.07 There will be a single higher rate of income tax of there cent.

LIST ONLY

Life assurance premium relief 4.08 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 1982

Benefits in kind 4.09 Car benefit scale charges for 1988-89 will be set at twice their 1987-88 levels.

Mortgage interest relief 4.10 For loans taken out from 1 August 1988, tax relief will be limited to the interest on £30000 per residence, regardless of the number of borrowers. Relief on new loans for home improvements will be abolished from 6 April 1988. So will relief on new loans for the purchase of residences for dependent regionage for second pous NOT TO BE COP

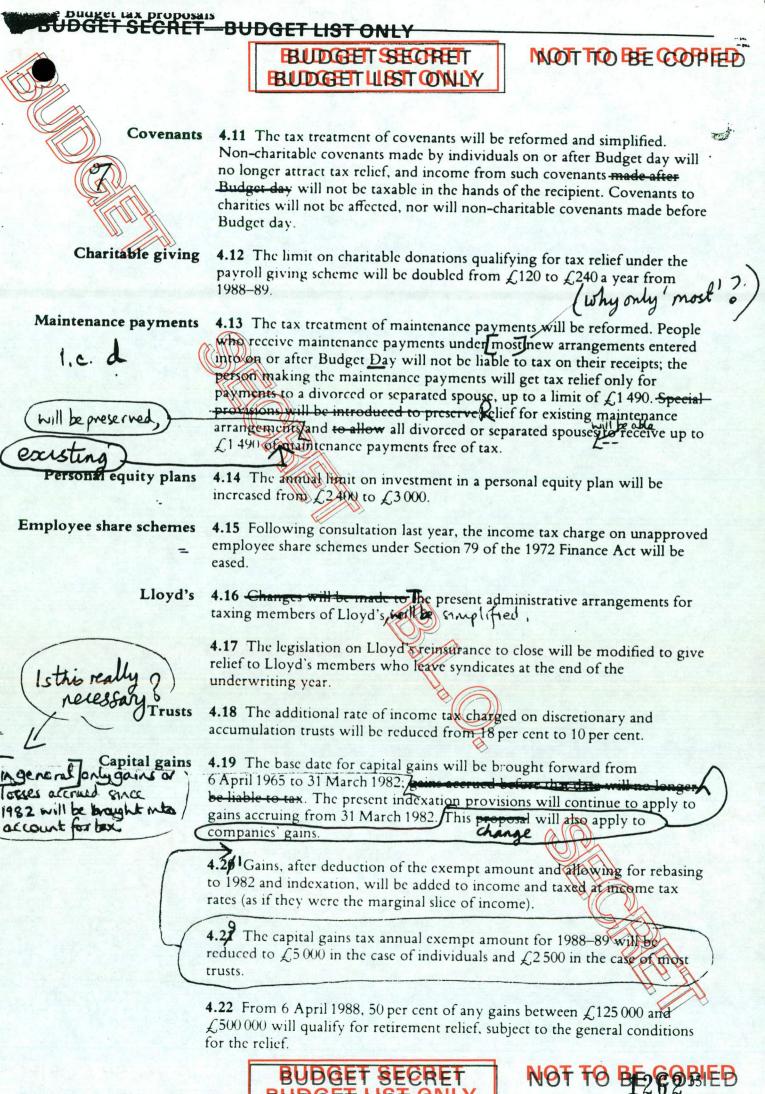
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Inheritance tax I.C

4.23 From Budget Day the threshold for inheritance tax will be increased from $\pounds 90\,000$ to $\pounds 110\,000$. Chargeable transfers above this amount will be taxed at a flat 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.

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Business tax

4.24 The small companies' rate of corporation tax will be reduced to 25 per cent for the financial year 1988.

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4.25 The rate of advance corporation tax (ACT) for 1988-89 will go down automatically to 1/3rd as a consequence of the reduction in the basic rate of income tax.

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

4.27 In common with other business entertainment, the cost of entertaining overseas feustomers will no longer be an allowable business expense for tax purposes. This change will take effect from Budget Day, except for commitments calered into before that date. From 1 August 1988 the VAT paid by businesses on this entertainment will no longer be deductible.

4.28 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

letting ships o

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4.29 Investment in private rented housing will be encouraged by extending the Business Expansion Scheme to give relief on investment in companies providing rented housing under the new assured tenancy scheme.

4.30 A general limit of £500 000 will be set on relief under the Business Expansion Scheme for total investment in any one company in any period of twelve months, with a higher limit of £5 million for investment in qualifying companies providing private rented housing or chip chartering.

Forestry

4.31 Income from the occupation of commercial woodlands will be removed from the scope of Income Tax and Corporation Tax.

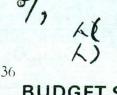
Oil taxation 4.32 The oil allowance for Petroleum Revenue Tax (PRT) will be reduced to 100 000 tonnes per chargeable period for all Southern Basin and onshore fields given development consent on or after 1 April 1982. (At the same time the Secretary of State for Energy proposes to abolish royalty payments for these fields.)

> 4.33 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. aunea

Company residence and

4.34 Section 482(1) (a) and (b) of the Taxes Act will be repealed with effect from Budget day. In future companies will be resident for tax purposes in the United Kingdom if incorporated here or centrally managed and controlled here. Mincorporated companies wishing to move their busis abroad, or non-UK incorporated companies moving their residence abroad may do so without consent if they pay the tax due including tax on capital gains).

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Stamp duties



4.35 Capital duty and unit trust instrument duty will be abolished with effect from/Budget day

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4.36 From 16 March 1988 the registration limits will become $\pounds 22100$ per annum and $\pounds 7500$ per quarter.

4.37 The provision for applying VAT to confectionery will be amended with the main effect of taxing all cereal bars at the standard rate.

Excise duties

4.38 The duties on beer and wines will rise by the equivalent of 1p on a typical pint of beer, just under 4p on a bottle of table wine, and just over 6p on a bottle of sherry (all inclusive of VAT). The duty on spirits 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

4.39 The duty on leaded petrol will be increased by the equivalent of yp gallon (inclusive of VAT). The duty on unleaded petrol will remain unchanged. The duty on derv will rise by the equivalent of just under 5p a gallon (inclusive of VAT).

4.40 The specific duries on cigarettes, hand-rolling tobacco and cigars will rise by the equivalent of just over 3p on a packet of 20 cigarettes and nearly 2p on a packet of 5 small cigars (inclusive of VAT). The duty on pipe tobacco will remain unchanged.

Tax administration

4.41 The VAT civil penalty system, introduced in 1985, has been reviewed and various easements are proposed.

4.42 In the light of recommendations by the Keith Committee, changes will be made:

to encourage people to notify the Inland Revenue if they are liable to tax;

to improve the information powers of the Inland Revenue;

to charge interest where payment to the Inland Revenue of income tax deducted by employers is delayed beyond the end of the tax year.

Independent taxation

4.43 A new system of taxation for married couples will be introduced in 1990. The details are set out in the box on the next page.



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1	Table 4.1 Direct effects of changes in taxation				
	C		£ million		1
		(A)	Estimated effect 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
		INLAND REVENUE			
		Income tax			
	1	Increase in single allowance of £180 and married allowance of £300 Increase in additional personal aflowance and widow's bereavement	-1245	-625	-810
	3	allowance of f120 Increase in age allowance of f220 (single) and f360 (married)	-15	-5	-10
	4	for those aged 65 to 79 Increase in age allowance of £240 (single) and £360 (married) for those aged 80 and over	-90	-45	-55
	5	Increase in income limit for age allowage of 1800	-15	-10	-10
78	X	Abolition of minor personal allowances	-10	-5	-10
8	X	Restriction on additional personal allowance for unmarried couples	+10	+10	+10
2	X	Increase in basic rate limit of £1,400 to £19,300	-155	- 75	+ 5
-0	9	Reduction of 2p in basic rate	-2190	-75 -2190	-125
	10	Abolition of higher rates of income tax above 40p	-1025	-2170	-3000 -2070
	11	Reduction in relief on life assurance premiums	-	-700	+ 70
	12	Fringe benefits - car benefit scales	+260	+260	+ 310
	13	Fringe benefits - car parking space	-5	-5	-5
	14	Mortgage interest relief ceiling applied to residence	÷	*	+ 25
	15	Abolition of tax relief on new home improvement loans	+ 80	+ 80	+ 200
	16	Abolition of tax relief on new loans for homes for dependent reactives	X		1.200
		and divorced or separated spouses	*		¥
	17	Abolition of tax relief on new non-charitable covenants	+ 45	+ 45	+105
	18	Pavroll giving to charities - increase in donation limit to £240 a	+	+	+
	17	Lhange in rules for maintenance payments	-10	-10	-5
		Change in additional rate on discretionary trusts	-	-5	-10
-	21	Llovd's - reform of administrative arrangements	A .	- 100 and - 1	×
		Lloyd's reinsurance to close - relief for leavers	÷	* · · · · · · · · · · · · · · · · · · ·	*
	20	Unapproved employee share schemes - relaxation of charge	÷	÷.	÷
		Employee priority in public offer of shares	*.	+	¥
	24	Approved FA 1984 employee share option schemes - restricted shares	*	÷	ŧ
		Assessing procedure for Schedule 2	~	- A	-
		Reductancy payments - change to scale of charge	()	+	•
		Withorawai of "top-slicing" relief for tax charged on premiums for leases, etc	here here here here here here here here		
		Amenament to tax treatment of overseas interest and	ŧ	FULL *	÷
		numentament it tax treatment of tverses interest and otterities	*		*
		Capital pains tax		15A	
	30	Rebasing capital gains of individuals and trusts to March 1982			2
٨	31	Actual exempt amount reduced to #5000			-55
N		Charoing gains of individuals and trusts at income tax rates		J.	4 5 +15
	3.3	Retirement reijef	+70	+70	+55
		Building and Co-operative society spares	4	*	○-10
		Homes provided for dependent relatives	ż	÷.	¥ ·
					*

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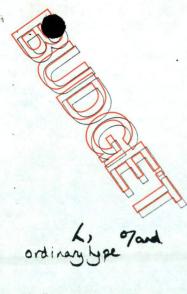


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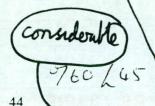


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Income tak and capital λ , gains tax

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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 \pounds 1 490 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 tax liability on the recipient will be limited to the amount taxable in 1988–89; and a divorced or separated spouse will be exempt from tax on an amount up to the difference between the single and married allowances.

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The changes are estimated to yield £5 million in 1990-91 and £15 million in 1991-92, and £35 million eventually.

20 The additional rate of income tax charged on the income of discretionary and accumulation trusts will be reduced from 18 per cent to 10 per cent from 1988-89/

21 The administrative arrangements for the assessment and collection of tax from members of Lloyd's will be reformed. The legislation will first take effect for the Lloyd's 1986 Account, which closes at the end of 1988.

22 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 closed at the end of 1987. This is the first year to which the 1987 legislation on Lloyd's RIC will apply.

23 The rules (Section 79 Finance Act 1972) governing unapproved employee share
 schemes will be relaxed with effect from 26 October 1987 (when draft clauses were published for consultation).

24 Any benefit resulting from priority in applying for a public offer of shares given to employees by virtue of their employment/will, subject to certain conditions, be exempt from income tax.

25 Changes will be made to the approved discretionary share option legislation to enable employees to borrow to purchase their option shares without losing tax relief.

26 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 arises.

27 The limit below which redundancy and certain other lump sum payments are exempt from income tax will be increased from $\pounds 25\,000$ to $\pounds 30\,000$. The reduced rates of tax which apply to the next $\pounds 50\,000$ of such payments will be abolished.

28 The "top-slicing" relief which applies to the tax charged on premiums for leases and certain other payments will be withdrawn.

29 The definition of a recognised clearing system will be amended and the deduction of tax rules will be extended to collecting agents obtaining payment of overseas interest and dividends in the UK.

The new system of independent taxation for husbands and wives will apply from 1990–91. For income tax, the revenue costs in 1990–91 and 1991–92 (based on the existing distribution of income between husbands and wives) are estimated at \pounds 500 million and \pounds 1 billion respectively. For capital gains tax, the prospect of independent taxation may lead some couples to defer disposals until the new arrangements are in place; and the figure for 1989–90 in Table 4.1 reflects this. Costs for capital gains tax in 1990–91 and 1991–92 are estimated at \pounds 50 million and \pounds 50 million respectively. The estimates are subject to a high degree of uncertainty.

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	From 1988-89, th	e capital gains of individu	ils and trusts will be taxed at income
see redrate at Annex	take account of the lik and timing of disposal the gains of married c income.	at £75 million and in 1991 cely effect of taxing gains : ls. Until the introduction ouples will be taxed as the	lice of income. The revenue yield in -92 at \pounds 120 million. The figures at income tax rates on the volume of independent taxation in 1990–91, marginal slice of the husband's
3	case of individuals and	1 1,2 500 m the case of mo	will be reduced to £5000 in the st trusts. The revenue yield in 1990-
	account of the likely	fict of this measure on th	£50 million. The figures take e volume and timing of disposals.
	I ne costs of allowing	separate exempt amounts ese figures but at item 30.	for husband and wife from 1990-91
~ ~ ~			
	certain qualifying cond	ditions. From 6 April 1988	gains up to £125000, subject to half of any business gains between ject to the same conditions.
3	4 AT From Huly 1987, c not qualify for indexat	disposals of shares in Build tion relief.	ing and Co-operative Societies will
3	dependent relatives wi	Il be abolished. There will	ption for homes provided for be special provisions to ensure that
- the second second	a disposal before 1988-	-89.	ve qualified for this exemption on
Corporation tax	49 The small compani reduced to 25 per cent.	es' rate of corporation tax	for the financial year 1988 will be
	corporation tax (ACT)	will be balanced by an in	rate, the rate of advance of the amount of the distribution. rease in the subsequent liability to
	51 The rules for comp	any residence and migratio	on will be changed. In future
(in the UK)	managed and controlled	d here. UK incorporated	ompanies will be able to transfer
Treasury	their residence abroad-	-in both cases without/con e, including tax on capital	sent—on providing for the
(auned)	52 The Finance (No 2) trust. The full definition to ensure that the repeat	n will be reinstated, and th	the definition of an investment e legislation will include provision
	intra-group debts and si	hareholdings. This provisi	stricted on disposal of certain on counters use of the indexation nich could cause a significant loss
	group can now give rise	nt court ruling, share exch e to capital gains or losses ill be amended so as to ren	anges by companies in the same being taxed or allowed more than
	55 Capital allowances in "approved bodies" will Changes will be made to	n respect of properties let come to an end when the o the capital allowances le wwn and to provide transit	on assured tenancy terms by
Corporation tax and capital gains tax	56 Rollover relief will I and to milk quotas and	be extended to satellites an potato quotas from 30 Oct	d spacecraft from 28 July 1987 ober 1987.

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gains tax and to milk quotas and potato quotas from 30 October 1987 BUDGET SECRET—BUDGET SECRET

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Annex to Chapter 4

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Income tax, corporation tax and capital gains tax





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

1

(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 highly uncertain.

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

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Oil taxation

50

Can we find another way of putting this? Sound too much whe CTT.

Inheritance tax

Stamp duties

58 Changes in the tax rules concerning the conversion of building societies into public hanged companies are necessary in order to prevent unintended tax charges arising.

59 The PR t on 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 royalties on these fields. These two measures have a cumulative cost of around figures 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.

60 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.

61 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

62 The estimated full year cost attributable to transfers in 1988-89 is £220 million measured against an indexed base.

63 The $\[L100\]000\]$ exemption limit on transfers to political parties made on or within one year after death is abolished from Budget day.

64 Capital duty will not be payable on transactions completed after 15 March 1988. Unit trust instrument duty will not be payable on instruments executed after 15 March 1988, nor on property put into an existing trust after that date.

65 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.

Value added tax 66 The taxing provision relating to confectionery will be amended, with the main effect of taxing all cereal bars at the standard rate.

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67 Amendments will be made to the civil penalty system including 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.

68 From 16 March 1988 the registration limits will become £22100 per an £7500 per quere 1988 the registration limits will become £22100 per an

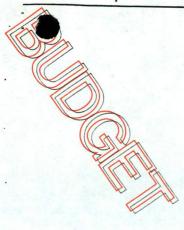
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69 The rules for registration of voluntary and intending traders will be simplifed and restrictions and conditions removed.

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70 From Royal Assent, 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.

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

Excise duties

s 72 There will be no change in the rate of duty on spirits.

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

From 1 October 1988, beer duty will be charged on the basis of $\pounds 0.90$ a hectolitre for every degree by which the original gravity of the beer exceeds 1 000°.

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

76 The duties on wine and made-wine will be increased by 4.5 per cent, equivalent to 3.8p on a 3ch bottle of still wine, 5.9p on a 70cl bottle of sparkling wine and 6.1p on a bottle of sherry (all inclusive of VAT).

77 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.

78 The duty on leaded petrol will be increased by 5.5 per cent or 5.5 pa gallon (inclusive of VAT). The duty on unleaded petrol will remain unchanged so that the tax differential in favour of unleaded petrol will rise to 10.6 pa gallon.

79 The duty on derv will be increased by 5.5 per cent, equivalent to 4.7p a gallon (inclusive of VAT).

80 There will be no change in the rates of duty on gas oil and fuel oil.

81 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, 5.3p on a 25 gram packet of hand-rolling tobacco and 1.9p/a packet of 5 small cigars (all inclusive of VAT).

82 The duty on pipe tobacco will be unchanged.

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Vehicle excise duties

83 There will be no change in the duties on cars, light vans, motor cycles, buses, coaches and most lorries.

84 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 arroulated vehicles of similar gross weight.

85 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 $\pounds 1600$. These vehicles cauches much wear and tear as the heaviest HGVs but currently pay a restricted HGV rate (1400).

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86 Bus fuel grants to certain bus service operators will automatically be increased to compensate them for the increase in duty on derv.

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INTERIM COMMITTEE

Ch Muchael feels that Ch I should include a reference t 'balanced hudget'. Ite suggests one/white A. additions marked lelas Colors one or two other Madad Son Mar Jon aver Mar Son Mar Jon aver minor points)

CONFIDENTIAL



FROM: A C S ALLAN DATE: 10 March 1988

MISS C EVANS

cc PS/Financial Secretary PS/Economic Secretary Sir P Middleton Mr Scholar Mr Odling-Smee Mr Culpin Mr R I G Allen Mr Pickford Miss Sinclair Miss Simpson Mr Cropper Mr P R H Allen - C&E

FSBR CHAPTER 1

The Chancellor was grateful for your minute of 9 March, and is content with the text.

2. His only comment was that he would prefer the entry in Table 1.1 currently labelled "oils" to be labelled "petrol and derv" instead.

A C S ALLAN

CONFIDENTIAL



FROM: A C S ALLAN DATE: 10 March 1988

MR S J DAVIES

cc Sir T Burns Mr Sedgwick Mr R I G Allen Mr Pickford Miss C Evans Miss Simpson

FSBR: CHAPTER 2

Further to my note earlier today, the Chancellor now wishes the end of paragraph 2.03 to read "with inflation approaching 4 per cent.".

A C S ALLAN

FROM:	JH	IBBERI)
DATE:	10	March	1988

PS/Chancellor cc: Sir P Middleton Sir T Burns Mr Turnbull Mrs Butler Mr S J Davies Mr Mowl Mr Allum

MR SEDGWICK

CSO REVISIONS TO GDP

As foreshadowed in my minute of yesterday, the CSO are still revising numbers for 1987. The latest substantive revision concerns GDP increased general government consumption in 1987, worth £650 million (1980 prices). There is also an additional £200 million (1980 prices) on consumers' expenditure.

On reasonable assumptions regarding growth between 1987Q4 and 2. 1988Q1, money GDP (average measure) is now likely to turn out £500 million higher in 1987/88 than we thought yesterday, to a level of £424.8 billion. This implies that growth between 1986/87 and 1987/ 88 is now likely to round to 10 per cent rather than 9% per cent, as reported yesterday. Revised levels and growth for money GDP are shown below.

	Money GDP market prices average measure (f million)	Growth on year earlier	
1987/88	424800	10	
1988/89	456600	71/2	
1989/90	486800	61/2	
1990/91	516200	6	
1991/92	544800	5½	

I must stress that there may be further revisions during the 3. course of tomorrow.

Tion this bend

J S HIBBERD

BUDGET SECRET: TASK FORCE LIST



COPY NO 19 OF 20

FROM: A C S ALLAN DATE: 10 March 1988

S J DAVIES

PS/Chief Secretary CC PS/Financial Secretary PS/Economic Secretary Sir P Middleton Sir T Burns Sir G Littler Mr Anson Mr Scholar Mr Odling-Smee Mr Peretz Mr Sedgwick Mr Turnbull Mr R I G Allen Mr Pickford Miss C Evans Miss Simpson Mr Cropper

FSBR: CHAPTER 2

0 . 0

The Chancellor was grateful for your minute of 9 March. He had the following comments on the text etc:

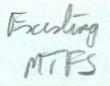
- (i) He wants to reflect further on the wording of the very end of paragraph 2.03 (which currently reads "with inflation at around 4 per cent"); I shall let you know during the course of the afternoon if he wishes to change this.
- (ii) He notes that the Q4 figures for money GDP and output need to be added to chart 2.1.
- (iii) The attached redraft of paragraphs 2.09 to 2.11 should be used.
 - (iv) The layout of page 9 is ugly. He would prefer chart 2.2 to be shrunk a little.



- (v) He prefers the years to be labelled as in chart 2.4, but with the spaces in, eg, "79-80" closed up. This format should be used for chart 2.5.
- (vi) The heading to chart 2.5 should be "Public Sector Borrowing Requirement" only, and not "and privatisation proceeds".
- (vii) In paragraph 2.16, the figure for the PSBR for 1988-89 should be type-set with a minus sign not a dash.
- (viii) In paragraph 2A.5, the last sentence should read "...oil revenues in 1988-89 are now forecast to be lower than projected a year ago". (ie omitting "somewhat").

Mpw PP. A C S ALLAN

MONETARY POLICY



2.09 Interest rate decisions are based on a continuous and comprehensive assessment of monetary conditions so as to ensure downward pressure on inflation.

2.10 Industry has benefitted from the greater stability of exchange rates over the past year, and the Government will continue to pursue a policy of exchange rate stability, with the rate against the Deutschmark being of particular importance. This provides an important financial discipline, which both ensures that increases in domestic costs will not be accommodated by a lower exchange rate, and at the same time unpins the declining path of money GDP growth and inflation.

2.10 Achieving these objectives requires a reduction in monetary growth over the medium-term ...

PS/CHANCELLOR

FROM: S J DAVIES DATE: 10 March 1988

PS/Chief Secretary PS/Financial Secretary PS/Economic Secretary Sir P Middleton Sir T Burns Sir G Littler Mr Anson Latyen we had Mr Scholar Mr Odling-Sme Mr Sedgwick Mr Sedgwick Mr Sedgwick Mr Turnbull Mr R I G Alle Mr Scholar Mr Odling-Sme Mr Sedgwick Mr Turnbull Mr R I G Alle Miss C Evans Miss Simpson Mr Cropper Mr Odling-Smee Mr R I G Allen

Can I clarify one point in your minute to me of 10 March. 2. Chart 2.1 currently has 1987 Q4 figures for money GDP and output, and a later observation for the RPI which can be thought of equally as the January outturn or the estimated January/ February average.

Could you confirm that it is agreed that we should show a 3. later observation for inflation than for money GDP and output? The alternative would be that we add 1988 Q1 forecast values for money GDP and output: these would show money GDP growth at just under 10 per cent, and output growth at just under 4 per cent: in both cases a small decline from the 1987 Q4 observations.

S J DAVIES



COPY NO LOF 15

FROM: A C S ALLAN DATE: 10 March 1988

MR MOWL

cc PS/Financial Secretary Sir P Middleton Sir T Burns Mr Scholar Mr Odling-Smee Mr Sedgwick Mr Culpin Mr S J Davies Mr Pickford Mr R I G Allen Miss C Evans Mr Cropper

FSBR CHAPTER 6

The Chancellor was grateful for your minute of 9 March. As I told you on the phone, he does <u>not</u> want to show a fall in total tax and NICs as a share of total money GDP in 1988-89 (the figures in Table 6.2 show shares of 37.8 per cent and 37.6 per cent for the two years). He would, if necessary, be prepared to show non-oil taxes and NICs rising from 37.5 per cent to 37.6 per cent, if that was consistent with a flat path for total taxes and NICs at, say, 37.7 per cent.

2. He was content with the other points in your cover note. He had a few minor points on the text:

- (i) The second sentence of paragraph 6.02 should start "This net repayment of debt ...".
- (ii) He may want to consider the wording of paragraph 6.10 and
 6.16 again, in the light of your advice on the paths for taxes and NICs.

A C S ALLAN

10

FROM: P N SEDGWICK DATE: 10 MARCH 1988

MR MOWL

cc PS/Chancellor Sir P Middleton Sir T Burns Mr Scholar Mr Odling-Smee Mr Turnbull Mrs R Butler Mr S J Davies Ms C Evans Mr Franklin Mr Ritchie

FSBR: CHAPTER 6

I have a few comments on the text of the version that you circulated last night.

Paragraph 6.06

Second Sentence: We do not have recorded consumers' expenditure for 1988Q1. I think therefore that you should replace "recorded" by "estimated". However true it may be I do not think that we should assert in the FSBR that growth of consumers' expenditure in 1987 may have been greater than the figure of 5 per cent that will appear in table 3.12. I suggest that you delete the rest of the sentence beginning with "this implies.....".

Paragraph 6.08

Fourth sentence: This should begin

"A \$1 a barrel difference in the <u>average</u> oil price in 1988...."

Paragraph 6.24

It would help this paragraph to be more comprehensible if you could say which public corporations had left the PC sector, or at least the main ones such as BGC.

P N SEDGWICK

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COPY NO. 17, OF 21

FROM: COLIN MOWL DATE: 10 March 1988

cc Financial Secretary Sir P Middleton Sir T Burns Mr Scholar Mr Odling-Smee Mr Sedgwick Mr Culpin Mr S J Davies Mr Pickford Mr R I G Allen Mr A C S Allan Ms C Evans Mr Ritchie Mr Franklin Mrs Todd Ms Chapman Mr Cropper Mr Calder - IR

Mr P R H Allen - C&E

FSBR CHAPTER 6

CHANCELLOR

Mar

I attach the proofs of chapter 6, further revised to incorporate your final decisions on the PSBR numbers and other changes to the components of the public sector finances. We have done our best in the time available to check all the numbers, but this process will continue tomorrow. Some final changes could well be made at book proof stage on Saturday morning. We would let you know immediately if there were any problems with key numbers such as the tax burden.

2. We have been able to meet your request that there should be no change between 1987-88 and 1988-89 in the total tax burden. The non-oil tax burden is also unchanged in 1983- 89, You said you would wish to look again at the wording of paragraphs 6,10 and 6.16 in light of the revisions to the tax burden figures in table 6.2. (Chart 6.1 has not yet been revised in line with table 6.2.)

There are a number of features of the numbers you might 3. note:

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LA rates and rate rebates

4. Tables 1.2, 6.5 and 6.7 show a 12½ per cent increase in net nate income in 1988-89. This is consistent with an estimated 7-8 per cent increase in gross rate poundage (this is not given in the FSBR but is the to DOE are likely to quote if asked). About 1½ points of the difference between the increases in net rate income and gross rate poundage is accounted for by the buoyancy of rateable values (from new building, for example). A further 2½ points is due to the projected fall in rate rebates.

5. The rate rebates figures are shown as a memo item in table 6.5. The fall in 1988-89 is due to the social security reforms to be implemented in April. The FSBR figure for 1988-89 is £0.25 billion higher than in the PEWP, partly because the coverage is different and partly because rate bills are set to increase by more than assumed in the PEWP. ST and DHSS are both aware of the numbers we intend to publish.

Tax payments by public corporations

6. Table 6.7 shows these increasing from £0.2 billion in 1987-88 to £0.7 billion in 1988-89. This increase is largely due to the electricity industry coming into CT for the first time. Numbers are consistent with the Electricity Council's expectations. PE are aware of the figures to be published.

Miscellaneous Financial Transactions (MFT)

7. These are shown in table 6.7 and largely comprise the sectoral balancing items ie. data discrepancies between income/expenditure estimates on the one hand and the borrowing figures on the other. It is these items to which City analysts may look in the hope of finding evidence that we have padded the PSBR figures. Unfortunately there are major discrepancies in the accounts for 1987-88 which we cannot avoid showing. The LA estimate is mentioned in the last sentence of paragraph 6.22.





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Miscellaneous Financial Transactions - £ billion

	CG	LA	PC	Public Sector
1987-88 1988-89	- 0.5	1.4	0.2	1.0
1988-89	- 0.1	1.1	0.0	1.0

Positive MFTs increase the PSBR. It may look therefore as though we are padding the PSBR in both years.

Corporation Tax (CT)

1 ×

Table 6B.3 shows total CT in 1987-88 £0.6 billion above 8. the 1987 FSBR forecast. Table 1.2 will show an overshoot of only £0.2 billion for non-North Sea CT. The difference is North Sea CT and CT on gains (included in taxes on capital in table 1.2), both of which are higher than forecast.

Conclusion

9. We should be grateful for comments by noon tomorrow, Friday.

COLIN MOWL

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6 The public sector's finances

The scope of this chapter

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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 borrowing¹

L billion			
1986-87	1987-88		1988-89
Outturn	1987 Budget	Latest estimate	Forecast
164.8	173.5	171.68	182.8
160.0159.0	168.8	173.77	184.7 8
4.9	4.7	-2-0-1.9	-19-2.0
- 1.5	-0.8	-09-1.2	-1.2
3.4	3.9	-29-3.1	-3.1 2
	1	$-\frac{3}{4}$	$-\frac{3}{4} \in bol$
D	\wedge		1.0
7.8	8.9 <u>21</u>	2-2- 1.9 1	
	1986-87 Outturn 164·8 160°0 15°9.0 4·9 -1·5 3·4 4 7·8	$ \begin{array}{c ccccccccccccccccccccccccccccccccccc$	1986-87 1987-88 Outturn 1987 Latest Budget estimate 164.8 173.5 171.978 164.8 173.5 171.978 16000159.9 168.8 173.7 4.9 4.7 -20-1.9 -1.5 -0.8 -09-1.2 3.4 3.9 -29-3.1 1 $-\frac{3}{4}$ 7.8 8.9 22.1.9

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1 Net borrowing: positive; net dest repayment: negative. 6.02 There is now estimated to be a negative privation of about (3) 6.02 There is now estimated to be a negative public sector borrowing requirement, ie a budget surplus, of about £3 billion in 1987-88. This net repayment of debt compares with the forecast of a borrowing requirement 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. A budget surplus of about $\pounds 3$ billion is forecast for 1988-89.

> 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.

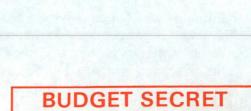
Public sector's finances: analysis by type or activity

6.04 Table 1.2 analyses the public sector's finances by type or activity. The main receipts of general government (ic 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. NOT TO BESORIED



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6.05 General government receipts in 1987-88 are now projected to exceed the 1987 Budget forecast by about £44 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 (\pounds]billion), VAT (\pounds 1 billion), and North Sea Revenues (\pounds ³/₄ billion).

6.06 Additional income tax receipts are mainly the result of the stronger growth of the economy and higher incomes. VAT receipts have increased by more in 1987-88 than would have been expected from the recorded increase in total consumer spending, this implies either that the proportion of total spending which goes on goods and services subject to VAT hasincreased, or that estimates of consumer spending in 1987 may be revised up later. The higher than expected oil revenues in 1987-88 are largely the result of a higher dollar oil price than assumed last year.

6.07 General government receipts are forecast to rise by $6\frac{1}{2}$ per cent in 1988-89 following an estimated $8\frac{1}{2}$ per cent increase in 1987-88. This is a little less than the rate of growth forecast for money GDP. Without the Budget measures however forecast growth in receipts would be about 1 percentage point 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 a lower average oil price and lower production. As last year, the forecast assumes that North Sea oil prices will average \$15 a barrel over the year ahead. 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 joil price in 1988 would change revenues by about $\pounds 270$ million in 1988-89 and \pounds 330 million in a full year. A change of 1 million tonnes in oil production in 1988, spread eventy across fields, would alter revenues by about \pounds 35 million in 1988–89 and \pounds 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 per cent increase in income tax receipts. Without the Budget & around measures the forecast increase would have been 10 per cent;

> a further rise of 24 per cent in receipts of corporation tax (including ACT but excluding North Sea mainstream corporation tax). This reflects continued growth in company profits in 1987;

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

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

a 5_2 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 turnover, and the abolition of cepital duty and unit trust investment duty in the Budget.

6.10 Table 6.2 shows taxes (including rates) and national insurance contributions as a percentage of GDP. Non-oil taxes have risen stightly as a percentage of non-oil GDP in each of the last two years, and la further marginal increase is forecast for 1988-89. Without the Budget measures the 1988-89 figure would have been almost a full percentage point higher.

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Table 6.2	Taxes and GDP	national i	insurance	contribut	ions (NICs	s) as a perce	entage of
	1982-83	1983-84	1984–85	1985–86	1986–87	1987–88 Latest estimate	1988–89 Forecast
Fotal taxes and NICs as a share of total money GDP Non-oil taxes and NICs as a	38-9	38.76	39.12	38.5	38,0 378	37. / 9	37·6 9 37·6 7
Non-on taxes and MICs as a	38-2	37.8	37.89	37.0	37.15	37.57	717

Expenditure 6.11 General government expenditure is now forecast to be about (17) billion in 1987–88, Libillion lower than in the 1987 Budget forecast. The outturn for the planning total is expected to be $\pounds 2\frac{1}{2}$ billion lower than in the original plans, and gross debt interest payments nearly \pounds_2^1 billion lower than forecast.

> 6.12 General government expenditure is expected to rise by 6² per cent in 1988-89, to about & billion. The planning total, at £156.8 billion, is as published in the public expenditure White Paper (Cm 288). 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 marked reduction in the PSBR.

Borrowing

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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 $\pounds 5\frac{1}{2}$ 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 of about $\pounds 3$ billion, or $\frac{3}{4}$ per cent of GDP.

about 6.15 A further budget surplus of $\pounds 3$ billion, or $\frac{3}{4}$ per cent of GDP, is forecast for 1988-89.

Trends in receipts and expenditure

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6.16 Chart 6.1 shows trends in taxes and expenditure as percentages of GDP. Revenues from non-oil taxes and national insurance contributions fell as a percentage of non-oil GDP between 1981–82 and 1985–86, but since then they have been rising. The percentage is forecast to rise again, although only marginally, in 1988-89.5 The ratio of general government expenditure (excluding privatisation proceeds) to GDP has fallen every year since 1982-83 except for a small rise in 1984-85 as a result of the miners' strike; it is forecast to fall again in 1988-89.

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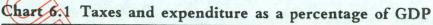


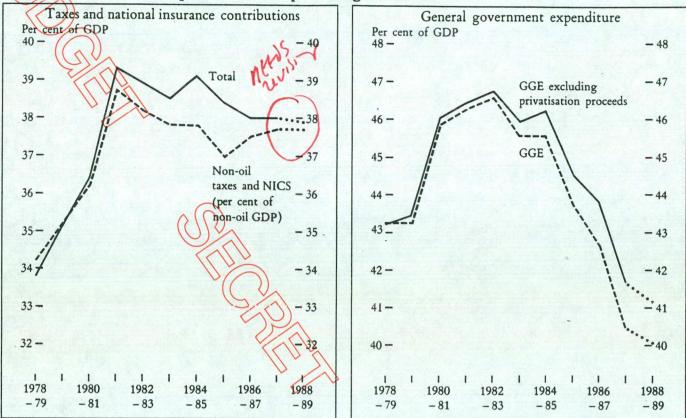
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6.17 Chart 6.2 shows the significant changes in the structure of general government receipts and expenditure which have taken place since 1978–79.

Receipts 1	978 - 79	1988 - 89	Expenditure	1978 – 79	1988 – 89
Income ta	x 29%	23%	DHSS-social secur	rity 22%	27%
Corporation ta	x 6%	9%	DHSS-health and personal social serv	ices 10%	11%
Capital taxe		2%-	Defe	ence 10%	11 /0
Local authority rate	es 9%	10%		A	11%
Central governmer expenditure taxes	^{1t} 28%	30%	Education and scie Scotland, Wales Northern Ireland	and	10%
North Sea revenue National insurance contributions		<u>- 2% -</u> 17%	Other departmen	nts* 25%	18%
Interest and dividend Other receip		3%	Debt inte Other adjustme		10%
	E	BUDGET SE	Cincluding privatisation proceeds and R	estrue TO B	E COPIE
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Chart 6.2 The structure of general government receipts and expenditure





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6 The public sector's financesUDGET SECRET-BUDGET LIST ONLY

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Public sector's finances: analysis by sector

6.18 Table 6.3 shows net borrowing in 1986-87 and 1987-88 by central government, local authorities and public corporations.

Public sector borrowing requirement Table 6.3

6–87 tturn • 5 5·9	1987–88 Latest estimate -2-8-3.7- 5.2
• 5 5·9	-28-3.2
5.9	
	5.2
	A REAL PROPERTY OF A REAP
- 5.6	-40-3.7
-2	1.15
	-0.12
	-0.12 -0.9-1.2
	-1.24
i-4	=29-3.1
5	241.7
1 3	0·1 - 1·5 1·4 3·4

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 Table 6.5 and 6.6.

Central government transactions Table 6.4

	£ billion		and the second
	1986-87	1987-88	1988-89
	Outturn	Latest estimate	Forecast
Receipts	11	0	101-10
Taxes and royalties	104.4 6	15.7 3	121.79
National insurance and other contributions	26.7 6	28.87	31.6
Other	10.4 5	11.26	11.76
Total receipts	141.47	155.76	164-5 165
Expenditure			A
Current expenditure on goods and services	49.4	330.02	55.7
Current grants and subsidies	77.84	80.7	82.85
Interest	16.5	169 1	0 177 16
Net lending ¹ , capital expenditure, and cash expenditure on company securities	2.79	1\$2.	0 203.
Total expenditure	146.02	152.5 4	158.423

¹Excluding lending to local authorities and public corporations ²Excluding any allocation from the Reserve LUST ONLY TO BEO & BIED

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6 The public sector's finances

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Local authorities

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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 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.

6.22 The local authority borrowing requirement (LABR) fell sharply in 1986–87 to $\pounds_{\frac{1}{4}}$ billion, from $\pounds_{1\frac{3}{4}}$ 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 scents likely that borrowing in the year as a whole will be above that in 1980–87 although still well below the levels of carlier years. The estimates of local authority receipts and expenditure do not fully explain the LABR in 1980–87 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

	L billion		
	1986–87 Outturn	1987–88 Latest estimate	1988–89 Forecast
Receipts			
Rates (net of rate rebates) ¹	15.6	17016.9	19.70
Rate support grant	11.8	12.6	13.3
Other grants from central government	4-0-10.3	12.20	12.7 4
Other	637.1	524.8	B.\$ 4.7
Total receipts	44.78	46.94	504 49.1
Expenditure)		
Current expenditure on goods and services	31.13	34.13	35.25
	♦ 5.4	5.87	6.0
Interest	4.14	4.43	4.\$6
Net lending and capital expenditure	4.20	3.86	4.41
Total expenditure	448 45.	481 47.0	i 50·1 ^{'2}
¹ Memo: Rate rebates ² Excluding any allocation from the Reserve	1.7	1.199	1.46

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 includes, in addition to borrowing, subsidies and grants provided by central government which have to be financed from taxation or central government borrowing.

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Table 6.6 Public corporations' transactions

rn Lat	$\frac{37-88}{\text{imate}}$ $\frac{7\cdot0}{2\cdot1} \text{ w}$	1988-89 Forecast 7.4 5 2.7 2
esti	7.0 2.1 v	7.4 5 2.7 2
)	2.1 v	7.45
)	2.1 v	7.45 2.72
	-1	2.72
12	0.114	0.00
12	74	9.68
	4. 4.	
3	3.13	3.8 5
5	47	5.7 €
3	798.0	9.\$*
1	0.4	0.7
3	06	0.8
	5 5 8 4 8	5 47 3 798,0 4 04

1 X 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 involve re-classifying privatised industries from the public 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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6 The public sector's finances

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

		\mathcal{L} billion ¹		The state		No. of the lot
(J)		1987-88 Latest	estimates			
		General govern	ment	<u> </u>	Public	Public
	Line ²	Central govern- ment	Local authori- ties	Total	corpora- tions	sector
Current and capital receipts		50 3 7		59.23	-0.12	59-1
Faxes on income, and oil royalties	1	59.23	1701/0		UNZ	69.4
Faxes on expenditure	2	52.43	17-0-16-9	69.43		3.67
Faxes on capital	3	3.67		3.87		28.89
National insurance and other contributions	4	28.87		28.87		6.98
Gross trading surplus	5	-0.6	0.5	-0.12	7.0	and the second second
Rent and miscellaneous current transfers	6	0.3	3-0 3.1	3.4	0.5	3.9
nterest and dividends from private sector and abroad	7	3.23	0.9	4.1.2	0.7	4.89
nterest and dividends within public sector	8	5.8	- 3.26	2.1	-2.1	
mputed charge for non-trading capital consumption	9	1.2	1.6	2.88		2· V B
Capital transfers from private sector	1 10	1 1 1 - 1 - 1 - 1 - 1 - 1 - 1 - 1 - 1 - 1 - 1	Sale		0.1	0.1
Fotal receipts	H	154-0	19-3	173-23	6.10	179.4
Current and capital expenditure		520 - 0	2 24 4 7	87.13		87:13
Current expenditure on goods and services	12	53-0 52.9	<u>34.1.3</u> 1.01	6.2		6.2
Subsidies	13	5.2		53-0.52		53-0 52
Current grants to personal sector	14	48.2	4.86			3.65
Current grants paid abroad	15	3.65		3.65		545
Current grants within public sector	16	23.86	-23.86			18-1 18
Debt interest	17	169720	0.85	17.5	0.65	11.98
Gross domestic fixed capital formation	18	3.6	3.86	7.43	4.5	0
Increase in stocks	19	-0.12	81.2-1	-0.12	01-	
Capital grants to private sector	20	1.98	0.6	2.5	0.1	2.65
Capital grants within public sector	21	1.7	(-1.0)	0.7	-0.7	
Total expenditure	22	157.74	20.2	177.9.6	4.65	182.4.0
Unallocated Reserve	23	2 	0			<u></u>
Financial deficit	24	3.84	0.98	4.63	-1.6	3.0 2
Financial transactions Net lending to private sector and abroad	25	0.13	- 0.6	-0.53	0.1	-0.42
Cash expenditure on company securities (including privatisation proceeds)	26	- 5.4	M	- 5.4) -	- 5.4
Transactions concerning certain public sector pension schemes	27	- 0.6		-06	-17	-0.6
Accruals adjustments	28	-0.1.5	-0.1	-0.15	1 -	-0.25
Miscellaneous financial transactions	29	-0.65	0-91-4	- 0· 3 8	0.2	061
Borrowing requirement	30	-2-8-3-	2 1.15	-1.67	1.24	-2-9 -

1 Financial deficits and borrowing requirements: positive ² Financial deficit (line 24) = expenditure (line 22) + Reserve (line 23) - receipts (line 12)

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Borrowing requirement (line 30) = financial deficit (line 24) + financial transactions (lines 25 to 29)





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6 The public sector's finances DGET SECRET-BUDGET LIST ONLY

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	L bittion			No. 19 Jak	Section 1	
	1988-89 Fore	1			£	
	General gove	mment		Public	Public	
		1, c		corpora- tions	sector	
		Local	Total			
Line ²	0	authori- ties				
Line	ment					Current and capital receipts
1	62-061-8	10 <u>-</u>	62-0 61-8	-0.7	61.3.]	Taxes on income, and oil royalties
2	55%4	19.30	74.84		74.84	Taxes on expenditure
3	4.87		437		4.87	Taxes on capital
4	31.6		(3).6	- 1	31.6	National insurance and other contributions
5	-0-1-	0.5	P-5	7.45	798.0	Gross trading surplus
6	0.4	3-112.8	3.42	0.6	3.98	Rent and miscellaneous current transfers
7	3-02.7	0.9	3.86	0.7	4.52	Interest and dividends from private sector and abroad
8	6.1	- 4.1	2.0	-2.0	-	Interest and dividends within public sector
9	1.23	1.6	2.89) PA	2.89	Imputed charge for non-trading capital consumption
10		<u></u>		0.2	0.2	Capital transfers from private sector
11	163.89	21-120.8	184.97	6.13	191.0	Total receipts
12	55.57	35.2 5	90-7 91.2	_/	~q1.2 907	Current and capital expenditure Current expenditure on goods and services
13	4.6	0.9	5.65		5.65	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		-24.86	<u> </u>		-	Eurrent grants within public sector
17	174170	0.25	17.65	0.27	11	Rebt interest
18	3.9	403.7	8-07.7	5.4	13.40	Gross domestic fixed capital formation
19	+0.1		+0.1	0.1		Increase in stocks
20	1.9	0.7	2.6	0.1	2.6	Capital grants to private sector
21	1.58	-0-8-1-1	0.7	-0.7	—	Capital grants within public sector
22	163-0 162.9	20.6	183.6	5.86	189-4/	Total expenditure
23					3.5	Unallocated Reserve
24		20 7 12 (L.).			1.97	Financial deficit
25	0.5	-0.3	0.2	0.1	0.32	Financial transactions Net lending to private sector and abroad
26	- 5.0		-5.0		- 5.0	Cash expenditure on company securities (including privatisation proceeds)
27	-0.67		-0.67		-0.87	Transactions concerning certain public sector pension schemes
28 -	0301	4 - Sa - S	-0.13	a state in the	-0.4 +	Accruals adjustments
29	-0.81	0.51.1	0-1-0	0-2 -	1.0 03	Miscellaneous financial transactions
30	State State	Frank Martin			-3.12.	Borrowing requirement

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Annex to Chapter 6

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 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 from lines 22, 23, 25 and 26 (third column) in Table 6.7 and onlending 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

BUDGET

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 and 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.

6A.7 The first outturn for the PSBR in 1987–88 will accordingly be published on 20 April. The first national accounts outturns for 1987–88 will appear in the June issue of Financial Statistics.

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Part B: central government transactions

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

THE .	£ billion 1987–88 latest estimate
Consolidated Fund	Dennis de la contractione
Revenue (Pable 6B 3)	123.92
Expenditure (Table 68.2)	121.70
National Loans Fund (Table 6B.4)	and the second second
Receipts	16.7
Payments	21.67
Surplus transferred from Consolidated Fund	18-2.2
Total net borrowing by the National Loans Fund	3+ 2.9
Surplus on other funds and accounts (net)	101.1
Central government borrowing requirement (Table 6.3)	211.7

1 fIncluding borrowing for on-lending to local authorities and public corporations.

Table 6B.2 Consolidated Fund expenditure

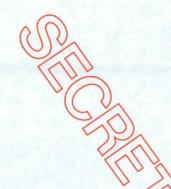
BUDGET

	£ million 1987–88 latest estimate
Supply issues 1	105 190 0
Standing services	States All
Payment to the National Loans Fund in respect of service of the national debt	9 800
Northern Ireland—share of taxes etc.	2 2 2 2 0
Payments to the European Communities	38077
Other services	100
Total standing services	16010 159
Total Consolidated Fund expenditure	121 200 0

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 Consolidated Fund revenue

	\mathcal{L} million	The second second	And the second
	1987-88		1988-89
	1987	Latest	Forecast
	Budget	estimate	
Inland Revenue		Yo	200
Income tax ¹	39 900	41 250	4/ 1/0 0
Corporation tax ²³	15 000	15 800	19 420
Petroleum revenue tax ⁴	1 680		1340 1180
Capital gains tax	1 300	1 350	1-790 1950
Development land tax	20	25	10
Inheritance tax5	1 100	1 070	970 1000
Stamp duties	2100	*	2200 1950
Total Inland Revenue	1987–88 1987 Latest Budget estimate 39 900 41 400 15 000 15 600 15 000 15 600 1680 2 410 1300 1350 20 25 1100 1070 2100 2430 ae 6 1100 4 400 7 800 7 800 7 800 7 800 7 800 800 7 800 7 800 800 800 800 1 100 1 100 1 100 1 100 1 100 1 100 1 100 1 100 1 100 1 100 1 100 1 100	67 440 80	
Customs and Excise		11	
Value added tax	23 300	24 800	26 220
		1.8	8410 40
Petrol, derarete		and the state of the second	4930 5000
Cigarettes and other tobacco		str.	4,400
Spirits, beer, while, ender and perry			860
Betting and gaming		A State of the second	
Car tax			1210
Other excise duties	20	20	20
EC own resources ⁶		,7	
Customs duties, etc.	1 350	1440	1480 1550
Agricultural levies	230		200 120
Total Customs and Excise	43 800		47 970 90
Vehicle excise duties ⁷	2 600	2720 0	27/05
Gas levy	490	520	500 490
Broadcasting receiving licences	1 030		1 1 40
Interest and dividends	1020	1 080	680
Other ⁸	2600	8980	7 050 30
Total Consolidated Fund revenue		and the second se	127270 12800
	-	No. Contraction	10 A. C. M. A.
¹ See paragraph 6B.1. ² Includes advance corporation tax		5	25
(net of repayments)			5 19 0 1 500
³ North Sea corporation tax of which satisfied by setting off ACT			780
Liability to corporation tax arising in respect of North Se	a production may be sati shore activities. Dividen	isfied by setting off ACT aris ids and ACT associated with	ing on dividends North Sea
 ⁵ Includes estate duty and capital transfer tax. ⁶ Customs duties and agricultural levies are accountable to the Communities are recorded in Table 6B.2. ⁷ Includes driving licence receipts. 	the European Commun	$\sim (())$	al payments to

* Includes the 10 per cent of 'own resources' refunded by the European Communities to meet the costs of collection, privatisation proceeds and oil royalties (see Table 1.2).

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Table 6B.4

3.4 National Loans Fund receipts and payments

	£ million 1987–88 Latest estimate
Receipts	
Interest on loans, profits of the Issue Department of the Bank of England, etc.	80 6p20
Service of the National Debt-balance met from the Consolidated Fund	9800
Total receipts	16 720
Payments	
Service of the National Debt:	,0
interest	16550
management and expenses	170
Total service of the National Debt	16 720 0
Loans to	-320-18
nationalised industries	
other public corporations	-1607 518020
local authorities	5190
private sector and within central government	180
Total National Loans Fund lending * 1	4890 600
Consolidated Fund surplus	1.840
Total payments	20 610

7 1 KOn-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).

Consulidated Fund surgive	2170
Total net sorrowing by me National Loans Fund	2462

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COPY NO 8 OF 18

FROM: A C S ALLAN DATE: 10 March 1988

MR SEDGWICK

cc PS/Chief Secretary Sir P Middleton Sir T Burns Mr Anson Mr Scholar Mr Culpin Mr Odling-Smee Mr Turnbull Mr S J Davies Mr Hibberd Mr Mowl Ms C Evans Mr Franklin Mr Ritchie Mrs Todd

THE PSBR IN 1987-88 AND 1988-89: FINAL FIGURES FOR THE FSBR

The Chancellor was grateful for your minute of 9 March. He wishes to publish PSBRs of £-3.1 billion for 1987-88 and £-3.2 billion for 1988-89.

ACSA

A C S ALLAN

1 5

BUDGET CONFIDENTIAL

1. MR TURNBULL AT .. 13

2. MR CULPIN

FROM: I R CUNNINGHAM DATE: 11 MARCH 1988

cc PS/Chancellor PS/CST Mr Anson Mr Scholar Miss Sinclair Mr A Williams

BUS FUEL GRANTS

You asked why bus fuel grants by Department of Transport had an economic classification out of public expenditure.

2. They are classified as refunds of taxes on expenditure, reflecting the fact that they are payments to road transport operators rebating customs duty on fuel used in the provision of public bus services.

3. Originally these grants, introduced in the Finance Act 1965, were classified as subsidies, ie as public expenditure. The change to regarding them as reducing tax receipts rather than increasing expenditure was made in 1976. The Central Statistical Office changed the national accounts treatment in the same way at the same time though, from the papers I have available, it is not clear whether the initiative for the change came from them or the Treasury.

I R CUNNINGHAM 270 5338

203/2

The implication of this is that reference to bus fuel grants belongs in Chapter 4 and that the figures should be in the falle as an offset to the higher revenue from derv.

Whether the policy of allowing bus operators, more and more of whom are in the private sactor, to get their fiel tax free is still valed is another question. (abbance copy of the D(Tp Vole though which the velocits are paid. The symbol • nears not public escipenditure.

A7 "13

1985-86	1986-87		1987-8
Outturn £'000	Total provision £'000	- Other (non-public) expenditure	Provisio £'00
		Section H: Bus fuel grants	
131,155	127,000	H1 Bus fuel grants 100 per cent rebates to bus operators of duty paid on fuel used on publicly available local bus services. Provision is calculated on rate of 74.51p per gallon for derv applicable from 19 March 1986. Provision takes account of adjustments to previous years' claims.	130,00
/		Section I: Driver testing and training	
7	_	I1 Driver testing and training • 1,735 staff at 1 April 1987 decreasing to 1,498 by 31 March 1988.	33,70
	=	 (1) Direct current expenditure (2) Payment to the Department of Transport for services (see Class VIII, Vote 2, subhead HZ) 	27,90 5,80
131,155	127,000	Total	163,70

Part III Extra receipts payable to the Consolidated Fund

1987-88		1986-87	1985-86
000'3		£'000	£'000
35	In addition to appropriations in aid there are the following estimated receipts: (1) Interest on and repayment of loans under the Local Employment Act 1972	38	91
494	(2) Interest on and repayment of loans under the Ports (Financial Assistance)	563	1,375
156,856	Act 1981 (3) Receipts from levy under section 13 of London Regional Transport Act 1984	193,608	212,024
2,667	 (4) Testing of heavy goods vehicle and public service vehicle drivers (5) Testing of motor car drivers and motorcyclists 		
30,956	(5) Testing of motor car drivers and motorcyclists		
1,935	(6) Testing of approved driving instructors including registration		-
306	(7) Miscellaneous receipts •	291	444
193,249	Total	194,500	213,934

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) OF 13 COPY NO V

FROM: A C S ALLAN DATE: 11 March 1988

MISS C EVANS

cc PS/Financial Secretary Sir P Middleton Mr Scholar Mr Odling-Smee Mr Culpin Mr R I G Allen Mr Pickford Miss Sinclair Miss Simpson Mr Cropper

FSBR: CHAPTER 1

The Chancellor has a few further points on Chapter 1:

- (i) He would prefer to see the layout as in last year's FSBR: ie with the table on the left hand page and the text on the right hand page.
- (ii) In paragraph 1.03 delete the words "and fiscal" in the second sentence, so that it begins "Monetary policies are designed to keep the growth of money GDP on a downward trend...". And begin the next sentence "This year's MTFS provides for a balanced budget over the medium term, with both taxes and public expenditure declining as a share of GDP. It is complemented by supply side policies...".
- (iii) In paragraph 1.07 add "around" to the two references to the budget surplus of £3 billion. And amend the third sentence to read "A further surplus of around £3 billion is envisaged for 1988-89, with a balanced budget thereafter".

A C S ALLAN

CONFIDENTIAL



FROM: A C S ALLAN DATE: 11 March 1988

MR ODLING-SMEE

cc Sir P Middleton Sir T Burns Mr Scholar Mr S Davies Miss C Evans

FSBR: CHAPTER 2

The Chancellor was grateful for your minute of 11 March, and for Mr Davies' minute of 10 March.

2. He is content with your redraft of the final sentence of paragraph 2.15.

3. On Chart 2.1, he would prefer to add 1981 Ql forecast values for money GDP and output: this will make the chart consistent with what was done last year.

TCSA

C S ALLAN

SECRET

From: J ODLING-SMEE 11th March 1988

CHANCELLOR OF THE EXCHEQUER

cc Sir Peter Middleton Sir Terence Burns Mr Scholar Mr S Davies Ms C Evans

FSBR: CHAPTER 2

Mr Scholar has pointed out that the final sentence of paragraph 2.15 is rather inelegant. I propose that we should redraft it as follows:

or?

"A PSBR of zero on the basis of current privatisation plans implies a PSBR of only 1 per cent of GDP in the absence of privatisation proceeds."

2. It would be helpful to know whether you are content with this by close of play today.

Dors

J ODLING-SMEE

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BUDGET CONFIDENTIAL



FROM: A C S ALLAN DATE: 11 March 1988

MISS SINCLAIR

cc PS/Financial Secretary Sir P Middleton Sir T Burns Mr Scholar Mr Culpin Mr Odling-Smee Mr R I G Allen Mr Pickford Mr Riley Miss Simpson Miss Evans Mr Hudson

> PS/IR Mr Calder IR

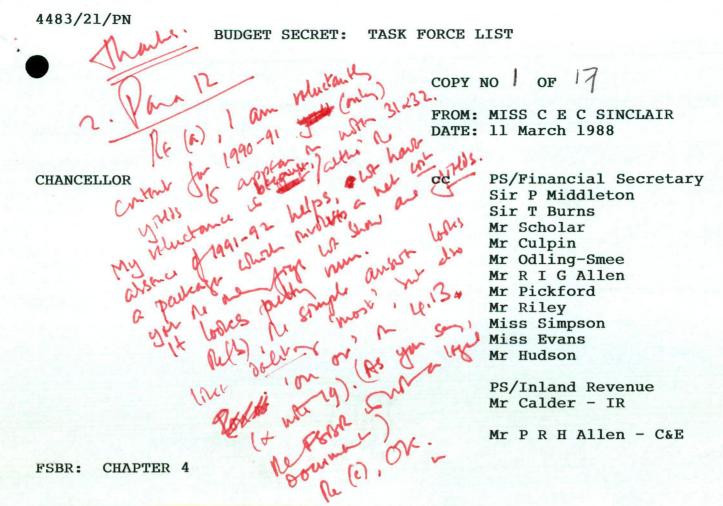
Mr P R H Allen C&E

FSBR: CHAPTER 4

The Chancellor was grateful for your minute of 11 March. On the questions in your paragraph 12:

- (a) he is, reluctantly, content for yields for 1990-91 (only) to appear in notes 31 and 32. His reluctance is because, although the absence of 1991-92 helps, we have a package which involves a net <u>cost</u> yet the only figures we show are yields. It looks pretty rum.
- (b) He thinks the simple answer looks to be to delete "most", but also to delete "on or" in paragraph 4.13 and note 19, leaving the text as "people who receive maintenance payments under new arrangements entered in to after Budget day will not be liable to tax on their receipts etc". (As you say, the FSBR is not a legal document).
- (c) He was content to retain the words "in general" in paragraph 4.19.

A C S ALLAN



You had a number of questions on the second printers' proof of Chapter 4.

2. Taking the points in Mr Allan's minute of 10 March first:

(i)

The costings in para 31 <u>do</u> assume annual indexation of the exempt amount.

It is not essential to show the yield in 1990-91 and (ii) 1991-1992 from reducing the CGT exempt amount, and taxing gains at income tax rates. But both can be estimated with more certainty than the cost of rebasing in later years (note 30). Inland Revenue feel that the preamble to the Annex - which says that additional information is provided in the commentary where the impact of a proposal is expected to build up over a period of years - makes it difficult and possibly OK? misleading not to give the figures for at least one (it's pretty) orld, since it is relating later year . Would you be content with this ie to show the figures for 1990-91 only in notes 31 and 32? do build up substantially

(iii) We have now revised paras 30-32 so that we only say <u>once</u> that estimates of cost take account of the likely effect of the measures on the volume and timing of disposals.

3. You had two questions on the text of the narrative.

4. In para 4.13 you queried the word 'most' in the sentence "People who receive maintenance payments under most new arrangements entered into on or after Budget Day will not be liable to tax on their receipts etc". Swe "entered into" who they pend?

5. "Most" was included because some arrangements made on or after Budget Day will stay on the old rules. In particular, people who apply for Court Order <u>on or before</u> Budget Day and are awarded them <u>on or before</u> 30 June will come under the old rules. Post-Budget Orders or agreements which merely vary or replace pre-Budget arrangements will also stay on the old rules. (Those who apply before Budget Day for the first time but do not get their awards until <u>after</u> 30 June will come under the new rules, as will those who apply after Budget Day.)

6. The Lord Chancellor was particularly concerned about Court Orders applied for <u>and</u> awarded on Budget Day (apparently a possibility). He wished such cases to fall under the old rules (to avoid possible problems if the Courts were unaware of your Budget proposal at the time they granted awards). This has been agreed.

7. All this means that it is not accurate to suggest that anyone who receives maintenance payments under a new arrangement entered into on or after Budget Day will necessarily come under the new rules ie will not pay tax on the payments.

8. This has taken several paragraphs to explain. But we can only include very short descriptions of the the position in the FSBR, even in the Annex. 'Most' seemed to the Revenue to be the neatest way of avoiding any misunderstanding. You may feel that such caution is misplaced as far as the FSBR is concerned (people will be able to read about the new rules in the press notices and leaflet). But on balance we think it is better to avoid statements which could be misleading.

9. A similar point arises in para 4.19, where you queried the need to say that "in general" only gains or losses accrued since 1982 will be brought into account for tax. The point is explained a little more in Annex note 30, which now reads

"There will be provisions to ensure that this change will never produce greater taxable gains or tax losses than the present system".

The way these will work is as follows:

The indexed gain or loss will be calculated on two bases: taking the price at acquisition, as now, and the value at 1982.

- (i) if both calculations show a gain, the smaller of the two gains will be used for calculating tax liability;
- (ii) if both calculations show a loss, the smaller of the two losses will be taken into account;
- (iii) if one result is a gain, and one a loss, there will be no gain/no loss for tax purposes.

An example at Annex A illustrates the point (so does the Inland Revenue press notice).

10. You will see that it is thus <u>not</u> strictly accurate to say that only gains or losses accrued since 1982 will be brought into account for tax. Losses or gains made before 1982 will still be relevant in some cases. You have asked to be reminded when Ministers decided this point (Mr Taylor's minute of 10 March to PS/FST). The Financial Secretary considered the issue again this morning and will be minuting you later today recommending that the policy decision should stand.

11. Assuming that you are content with the policy, what should be said in the FSBR, is a matter of judgement. We are inclined to agree with the Revenue's wording. The FSBR is not a legal document, and we do strive to make the narrative simple and readable. At the same time, it is the most formal printed version of your Budget measures, and there is much to be said for avoiding statements which could mislead, and provoke recriminations.

12. We have taken all your other points on board. It would be very helpful to know as soon as possible today.

- (a) whether you are content for the figures for the yield in 1990-91 only to appear in notes 31 and 32 (para 2(ii) above);
- (b) whether you agree that we should retain the word "most" in para 4.13 (and note 19).
- (c) whether you agree that we should retain the words "in general" in paragraph 4.19.

but pout is covered in Annese.

PP MAAn

CAROLYN SINCLAIR

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ANNEX

- (i) Acquisition cost = £100 value at 1982 = £ 80 value at sale = £150 taxable gain = £ 50
- (ii) Acquisition cost = £100
 value at 1982 = £ 80
 value at sale = £ 50
 loss for tax = £ 30
- (iii) Acquisition cost = £100
 value at 1982 = £ 80
 value at sale = £ 95
 gain/loss = zero

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OF 13 COPY NO

FROM: A C S ALLAN DATE: 11 March 1988

MISS C EVANS

cc PS/Financial Secretary Sir P Middleton Mr Scholar Mr Odling-Smee Mr Culpin Mr R I G Allen Mr Pickford Miss Sinclair Miss Simpson Mr Cropper

FSBR: CHAPTER 1

The Chancellor has a few further points on Chapter 1:

- (i) He would prefer to see the layout as in last year's FSBR: ie with the table on the left hand page and the text on the right hand page.
- (ii) In paragraph 1.03 delete the words "and fiscal" in the second sentence, so that it begins "Monetary policies are designed to keep the growth of money GDP on a downward trend...". And begin the next sentence "This year's MTFS provides for a balanced budget over the medium term, with both taxes and public expenditure declining as a share of GDP. It is complemented by supply side policies...".
- (iii) In paragraph 1.07 add "around" to the two references to the budget surplus of £3 billion. And amend the third sentence to read "A further surplus of around £3 billion is envisaged for 1988-89, with a balanced budget thereafter".

A C S ALLAN

RA3.1

SECRET



FROM: A C S ALLAN DATE: 11 March 1988

MR MOWL

cc PS/Financial Secretary Sir P Middleton Sir T Burns Mr Scholar Mr Odling-Smee Mr Sedgwick Mr Culpin Mr S J Davies Mr Pickford Mr R I G Allen Miss C Evans Mr Cropper PS/IR Mr P R H Allen - C&E

FSBR CHAPTER 6

The Chancellor was grateful for your minute of 10 March. He is most grateful to you for meeting his request that there should be no change between 1987-88 and 1988-89 in the total tax burden. He was content with the other points you made in your cover note.

- 2. He had two small drafting changes:
 - (i) In paragraph 6.10, amend the second sentence to read "Non-oil taxes have risen as a percentage of non-oil GDP in each of the last two years; they are forecast to remain unchanged in 1988-89".
 - (ii) In paragraph 6.16, amend the third sentence to read "The percentage is forecast to remain unchanged in 1988-89".

A C S ALLAN



COPY NO 8 OF 9

FROM: J M G TAYLOR DATE: 14 March 1988

PS/FINANCIAL SECRETARY

cc Mr Scholar Mr Culpin Mr Cropper Mr Pitts - IR Mr Cayley - IR PS/IR

CGT: GENERAL CHANGES

The Chancellor has seen the Financial Secretary's minute of 11 March.

2. He is content to leave matters as they are. But he notes that the Financial Secretary has confined himself to the case where the "special measures" work to the taxpayer's advantage. There will equally be cases where they may work to the taxpayer's disadvantage: eg example 4 on the Inland Revenue press release.

J M G TAYLOR

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COPY NO.) OF 21

FROM: COLIN MOWL DATE: 10 March 1988

cc Financial Secretary Sir P Middleton Sir T Burns Mr Scholar Mr Odling-Smee Mr Sedgwick Mr Culpin Mr S J Davies Mr Pickford Mr R I G Allen Mr A C S Allan Ms C Evans Mr Ritchie Mr Franklin Mrs Todd Ms Chapman Mr Cropper

Mr Calder - IR Mr P R H Allen - C&E

FSBR CHAPTER 6

I attach the proofs of chapter 6, further revised to incorporate your final decisions on the PSBR numbers and other changes to the components of the public sector finances. We have done our best in the time available to check all the numbers, but this process will continue tomorrow. Some final changes could well be made at book proof stage on Saturday morning. We would let you know immediately if there were any problems with key numbers such as the tax burden.

2. We have been able to meet your request that there should be no change between 1987-88 and 1988-89 in the total tax burden. The non-oil tax burden is a so onchanged in 1985-89. You said you would wish to look again at the wording of paragraphs 6.10 and 6.16 in light of the revisions to the tax burden figures in table 6.2. (Chart 6.1 has not yet been revised in line with table 6.2.)

3. There are a number of features of the numbers you might note:









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LA rates and rate rebates

4. Tables 1.2, 6.5 and 6.7 show a 12½ per cent increase in net rate income in 1988-89. This is consistent with an estimated 7-8 per cent increase in gross rate poundage (this is not given in the FSBR but is the to DOE are likely to quote if asked). About 1½ points of the difference between the increases in net rate income and gross rate poundage is accounted for by the buoyancy of rateable values (from new building, for example). A further 2½ points is due to the projected fall in rate rebates.

5. The rate rebates figures are shown as a memo item in table 6.5. The fall in 1988-89 is due to the social security reforms to be implemented in April. The FSBR figure for 1988-89 is £0.25 billion higher than in the PEWP, partly because the coverage is different and partly because rate bills are set to increase by more than assumed in the PEWP. ST and DHSS are both aware of the numbers we intend to publish.

Tax payments by public corporations

6. Table 6.7 shows these increasing from £0.2 billion in 1987-88 to £0.7 billion in 1988-89. This increase is largely due to the electricity industry coming into CT for the first time. Numbers are consistent with the Electricity Council's expectations. PE are aware of the figures to be published.

Miscellaneous Financial Transactions (MFT)

7. These are shown in table 6.7 and largely comprise the sectoral balancing items ie. data discrepancies between income/expenditure estimates on the one hand and the borrowing figures on the other. It is these items to which City analysts may look in the hope of finding evidence that we have padded the PSBR figures. Unfortunately there are major discrepancies in the accounts for 1987-88 which we cannot avoid showing. The LA estimate is mentioned in the last sentence of paragraph 6.22.









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Miscellaneous Financial Transactions - £ billion

	CG	LA	PC	Public Sector
1987-88	- 0.5	1.4	0.2	1.0
1987-88 1988-89	- 0.1	1.1	0.0	1.0

Positive MFTs increase the PSBR. It may look therefore as though we are padding the PSBR in both years.

Corporation Tax (CT)

Table 6B.3 shows total CT in 1987-88 £0.6 billion above 8. the 1987 FSBR forecast. Table 1.2 will show an overshoot of only £0.2 billion for non-North Sea CT. The difference is North Sea CT and CT on gains (included in taxes on capital in table 1.2), both of which are higher than forecast.

Conclusion

9. We should be grateful for comments by noon tomorrow, Friday.

COLIN MOWL

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6 The public sector's finances

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 borrowing¹

	L billion	State of the second		
	1986-87			1988–89
	Outturn	1987 Budget	Latest estimate	Forecast
General government expenditure	164.8	173.5	171.68	182.8
General government receipts	160-0159.9	168.8	173.77	184.7 8
General government borrowing requirement Public corporations' market and overseas	4.9	4.7	-20-1.9	-19-2.0
borrowing	- 1.5	-0.8	-09-1.2	-1.2
Public sector borrowing requirement	3.4	3.9	-2-9-3.1	-3.1 2
WPSBR as per cent of GDP	10p	1	$-\frac{3}{4}$	$-\frac{3}{4} \in bold$
Memorandum item: PSBR excluding privatisation proceeds	7.8	8.9	2-2-1.9	1.∮ ₹
A As per cent of GDP	2	24	$\frac{1}{2}$	1/2

2 Net borrowing: positive; net dest repayment: negotive.

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6.02 There is now estimated to be a negative public sector borrowing requirement, ie a budget surplus, of about $\pounds 3$ billion in 1987–88. This net repayment of debt compares with the forecast of a borrowing requirement of $\pounds 4$ 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. A budget surplus of about $\pounds 3$ billion is forecast for 1988–89.

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.

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 (ic 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.



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Receipts

6.05 General government receipts in 1987–88 are now projected to exceed the 1987 Budget forecast by about $\pounds 44$ 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 (\pounds 1) billion), VAT (\pounds 1 billion), and North Sea Revenues (\pounds_4^3 billion).

6.06 Additional income tax receipts are mainly the result of the stronger growth of the economy and higher incomes. VAT receipts have increased by more in 1987–88 than would have been expected from the recorded increase in total consumer spending<u>in this implies either that the proportion of total spending which goes on goods and services subject to VAT has-increased, or that estimates of consumer spending in 1987–88 are largely the result of a higher dollar oil price than assumed last year.</u>

6.07 General government receipts are forecast to rise by $6\frac{1}{2}$ per cent in 1988–89 following an estimated $8\frac{1}{2}$ per cent increase in 1987–88. This is a little less than the rate of growth forecast for money GDP. Without the Budger measures however forecast growth in receipts would be about $1\frac{1}{2}$ percentage points 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 a lower average oil price and lower production. As last year, the forecast assumes that North Sea oil prices will average \$15 a barrel over the year ahead. 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 £270 million in 1988– 89 and £330 million in a full year. A change of 1 million tonnes in oil production in 1988, spread eventy across fields, would alter revenues by about £35 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 per cent increase in income tax receipts. Without the Budget measures the forecast increase would have been 10 per cent;

a further rise of 24 per cent in receipts of corporation tax (including ACT but excluding North Sea mainstream corporation tax). This reflects continued growth in company profits in 1987;

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

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

a 5/2 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 turnover, and the abilition of coerital duty and unit trust investment duty in the Tudget. 6.10 Table 6.2 shows taxes (including rates) and national insurance contributions as a percentage of GDP. Non-oil taxes have risen stigntly as a percentage of non-oil GDP in each of the last two years, and [a further marginal increase] is forecast for 1988–89. Without the Budget measures the 1988–89 figure would have been almost a full percentage point higher.

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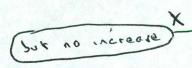
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Taxes and national insurance contributions (NICs) as a percentage of Table 6.2

	UDI		in the second	and share to be the state			
	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.\$6	39.12	38.5	38,0	37.79	37.89
Non-oil taxes and NICs as a share of non-oil money GDP	38-2	37.8	37. \$ 9	37.0	37.75	37.47	37.6.7

Expenditure 6 Concral government expenditure is now forecast to be about (1) Ebillion in 1987–88, Labillion lower than in the 1987 Budget forecast. The outturn for the planning total is expected to be $\pounds 2\frac{1}{2}$ billion lower than in the original plans, and gross debt interest payments nearly \pounds_2^1 billion lower than forecast.

> 6.12 General government expenditure is expected to rise by 6²/₄ per cent in 1988-89, to about 2 billion. The planning total, at £156.8 billion, is as published in the public expenditure White Paper (Cm 288). 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 marked reduction in the PSBR.

Borrowing

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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 $\pounds 5\frac{1}{2}$ billion lower than in the same period of 1986-87. Phis 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 of about \pounds 3 billion, or $\frac{3}{4}$ per cent of GDP.

about 6.15 A further budget surplus of $\pounds 3$ billion, or $\frac{3}{4}$ per cent of GDP, is forecast for 1988-89.

Trends in receipts and expenditure

6.16 Chart 6.1 shows trends in taxes and expenditure as percentages of GDP. Revenues from non-oil taxes and national insurance contributions fell as a Revenues from non-oil taxes and national instruction of 1985-86, but since then percentage of non-oil GDP between 1981-82 and 1985-86, but since then they have been rising. The percentage is forecast to rise again, although only marginally, in 1988-89.5 The ratio of general government expenditure (excluding privatisation proceeds) to GDP has fallen every year since 1982-83 except for a small rise in 1984-85 as a result of the miners' strike; it is forecast to fall again in 1988-89.

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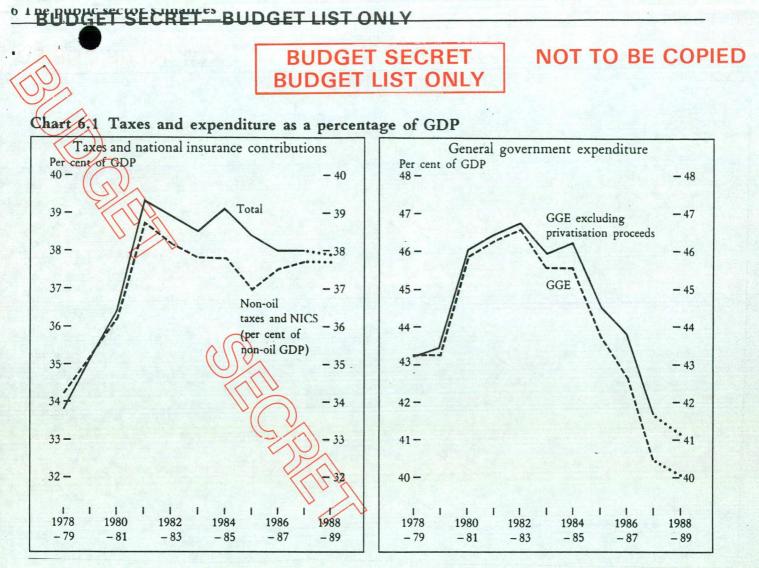
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6.17 Chart 6.2 shows the significant changes in the structure of general government receipts and expenditure which have taken place since 1978–79.

Receipts 1	978 - 79	1988 - 89	Expenditure	1978 - 79	1988 - 89
Income tax	c 29%	23%	DHSS-social secu	22%	27%
Corporation taz Capital taxe		9%	DHSS-health and personal social serv Defe	vices 10%	11%
Local authority rate	s 9%	10%	Education and soi	A	11%
Central governmen expenditure taxes	t 28%	30%	Scotland, Wales Northern Ireland	and	10%
North Sea revenue National insuranc contributions		2%-	Other departme	ents* 25%	18%
Interest and dividend Other receipt		3%	Debt inte Other adjustm	erest 10% ents 2%	10% 5%
	Е	UDGET SI	Cincluding privatisation proceeds and		E COPIE
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Chart 6.2 The structure of general government receipts and expenditure





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Public sector's finances: analysis by sector

6.18 Table 6.3 shows net borrowing in 1986-87 and 1987-88 by central government, local authorities and public corporations.

Public sector borrowing requirement Table 6.3

\mathcal{L} billion	State of the second second
1986-87	1987-88
Outturn	Latest estimate
4.5	-28-3.2
5.9	5.2
- 5.6	-40 -
	1.15
And the second state of th	-0.12
	-1.7 4
= 1:4	1.4 +
3.4	-29-3.1
10.5	241.7
	$ \begin{array}{r} 1986-87 \\ Outturn \\ 4.5 \\ 5.9 \\ -5.6 \\ 0.2 \\ 0.1 \\ -1.5 \\ -1.4 \\ 3.4 \\ \end{array} $

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 Table 6.5 and 6.6.

Central government transactions Table 6.4

	L billion		
	1986-87	1987-88	1988-89
	Outturn	Latest estimate	Forecast
Receipts	104.66	A15.13	121:79
Taxes and royalties National insurance and other contributions	26.7 6	28.87	31.6
Other	10.4 5	11.26	11.76
Total receipts	141.47	155.26	164516
<i>Expenditure</i> Current expenditure on goods and services	49.4	530.52	55.7
Current grants and subsidies	77.84	80.7.5	82.85
Interest	16.5	16-9 7	0 17t 1
Net lending ¹ , capital expenditure, and casi expenditure on company securities	h 2. 7 9	1\$2.	0 203
Total expenditure	146.02	152.5 4	158.423

¹Excluding lending to local authorities and public corporations ²Excluding any allocation from the Reserve GET UST ONLY TO EE & BETED

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Local authorities

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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 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.

6.22 The local authority borrowing requirement (LABR) fell sharply in 1986–87 to $\pounds_{\frac{1}{4}}$ billion, from $\pounds_{1\frac{3}{4}}$ 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 1980–87, although still well below the levels of carlier years. The estimates of local authority receipts and expenditure do not fully explain the LABR in 1980–87 and 1987–88 (other receipts in Table 6.5 and miscellaneous financial transactions in Table 6.7 include a balancing item).

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Table 6.5 Local authority transactions

	\mathcal{L} billion		
	1986–87 Outturn	1987–88 Latest estimate	1988–89 Forecast
Receipts			
Rates (net of rate rebates) ¹	15.6	17016.9	19.70
Rate support grant	11.8	12.6	13.3
Other grants from central government	110.3	12.20	12.7 4
Other	637.1	524.8	5.0 4.7
Total receipts	44.78	46.94	504 49.1
Expenditure)	Section and	
Current expenditure on goods and services	31.13	34.13	35.75
Current grants and subsidies	♦ 5.4	5.87	6.0
Interest	4.14	4.43	4.56
Net lending and capital expenditure	4.20	3.86	4.4 1
Total expenditure	448 45.1	48-1 47.0	50·1 ²
¹ Memo: Rate rebates ² Evolution any allocation from the Reserve	1.7	1.199	1.46

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 includes, in addition to borrowing, subsidies and grants provided by central government which have to be financed from taxation or central government borrowing.

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6 The public sector's finances DGET SECRET-BUDGET LIST ONLY

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Table 6.6 Public corporations' transactions

and the second of the second of the second of the	£ billion		and the second
	1986-87	1987-88	1988-89
	Outturn	Latest estimate	Forecast
Receipts			
Gross trading surplus (including subsidies)	7.4	7.0	7.45
Other	2.9	2.1 4	2.72
Total receipts	10.72	9.14	9.68
Expenditure		and an and a set	
Interest, dividends and taxes on income	3.3	3.1 3	3.8 5
Net lending and capital expenditure	5.5	47	5.7 €
Total expenditure	8.8	798.0	9.8%
Memo: nationalised industries' external finance other public corporations' contribution to the	0.4	0.4	0.7
planning roual	0.8	0.6	0.8

1 X Excluding any attocation from the Reserve

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6.24 Changes in public corporations' income and expenditure from one year to another are affected by privatisations which involve re-classifying privatised industries from the public 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

		\mathcal{L} billion ¹			CAN A STALL	
(0)		1987-88 Latest	estimates			<u></u>
2 AL		General govern	ment	1000	Public	Public
The second secon	Line ²	Central govern- ment	Local authori- ties	Total	corpora- tions	sector
Current and capital receipts		59.23		59.23	-0.12	59.1
Taxes on income, and oil royalties	1	52.43	17-0-16.9	69.43		69.4
Taxes on expenditure	2		State State States	3.67		3.67
Taxes on capital	3	3.67		28.87		28.89
National insurance and other contributions	4	28.87	0.5	-0.12	7.0	6.98
Gross trading surplus	5	- 0.6		3.4	0.5	3.9
Rent and miscellaneous current transfers	6	0.3	3-0 3-1	4.12	0.7	4.89
Interest and dividends from private sector and abroad	7	3.23	0.9	2.1	-2.1	
Interest and dividends within public sector	8	5.8		2.18	2.1	2.76
imputed charge for non-trading capital consumption	9	1.2	1.6	2.10	0.1	0.1
Capital transfers from private sector	1 10		-			179.4
Total receipts	11	154.0	19-3	173-23	0.70	1/9-4+
Current and capital expenditure Current expenditure on goods and services	12	53-0 52.9	34.1.3	87.13		87:13
Subsidies	13	5.2	1.01	6.2		6.2
Current grants to personal sector	14	48.2	4.86	53-05.	2.8 -	53-0 52.
Current grants paid abroad	15	3.65		3.65		3.65
Current grants within public sector	16	23.86	-23.86			
Debt interest	17	169120	0.85	17.5	0.65	18-1 18-
Gross domestic fixed capital formation	18	3-6	> 3.86	7.43	4.5	11.98
Increase in stocks	19	-0.12		-0.12	01-	1-0
Capital grants to private sector	20	1.98	0.6	2.5	0.1	2.65
Capital grants to private sector Capital grants within public sector	21	1.7	-1.0	0.7	-0.7	1997 <u>—</u> 1997
Total expenditure	22	157.7.4	20-2	177.9.6	4.65	182.4 0
Unallocated Reserve	23	and the second second	5		24	<u></u> 4=0
Financial deficit	24	3.84	0.98	4.63	- 1.6	3.0 2 -
Financial transactions Net lending to private sector and abroad	25	0.13	-0.6	-0.53	0.1	-0.42
Cash expenditure on company securities (including privatisation proceeds)	26	- 5.4		- 5.4	2	- 5.4
Transactions concerning certain public sector pension schemes	27	-0.6	<u> 10 10 10 10 10 10 10 10 10 10 10 10 10 </u>	-06		-0.6
Accruals adjustments	28	-0.15	- 0.1	-0.15		-0.15
Miscellaneous financial transactions	29	-0.65	091.4	A CONTRACTOR OF A CONTRACTOR OFTA CONTRACTOR O		061.0
Borrowing requirement	30	-2-8-3-	2 1.15	-1.67	L -1.24	-29-3

1 Financial deficits and borrowing requirements: positive 2 Financial deficit (line 24) = expenditure (line 22) + Reserve (line 23) - receipts (line 11)

Borrowing requirement (line 30) = financial deficit (line 24) + financial transactions (lines 25 to 29)

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	1988 89 For	casts				
	General gove	mment		Public	Public	
		NC		corpora- tions	sector	
	Central	Local	Total	tions		
	govern-	authori-				
Line ²	ment	ties				
	62-0 61-8		62-0 61-8	-0.7	61-3	Current and capital receipts Taxes on income, and oil royalties
1		19.30		- (). /	74.84	Taxes on income, and on royalties
2 3	55:64	19.30	74.84			Taxes on capital
4	4·27 31·6		4.37		31.6	National insurance and other contributions
5	-0+-	0.5	0.5	7.4.5		OGross trading surplus
6	0.4	342.8	342	0.6	3.98	Rent and miscellaneous current transfers
7	342.7	0.9	3.86	0.7		Interest and dividends from private sector and abroad
8	6.1	- 4.1	2.()	2-2-0		Interest and dividends within public sector
9	1.23	1.6	2.89	<u> (U)</u>	2.89	Imputed charge for non-trading capital consumption
10	-			0.2	0.2	Capital transfers from private sector
11	163-89	21-120-8	184.97	6:13	191.0	Total receipts
	105 4 1	A 120 V	101 19	42	91.2	Current and capital expenditure
12	55.57	35.25	90791.2		90-7	Current expenditure on goods and services
13	4.6	0.9	5.65	49. <u>—</u> 1. 19	5.65	Subsidies
14	50.5	5.0	55.5	<u></u>	55.5	Current grants to personal sector
15	2.9		2.9	<u> </u>	2.9	Current grants paid abroad
16	24.76	-24.86				Current grants within public sector
7	174170	0.25	17.65	0.27	18.52	Rept interest
18	3.9	403.7	8-07.7	5.4	13.40	Gross domestic fixed capital formation
19	+0.1		+0.1	0.1	0.12	Increase in stocks
20	1.9	0.7	2.6	0.1	2.6	Capital grants to private sector
?1	1.58	-0-8-1-1	0.7	- 0.7		Capital grants within public sector
22	163.0 162.9	20.6	183.6	5.86	189-4/	Total expenditure
23	A Party State				3.5	Unallocated Reserve
24			New York Street		1.97	Financial deficit
25	0.5	-0.3	0.2	0.1	0.32	
26	- 5.0	<u>_</u>	- 5.0		- 5.0	Cash expenditure on company securities (including privatisation proceeds)
27	-0.67		-0.67	-	-0.87	Transactions concerning certain public sector pension schemes
28 -	-0301	1 <u>14</u>	-0.13	Charles Ing	-0.4 +	Accruals adjustments
29	-0.81	0-51.1	0-21-0	02-	1.0 03	Miscellaneous financial transactions
30					-3.12	Borrowing requirement

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Annex to Chapter 6

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 Table 6.7 (including the "financial transactions" in lines 25–26), but also borrowing or capital 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 from lines 22, 23, 25 and 26 (third column) in Table 6.7 and onlending 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 and 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.

6A.7 The first outturn for the PSBR in 1987–88 will accordingly be published on 20 April. The first national accounts outturns for 1987–88 will appear in the June issue of Financial Statistics.

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Annex to Chapter 6

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Commentary on the tables

Table 6B.1

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Part B: central government transactions

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.

	£ billion 1987–88 latest estimate
Consolidated Fund	
Revenue (Vable 6B.3)	123.92
Expenditure (Table 68.2)	121.70
National Loans Fund (Table 6B.4)	The Astronomy
Receipts	16.7
Payments	21.67
Surplus transferred from Consolidated Fund	182.2
Total net borrowing by the National Loans Fund	3+2.0
Surplus on other funds and accounts (net)	101.1
Central government borrowing requirement (Table 6.3)	211

1 fincluding borrowing for on-lending to local authority's and public corporations.

Table 6B.2 Consolidated Fund expenditure

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◆ .	£ million 1987–88 latest estimate
Supply issues 2	105 190 0
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 2 2 2 0
Payments to the European Communities	38077
Other services	100
Total standing services	16010 15900
Total Consolidated Fund expenditure	121 200 0

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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

B.3 Consolidated Fund revenue

	\mathcal{L} million			
	1987-88		1988-89	
	1987	Latest	Forecast	
	Budget	estimate	No.	
Inland Revenue		Yo	200	
Income tax ¹	39 900	41 750	4/ 1/30	0
Corporation tax ²³	15 000	15 \$00	19 420	
Petroleum revenue tax ⁴	1 680	2210	1340	1180
Capital gains tax	1 300	1 350	1-790	1950
Development land tax	20	25	10	
Inheritance tax5	1 100	1 070	970	1000
Stamp duties	2100	2 4\$0	2-200	1950
Total Inland Revenue	61 100	64 150 20	67 440 8	20
Customs and Excise		"		
Value added tax	23 300	24 \$00	26 220	
Petrol, dera er	7 800	7 00	8 \$70	40
Cigarettes and other tobacco	4 800	4 800		5000
	4 300	4 200	4 400	
Spirits, beer, while, cuder and perry	4 300 800	780 810	860	
Betting and gaming				,
Car tax	1 100	1 100 5	120	
Other excise duties	20	20	20	
EC own resources ⁶		۲,		
Customs duties, etc.	1 350	1440		1220
Agricultural levies	230	190	and the second state in the second state of th	120
Total Customs and Excise	43 800	44 \$30 70	47 670	
Vehicle excise duties ⁷	2 600	27200	27/0	
Gas levy	490	520	500	. 489
Broadcasting receiving licences	1 0 3 0	1 030	1 1 4 0	
Interest and dividends	1020	1 080	680	
Other ⁸	7.600	8900	7 \$\$0	30
Total Consolidated Fund revenue	117 500	123 \$40 20	127-270	
See paragraph 6B.1.	and the second			
² Includes advance corporation tax		5	25	
(net of repayments)	4 700 1 400	4 9 9 0 1 360	5 19 0 1 500	
³ North Sea corporation tax of which satisfied by setting off ACT	800	7 \$30	780	
Liability to corporation tax arising in respect of North Si paid in previous periods in respect of both onshore and of activities alone cannot be identified. ⁴ Includes advance-payments of petroleum revenue tax.	ea production may be sati fshore activities. Dividen	isfied by setting off ACT ari. ids and ACT associated with	sing on dividends North Sea	
⁵ Includes estate duty and capital transfer tax. ⁶ Customs duties and agricultural levies are accountable t	o the European Commun	uities as 'own resources': artu	al payments to	
the Communities are recorded in Table 6B.2.	o inc European Comman		<i>[</i> ,,,,,	
⁷ Includes driving licence receipts.	the European Communit		im privatisation	

⁸ Includes the 10 per cent of 'own resources' refunded by the European Communities to meet the costs of collection, privatisation proceeds and oil royalties (see Table 1.2).

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Table 6B.4

National Loans Fund receipts and payments

	£ million 1987–88 Latest estimate
Receipts Interest on loans, profits of the Issue Department of the	80 6 92 0
Bank of England, etc. Service of the National Debt—balance met from the Consolidated Fund	9800
Service of the National Debt—balance met from the Consondated Fund	16 720 0
Payments	
Service of the National Debt:	0
interest	16 550
management and expenses	170
Total service of the National Debt	16720
Loans to	-320-16
nationalised industries	-1407
other public corporations	-107
local authorities	180
private sector and within central government	
Total National Loans Fund lending * 1	4890 50
Consolidated Fundsurplus	1.840
Total payments	20 610

7 1 XOn-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).

Consolidated	Fund surplus	2170
Total net !	porrowing by me National Loans Fu	nd 2867

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Financial Statement and Budget Report 1988-89

Return to an Order of the House of Commons dated 15 March 1988: for

Copy of Financial Statement and Budget Report 1988-89 as laid before the House of Commons by the Chancellor of the Exchequer when opening the Budget

> Treasury Chambers 15 March 1988

Norman Lamont

Ordered by the House of Commons to be printed 15 March 1988

HER MAJESTY'S STATIONERY OFFICE LONDON

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Last year's

BUDGET SNAPSHOT 17 MARCH 1987

1. TAX PROPOSALS

(1) Income Tax

Basic rate reduced from 29 per cent to 27 per cent.

Personal allowances increased in line with inflation (3.7 per cent RPI to December 1986).

Allowances (£)	1986-87	1987-88
Married man's	3655	3795
Single (and wife's earned income)	2335	2425
Additional personal (& widow's bereavement)	1320	1370
Aged: married	4505	4675
Aged: single	2850	2960
Aged income limit	9400	9800

New higher age allowance for those aged 80 or over of £3070 (single) and £4845 (married)

Allowance for blind up from £360 to £540 (from £720 to £1,080 where both married partners are blind).

Higher Rates (£)

Starting point for 40 per cent rate increased in line with inflation; starting point for 45 per cent rate increased by £200.

Taxable income

Rate of tax (per cent)	1986-87	1987-88
40	17201-20200	17901-20400
45	20201-25400	20401-25400
50	25401-33300	unchanged
55	33301-41200	unchanged
60	over 41200	unchanged

Profit Related Pay (PRP)

New tax relief for eligible PRP; half of PRP to be exempt from tax up to lower of £3000 a year or 20 per cent of pay.

Pensions

New tax regime for personal pensions from 4 January 1988 on lines set out in consultative document "Improving the Pensions Choice" published in November 1986. Personal pensions to be given similar tax treatment to retirement annuities.

Simpler occupational pension scheme arrangements to be made available to employers.

Members of occupational pension schemes to be able to make additional voluntary contributions within existing tax relief limits to pension arrangements outside employer's scheme.

Tax-free lump sums limited to £150,000 for new schemes and new members of existing schemes.

(ii) Excise Duties

No changes in duties on tobacco, drinks (beer, cider, wines, spirits), leaded petrol, derv or other oils. 5p differential in favour of unleaded petrol (from 17 March)

No change in £100 a year Vehicle Excise Duty on cars and light vans, nor in most other VED.

On-course betting duty for horse and greyhound racing abolished.

Gaming machine licence duty increased:

In pubs, arcades etc: 5p machines up from £120 to £150, 10p machines up from £300 to £375. In clubs: 5p machines from £300 to £375, 10p machines from £750 to £960.

(iii) Value Added Tax (VAT)

No change in 15 per cent rate.

Registration threshold (annual turnover below which traders are not obliged to register) up from £20,500 to £21,300.

Period during which businesses must apply to register extended from 10 to 30 days.

Businesses with turnover of up to £250,000 a year to have options of:

- (i) accounting for VAT on basis of cash paid and received (from 1 October 1987) (subject to EC agreement)
- (ii) making one VAT return a year (instead of four) (from summer 1988)

Package of changes to special VAT scheme for retailers. In particular simpler schemes to be available to more small and medium sized businesses.

Package of measures to eliminate various forms of VAT avoidance as announced on 19 December 1986. Right to deduct input tax to be limited to that incurred in making taxable supplies.

Modest extension of reliefs for charities caring for the disabled and terminally ill or engaged in medical research, first aid and mountain rescue.

(iv) Capital Taxes

Inheritance Tax (IHT)

Thresholds up from £71,000 to £90,000: number of rates reduced from seven to four (from 17 March):

Bands of chargeable value (£)	Tax rate (per cent)	
0-90000	NIL	
90000-140000	30	
140000-220000	40	
220000-330000	50	
over 330000	60	

IHT abolished for lifetime gifts into "Interest in Possession" trusts.

Capital Gains Tax

Limit for retirement relief increased from gains of £100,000 to £125,000 (from 6 April). Annual exempt amount for individuals increased in line with inflation from £6300 to £6600.

(v) Business Taxation

Small companies rate of Corporation Tax (CT) and rate of Advance Corporation Tax (ACT) down from 29 per cent to 27 per cent. CT on companies' capital gains to be charged as income at normal CT rate (35 per cent or 27 per cent) without adjustment. ACT set-off will be allowed against CT on capital gains.

CT payment dates to be 9 months after end of accounting period for all companies and building societies: change to be phased in.

'Pay and File' package of proposals reforming and simplifying administration of CT: legislation in 1987 for implementation in early 1990s.

Measures to remove unintended and unjustified tax breaks; includes tighter rules on:

- tax credit relief for banks;
- companies resident in both the UK and abroad;
- members of Lloyd's insurance market.

(vi) Business Expansion Scheme (BES)

Where investments made in first half of tax year, investor will be able to claim part of relief against income of previous year. Change will reduce bunching of BES investment at end of tax year.

Some relaxation of rules for film companies.

(vii) Petroleum Revenue Tax (PRT)

Companies may elect to have up to 10 per cent of costs of developing certain new fields immediately set against liability for PRT in existing fields until income exceeds costs.

Relief for research unrelated to any particular field.

2. DIRECT REVENUE EFFECTS OF BUDGET MEASURES

£million	1987-	-88
	Changes from non-indexed base	Changes from indexed base
Income Tax basic rate	-2200	-2200
Income Tax allowances and thresholds	- 770	+ 30
Excise duties + VAT	+ 185	- 360
Other changes	- 110	- 95
	-2895	-2625

3. **PUBLIC SECTOR BORROWING REQUIREMENT (PSBR)**

PSBR set at £4 billion in 1987-88, 1 per cent of GDP: 1986-87 outturn expected to be £4 billion, 1 per cent of GDP. PSBR projected to remain at 1 per cent of GDP throughout the new Medium Term Financial Strategy period which runs to 1990-91.

BUDGET SNAPSHOT: 15 MARCH 1988

1. TAX PROPOSALS

(i) Income Tax

Allowances

Main Allowances increased by twice rate of inflation. (RPI increase in year to December 1987 was 3.7 per cent).

Allowances (£)	1987-88	1988-89
Married Man's	3795	4095
Single (and wife's earned income)	2425	2605
Additional Personal (and widow's bereavement)	1370	1490
Aged: married		
age 65-79	4675	5035
age 80 and over	4845	5205
Aged: single		
age 65-79	2960	3180
age 80 and over	3070	3310
Aged income limit	9800	10,600

Unmarried couples with children to be limited to one additional personal allowance between them from April 1989.

Basic rate reduced from 27 per cent to 25 per cent.

Government's new aim is ultimately to reduce basic rate to 20 per cent.

Basic rate limit increased by twice rate of inflation.

Higher rates

Single higher rate of 40 per cent; rates of 45 per cent to 60 per cent abolished.

Taxable income

Rate of tax (per cent)	1987-88	1988-89
40	17,901-20,400	over 19,300
45	20,401-25,400	
50	25,401-33,300	
55	33,301-41,200	
60	over 41,200	

Additional rate on income of discretionary trusts reduced from 18 per cent to 10 per cent.

(ii) Mortgages and home improvement loans

Mortgage interest relief (MIR) limit to remain at £30,000 for 1988-89.

MIR to be changed to <u>apply to residence</u> instead of to individual or married couple; so unmarried sharers will get equal portions of ceiling (from 1 August 1988).Tax relief for home improvement loans to be abolished (from 6 April 1988). In both cases existing loans unaffected.

(iii) Company cars

Scale charges for private use of company cars to be doubled for 1988-89 over 1987-88 levels. For example 1987-88 scale charge of £700 on a 1.6 litre car, worth at least £3000 to an employee, will rise to £1400 in 1988-89. (Subsumes 1987 Budget announcement on 1988-89 scale charges).

Car fuel scale charges - No change

(iv) Forestry

Subject to transitional arrangements, commercial woodlands to be wholly removed from income and corporation tax.

Special Schedule B for income from woodland to be abolished (from 6 April 1988).

Parallel increases in planting grants for commercial woodlands.

On		y increase er cent)	Price increase including VAT (pence)	Comes into effect
Beer* Table wine Cider Spirits (Whisky etc) Fortified wine (port, sherry etc)	pint 75cl pint 75cl 70cl	4.7 4.5 9.7 No C 4.5	1 3.8 1 Change 6.1 sherry 7.1 port	6pm 15 March 1988
Cigarettes Cigars Pipe tobacco	20 King size 5 small	3.7 3.7 No C	3.4 1.9 Change	midnight 17- 18 March 1988
Leaded petrol Unleaded petrol Derv	gallon gallon	5.5 No C 5.5	5.5 Change 4.7	6pm 15 March 1988

* Minimum duty charge on beer to be abolished (from 1 October 1988)

Differential in favour of unleaded petrol therefore doubled; should give it 6p price advantage over 4-star leaded.

Lower strength mixed drinks (eg 'coolers') to be subject to duty according to strength on a scale related to table wine duty. To be introduced later in 1988 following consulations.

(vi) Vehicle Excise Duty (VED)

No change in £100 VED on cars and light vans. No change for most lorries; but VED increased for some very heavy goods vehicles.

(vii) Value Added Tax (VAT)

No change in 15% rate.

Registration threshold (annual turnover below which traders are not obliged to register) up from £21,300 to £22,100.

Clarification of VAT treatment of confectionery; main effect to bring to all cereal bars into tax (from 1 May 1988).

- 3 -

(viii) Maintenance payments

Maintenance payments under new court orders and agreements to be tax-free for recipients.

Maintenance payments under new court orders and agreements will qualify for tax relief only to separated or divorced spouses up to a new limit equal to difference between single and married allowance (£1490 in 1988-89) (from 15 March 1988).

Transitional arrangements for existing orders and agreements.

(ix) Covenants

For new non-charitable covenants, tax relief for donor and tax liability for recipient abolished (from 15 March 1988). Existing covenants unaffected.

Parallel reduction in parental contribution scale for new students.

(x) Charities

No change for covenants to charities. Limit on donations under payroll giving scheme doubled to £240 a year or £20 a month.

(xi) Personal Equity Plans (PEPs)

Limit to be increased from £2400 to £3000 for PEP year 1988.

Limit on investment in unit and/or investment trusts to be £540, (up from £420), or 25 per cent of subscription if higher.

Limit on cash in PEPs to be £300 (up from £240), or if greater, 10 per cent of market value of plan investments.

(xii) Capital Gains Tax (CGT)

Gains accrued before 31 March 1982 to be exempt: new base date to be applied to disposals made from 6 April 1988. Eliminates entirely taxation of inflationary gains.

Annual exempt amount down from £6600 to £5000 for individuals, and from £3300 to £2500 for most trusts.

Gains to be taxed at marginal rates of income tax (ie either 25 per cent or 40 per cent) as if marginal slice of income.

Retirement relief extended to half of gains between present full retirement relief limit of £125,000 and £500,000.

Retirement relief extended to half of gains between present full retirement relief limit of £125,000 and £500,000.

(xiii) Independent taxation and marriage

Major reform of taxation of husband and wife giving privacy and independence to married women from earliest practicable date of April 1990.

Husbands and wives to be given full independence in their own tax affairs.

Each partner to have own annual Capital Gains Tax threshold (transfers between spouses to remain entirely tax free).

(xiv) Inheritance Tax (IHT)

Threshold up from £90,000 to £110,000 (from 15 March 1988).

Present four rates replaced by a flat rate of 40 per cent.

(xv) Corporation Tax (CT)

Main CT rate of 35 per cent unchanged.

Small companies' rate of CT - down from 27 per cent to 25 per cent.

Advance Corporation Tax (ACT) rate reduced in line with basic income tax rate.

Tax on pre-1982 capital gains abolished.

(xvi) Business Expansion Scheme (BES)

BES to be targetted on smaller companies by new £500,000 limit on total amount of investment in a company in any 12 month period (£5 million for ship chartering companies)

BES extended to individuals investing in companies specialising in letting houses or flats on assured tenancies: relief available to 1993 with a limit on total investment in a company of £5 million in any 12 month period.



(xvii) Stamp duties

One per cent Capital Duty on share issues - abolished.

0.25 per cent Unit Trust Instrument Duty on property put into unit trusts - abolished. No change to main Stamp Duty and Stamp Duty Reserve Tax rates.

(xviii) Business entertainment

The exception to the direct tax rules which allows expenditure on the entertainment of, or gifts to, overseas customers to be allowable for tax, to be removed (from 15 March 1988). Similar exception to VAT rules for expenditure of overseas customers to be removed (from 1 August 1988).

(xix) Company migration

Requirement for Treasury consent to company migration abolished. New test of company residence based upon incorporation in UK. Companies not incorporated here will continue to be resident if centrally managed and controlled in UK. Companies which migrate from UK to pay tax on accrued gains.

(xx) North Sea

A number of changes include a new regime for Southern Basin and on-shore fields: will mean end to royalties for all future (ie post-1982) oil and gas fields.

(xxi) Building societies

Package of measures designed to eliminate unintended tax obstacles for societies wishing to convert from mutual status to become public limited companies (Plcs).

(xxii) Lloyd's

Arrangements for assessment and collection of tax from Lloyd's members to be reformed and simplified.

- 6 -

2. DIRECT REVENUE EFFECTS OF BUDGET MEASURES

£ million	Change from non- indexed base	Change from indexed base
Income tax: allowance	s -1530	- 765
basic rate	-2570	-2570
higher rat	es -1025	- 965
Excise Duties	+ 575	+ 20
Other changes	+ 275	+ 295
	-4275	-3985

1988-89

3. PUBLIC SECTOR FINANCES (PSBR)

. . . .

The public sector borrowing requirement (PSBR) set at minus £3 billion (ie net repayment) in 1988-89 equal to minus $\frac{3}{4}$ per cent of GDP. 1987-88 outturn expected to be net repayment of £3 billion, minus $\frac{3}{4}$ per cent of GDP.

PSBR for rest of Medium Term Financial Strategy period up to 1991-92 assumed to be zero (or borrowing of 1 per cent of GDP if privatisation proceeds are excluded).