

PO-CH/NL/0729 PART A

2/3

SECRET



FROM: CATHY RYDING  
DATE: 2 January 1987

MR KNOX - C&amp;E

cc: Chief Secretary  
Financial Secretary  
Economic Secretary  
Minister of State  
Sir P Middleton  
Sir T Burns  
Mr Cassell  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr Tyrie  
Mr Ross Goobey  
PS/IR  
PS/C&E

CR  
to  
KNOX  
2/1

**BUDGET 1987: EXCISE DUTIES**

The Chancellor was grateful for your minute of 18 December.

2. In your paragraph 10, the Chancellor has noted that you say that on past form the tobacco companies will raise their prices in the New Year. He has commented that on the contrary, they appear to be planning to reduce them. The Chancellor agrees with your comment that, other things being equal, we should take as our objective the need to keep as close as possible to 55 per cent, if necessary by increasing the ad valorem rate.

3. The Chancellor found the arguments for revalorising the duty on cigars in your paragraph 14 unconvincing.

4. On your paragraph 18, the Chancellor would be grateful to know if lorry VED is to be included in the RPI. He has noted that the impact effect of including derv in the RPI from January is likely to be negligible, but he thinks that we still need to know what the effect will be.



5. On your paragraph 19, the Chancellor wonders whether the increases in the pump price duty of derv are too much. He has commented that they should not be as part of a switch.

6. On the section on alcoholic drinks, the Chancellor has commented that the problem is beer: we have to start with that, and then wine and cider follow beer. He thinks it is doubtful if it is worth increasing spirits at all, although they could be the same as beer. In any event a revenue shortfall is in prospect, and he wonders what it would be and how it would be made up - cigarettes?, petrol?, not at all?

CR

CATHY RYDING

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CR

CATHY RYDING

CONFIDENTIAL



FROM: S P Judge

DATE: 7 January 1987

MR B H KNOX - C&E

cc PS/Chancellor

Mr Scholar

Miss Sinclair

PS/Customs & Excise

PS/MST  
To  
KNOX  
7/1

**1987 FINANCE BILL: CUSTOMS AND EXCISE STARTERS**

The Minister of State has seen your submission of 18 December, and agreed the following action on the remaining "minor starters".

No 25 (abolition of match a mechanical lighter duties): drop.

No 24 (marine diesel oil duty): keep for the moment. The Minister agrees that there is a strong case against going the full distance, but thinks that a modest increase in the duty, relative to other fuel duties, would be attractive (especially if those who pay consider themselves let off lightly). He wonders if this would have legislative complications? Of course it may be that the sums at stake (less than £5 million) mean that the hassle is not worth it.

No 15 (VAT powers to appropriate receipts): drop.

No 19 (repayment of import VAT to EC traders): retain.

No 13 (VAT motoring expenses), No 16 (VAT supply liability), No 18 (VAT registration of overseas traders): the Minister is inclined to leave them in, especially 13. I think he might be persuaded to drop 13 if you thought that, by converting an extra-statutory concession into a statutory one, businesses would be more likely to take advantage of it. An estimate of the revenue at risk here would be useful.

Nos 20 and 22 (restructuring of wine duties): see my separate minute of 29 December to Mr Jefferson Smith, which I understand he will be replying to shortly.

in box in  
own folder  
Folder

S.P.J.

S P JUDGE  
Private Secretary

BUDGET SECRET

Table 1: CHANGE IN REAL VALUE OF THE DUTIES: 1979-1987

		Level of duty May 1979	Level of duty post-87 Budget	Real change %(1)
Beer	p/pint	7.5	18.1	31.0
Table Wine	p/70cl	50.0	68.6	-25.5
Spirits	£/75cl	3.13	4.73	-17.9
Tobacco(2)	p/20 KS	23.5	61.2	41.4
Petrol	p/gal	30.0	88.10	59.5
Derv	p/gal	35.0	74.51	15.6
VED	£/car	50.00	100.00	8.6
-----				
ALL DRINKS	(3)			6
ALL TOBACCO	(4)			40
-----				
ALL DUTIES	(5)			32
-----				

(1) Based on RPI from April 1979 (last full month of Labour Govt.) to January 1987 (latest available).

(2) Based on specific duty only: August 1979 figure used because duty restructured.

(3) Beer, all types of wines, spirits and cider.

(4) Cigarettes and minor tobacco duties.

(5) All shown above plus other wines, cider, and minor tobacco duties.

BUDGET SECRET

Table 1A: CHANGE IN REAL VALUE OF THE DUTIES including VAT: 1979-1987

	Notes		Level of duty + VAT May 1979 (See Note 1)	Level of duty + VAT post-87 Budget (1)	Real change % (See Note 2)
Beer	(3)	p/pint	8.1	20.8	39.5
Table Wine	(3)	p/70cl	54.0	78.9	-20.7
Spirits	(3)	£/75cl	3.38	5.44	-12.6
Tobacco	(3)&(4)	p/20 KS	25.4	70.4	50.6
Petrol	(5)	p/gal	33.7	101.31	63.0
Derv	(3)&(6)	p/gal	37.8	85.69	23.1
VED	(7)	£/Car	50.00	100.00	8.6
-----					
ALL DRINKS	(8)				13
ALL TOBACCO	(9)				49
-----					
ALL DUTIES	(10)				38
-----					

Notes

- (1) Includes VAT on the duty only, not total VAT on the good as that would depend on the total price.
- (2) Based on RPI from April 1979 (last full month of Labour Govt.) to January 1987 (latest available).
- (3) Rate of VAT 8% in May 1979, 15% in 1987.
- (4) Based on specific duty only: August 1979 figure used because duty restructured.
- (5) Rate of VAT 12.5% in May 1979, 15% in 1987.
- (6) Most users able to reclaim VAT.
- (7) VAT not chargeable on VED.
- (8) Beer, all types of wines, spirits and cider.
- (9) Cigarettes and minor tobacco duties.
- (10) All shown above plus other wines, cider, and minor tobacco duties.



BUDGET SECRET

Table 2: CHANGE IN REAL VALUE OF THE DUTIES: 1979-1983

		Level of duty May 1979	Level of duty June 1983	Real change %(1)
Beer	p/pint	7.5	15.1	29.2
Table Wine	p/70cl	50.0	79.1	1.5
Spirits	£/75cl	3.13	4.56	-6.5
Tobacco(2)	p/20 KS	23.5	43.3	18.2
Petrol	p/gal	30.0	74.10	58.5
Derv	p/gal	35.0	62.8	15.1
VED	£/Car	50.00	85.00	9.1
-----				
ALL DRINKS (3)				12
ALL TOBACCO (4)				18
-----				
ALL DUTIES (5)				27
-----				

(1) Based on RPI from April 1979 (last full month of Labour Govt.) to May 1983 (last full month of first Conservative Govt.).

(2) Based on specific duty only: August 1979 figure used because duty restructured.

(3) Beer, all types of wines, spirits and cider.

(4) Cigarettes and minor tobacco duties.

(5) All shown above plus other wines, cider, and minor tobacco duties.

BUDGET SECRET

Table 2A: CHANGE IN REAL VALUE OF THE DUTIES including VAT: 1979-1983

Notes		Level of duty + VAT May 1979 (See Note 1)	Level of duty + VAT June 1983 (1)	Real change % (See Note 2)
Beer (3)	p/pint	8.1	17.4	37.8
Table Wine(3)	p/70cl	54.0	91.0	8.1
Spirits (3)	£/75cl	3.38	5.24	-0.5
Tobacco (3)&(4)	p/20 KS	25.4	49.8	25.9
Petrol (5)	p/gal	33.7	85.21	62.0
Derv (3)&(6)	p/gal	37.8	72.22	22.6
VED (7)	£/car	50.00	85.00	9.1
-----				
ALL DRINKS (8)				19
ALL TOBACCO (9)				26
-----				
ALL DUTIES (10)				32
-----				

Notes

- (1) Includes VAT on the duty only, not total VAT on the good as that would depend on the total price.
- (2) Based on RPI from April 1979 (last full month of Labour Govt.) to May 1983 (last full month of first Conservative Govt.)
- (3) Rate of VAT 8% in May 1979, 15% in 1987.
- (4) Based on specific duty only: August 1979 figure used because duty restructured.
- (5) Rate of VAT 12.5% in May 1979, 15% in 1987.
- (6) Most users able to reclaim VAT.
- (7) VAT not chargeable.
- (8) Beer, all types of wines, spirits and cider.
- (9) Cigarettes and minor tobacco duties.
- (10) All shown above plus other wines, cider, and minor tobacco duties.

BUDGET SECRET

Table 3: CHANGE IN REAL VALUE OF THE DUTIES: 1983-1987

		Level of duty June 83	Level of duty post-87 Budget	Real change %(1)
Beer	p/pint	15.1	18.1	1.5
Table Wine	p/70cl	79.1	68.6	-26.6
Spirits	£/75cl	4.56	4.73	-12.2
Tobacco(2)	p/20 KS	43.3	61.2	19.6
Petrol	p/gal	74.1	88.10	0.6
Derv	p/gal	62.8	74.51	0.4
VED	£/car	85.00	100.00	-0.4
-----				
ALL DRINKS	(3)			-7
ALL TOBACCO	(4)			18
-----				
ALL DUTIES	(5)			3
-----				

(1) Based on RPI from May 1983 (pre-Election) to January 1987 (latest available)

(2) Based on specific duty only.

(3) Beer, all types of wines, spirits and cider.

(4) Cigarettes and minor tobacco duties.

(5) All shown above plus other wines, cider, and minor tobacco duties.

BUDGET SECRET

Table 4: CHANGE IN REAL VALUE OF THE DUTIES: 1974-1979

Because of the many changes in the structure of taxes over this period, these figures should be treated with caution.

	Notes	Units	Level of duty Feb 1974	Level of duty May 1979	Real change % (Note 1)
Beer		p/pint	3.1	7.5	13
Table Wine	(2)	p/70cl	12.7	50.0	84
Spirits	(3)	£/26.75fl.oz	1.8025	3.1605	-18
Tobacco	(4)	p/20 KS	17.0	35.1	-4
Petrol	(5)	p/gal	22.5	30.0	-38
Derv	(5)	p/gal	22.5	35.0	-27
VED		£/car	25.00	50.00	-7
ALL DRINKS	(2) & (8)				7
ALL TOBACCO	(4) & (9)				-4
ALL DUTIES	(10)				-10

BUDGET SECRET

Table 4A: CHANGE IN REAL VALUE OF THE DUTIES including VAT: 1974-1979

	Notes	Units	Level of duty + VAT Feb 1974	Level of duty + VAT May 1979	Real change % (Note 1)
Beer	(6)	p/pint	3.4	8.1	11
Table Wine	(2) & (6)	p/70cl	14.0	54.0	80
Spirits	(3) & (6)	£/26.75fl.oz	2.0	3.4	-20
Tobacco	(4) & (6)	p/20 KS	18.7	37.9	-5
Petrol	(5)	p/gal	22.5	33.7	-30
Derv	(5)	p/gal	22.5	37.8	-22
VED	(7)	£/car	25.0	50.0	-7
ALL DRINKS	(2) & (8)				5
ALL TOBACCO	(4) & (9)				-6
ALL DUTIES	(10)				-9

BUDGET SECRET

NOTES

- (1) Based on RPI from January 1974 (last full month of the Conservative Govt.) to April 1979 (last full month of Labour Govt.)
- (2) During this period, wine duty affected by alignment to EC Common Tariff and was restructured in 1976 - so comparison only approximate.
- (3) 1979 figure differs slightly from that used in 1979-1987 comparisons because unit changed from £ per 75cl at 40% alcohol by volume to £ per 26.75 fluid ounces at 70 degrees proof.
- (4) Tobacco duty restructured in 1976. Comparison based on estimated total duty payable on King Size, being the most popular type at end of period but not at start. Results very sensitive to assumptions.
- (5) At beginning of period road fuels were not subject to VAT but later petrol was subject to VAT up to 25% and was charged at 12.5% at the end of the period. For derv this is less of problem as most derv users are able to reclaim VAT. Also during this period, duties affected by alignment to the EC Common Tariff.
- (6) Rate of VAT 10% in February 1974, 8% in May 1979.
- (7) VAT not chargeable on VED.
- (8) Beer, table wine and spirits only. (Cider duty not introduced until 1976 and other wines too affected by 1976 restructuring to make valid comparisons.)
- (9) Cigarettes and minor tobacco duties.
- (10) All shown above plus minor tobacco duties.

~~CONFIDENTIAL~~



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

~~BP 16/1~~

JEFFERSON  
SMITH  
TO  
MST  
8/1

*Handwritten signature in red ink*

FROM: P JEFFERSON SMITH

DATE: 8 January 1987

*Handwritten initials 'PJP'*

Minister of State

cc **Chancellor**  
Chief Secretary  
Financial Secretary  
Economic Secretary  
Mr Scholar  
Miss Sinclair  
Mr Cropper

*Ch*  
*Minor point for when we discuss raise duty revalorisation @ overns meet - Monday*

*AA*  
*When psc will be f rank cut in*

**REVIEW OF THE STRUCTURE OF WINE AND MADE-WINE DUTIES (STARTER NO 20)**

1. Your Private Secretary's minute of 29 December recorded your views on my submissions of 6 November and 2 December.
2. You asked what would be the implications for the revised wine duties of non- or under-revalorisation of beer duty. The answer is that the proposals would still work. They postulated that on top of an increase on table wine for example of 4p a bottle, fortified wines of 13-15% alcohol would go up another 4p; stronger fortified wines, which would include port as well as Spanish sherry, would go down by 4p - ie +4p for revalorisation offset by -8p for restructuring.

Internal circ: CPS, Mr Knox, Solicitor, Mr Butt, Mr Whitmore, Mr Wilmott, Mr Breuer, Mr Fotherby, Mrs Hamill, Mr Tullberg.

# CONFIDENTIAL

3. Thus, the restructuring element of any duty change would bring down the stronger wines by twice as much as the wines in the 13-15% category went up. The advantages would be:

- it would lead in the right direction to produce a less distorted duty structure;
- the advantage to Spanish sherry would be greater than the disadvantage to British and Cyprus sherry; but
- because of the relative market shares, the change would be roughly revenue neutral.

4. The magnitude of the change must be influenced not only by the view that the present duty differential is too great, but also by a view of what a reasonable future structure might be. There is no need to take a definite decision on this, since the duties must be reviewed each year. But one possibility is that the duty should progress by reference to strength. Taking as reference points the top strength in each band, the duty for the 13-15% band should be 15/13ths of the duty on light table wine. Table 1 shows in percentage terms the present differentials, the differentials on a scale proportionate to strength, and the differential which would obtain from putting 4p a bottle on 13-15% wines and taking 8p a bottle off stronger wines. It will be seen that these figures would move about a third of the way to a proportionate scale, which as a first step would seem about right.



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5. Table 2 shows the changes in pence per bottle on various assumptions about revalorisation (the previous over-revalorisation option is included in column (5) for reference purposes). Any of the columns seems to us to produce figures which would be a reasonable gesture towards Spanish sherry while limiting the damage to Cyprus, British sherry or vermouths but giving a firm signal.

6. You also asked whether we consider it necessary to consult the Law Officers before reversing the 1985 ban on duty-paid blending of wine. In the paper accompanying my minute of 6 November I suggested that we should consult the Law Officers, but this was in the context of reversal as a sufficient answer on its own to the Spanish sherry producers' complaint. The objective of reversal as part of a "first step" option would be to make a gesture which could be sufficient to put the Spanish sherry producers off taking any further action, or at least to muddy the waters sufficiently to force them to work up a new case against a substantially different situation. We do not expect an early reference to the European Court and it is therefore not essential to consult the Law Officers at this stage. Moreover, it is doubtful whether it would be helpful to ask the Law Officers to give advice when we are contemplating moving the goal posts so far and do not know what, if any, line of attack the Spanish might adopt as a result.

7. We will consult MAFF, DTI and the FCO about the proposed changes to the duty structure. We would also be grateful for authority to discuss the implications of our proposals for a "per degree" duty on low-strength mixed drinks with the trade (para 14 of my minute of 6 November refers).

Ph ←

P JEFFERSON SMITH

**CONFIDENTIAL**

From: P TREVETT

Date: 9 January 1987

*Papers  
Pse  
PWP*



HM CUSTOMS AND EXCISE  
VAT CONTROL DIVISION D  
ALEXANDER HOUSE 21 VICTORIA AVENUE  
SOUTHEND-ON-SEA X SS99 1AJ  
TELEPHONE SOUTHEND-ON-SEA (0702) 348944 ext

Minister of State

cc **Chancellor**  
Chief Secretary  
Financial Secretary  
Economic Secretary  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr Graham

**FINANCE BILL 1987 STARTER NO 16**

**SELF BILLING: LIABILITY OF SUPPLY TO BE THE RESPONSIBILITY OF PERSON ISSUING THE TAX INVOICE**

1. This note is further to Mr Knox's of 18 December, and details why this starter had been put forward and why we do not wish to proceed with it in the 1987 Finance Bill. The purpose of this measure would be to provide that where a taxable person issues himself with a tax invoice, in place of the supplier, he would be responsible for the liability of the tax on that supply.

Background

2. The problem concerns self billing, a procedure which allows the customer to make out the suppliers tax invoice, usually because the value of the supply was not known at the time the supply was made. It is a long standing commercial practice which precedes VAT and was allowed to continue on the introduction of the tax.

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Internal distribution:

CPS	Mr Butt
Mr Knox	Mr McFarlane
Mr Howard	Mr Holloway
Mr Jefferson Smith	

3. We have always had control problems with self billing in ensuring, for example, that a supplier accounts to us for the output tax paid to him by the customer and that a customer keeps an up to date record of the VAT status of his suppliers. This year we have encountered a new problem in the construction industry, where self billing is used extensively.

#### The problem

4. It is now common practice to include in new houses items such as washing machines, refrigerators (white goods), fitted carpets etc, all of which are liable to VAT at 15%. The new house is, of course, zero rated, but to ensure that VAT is paid on these items of normal consumer expenditure the law provides that the housebuilder cannot take deduction of input tax when they are included in the sale of a new house. In one particular case a major national building company self billed for such consumer items, showing the tax liability to be at the zero rate. The result has been a tax loss of some £250,000.

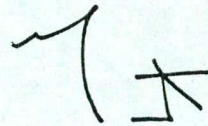
#### Legal position

5. Under section 2(3) of the VAT Act 1983 the responsibility for the tax on any supply is a liability of the person making the supply. The building company has argued, and our legal advisers support his view, that the liability for the tax on which he has self billed rests with his suppliers. Although we have the power to assess the suppliers (sub contractors) the exercise would not be practicable, nor cost effective, as this builder employs many hundreds, if not thousands of sub contractors. We are unable to assess the trader as he has not underdeclared his output tax, nor overclaimed his input tax.

6. A trader is allowed to provide himself with, in effect, a tax invoice (which determines the tax point or time of supply) under section 5(4) of the VAT Act, but although regulation 12(3) of the VAT (General) Regulation 1985 stipulates the content of the document, it does not enable us to hold the trader (self biller) concerned responsible for the correct tax liability of the supplies involved. Furthermore although we impose conditions on traders approved for self billing, we have no vires for doing so. Correct liability is not one of those conditions and even if it were it would be seen as overriding primary legislation and therefore be ultra vires.

Conclusion

7. The problem we have identified with this one builder may be isolated, but we are making enquiries to establish whether similar problems exist with other builders. These enquiries have yet to be completed and we do not think it appropriate to legislate this year. There is, however, a loophole which should be blocked and the method we propose, to make the self biller responsible for the correct tax liability, should further reduce the burdens of VAT accounting on smaller businesses. This is because the self biller is usually a large company with expert accounting staff well versed in areas of complicated liability, whereas his suppliers are frequently small firms with few, if any accounting staff. We would therefore propose to bring this starter forward in 1988 when in the context of Keith III we shall be bringing forward other starters to assist small businesses (Mr Howards note of 18 December 1986).



P TREVETT

WINE AND  
MADE-WINE DUTIES

PS/MST  
JEFFERSON  
SMITH  
91

CONFIDENTIAL



FROM: S P Judge  
DATE: 9 January 1987

MR JEFFERSON SMITH - C&E

cc PS/Chancellor  
PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
PS/Customs & Excise

REVIEW OF THE STRUCTURE OF WINE AND MADE-WINE DUTIES (STARTER No 20)

The Minister of State has seen your submission of 8 January. He is entirely content for you to consult with the trade about the proposals for a "per degree" duty on low-strength mixed drinks ("coolers"). I am sorry I did not cover this point in my note of 29 December to you.

S P JUDGE  
Private Secretary



SECRET CONFIDENTIAL

H.M. CUSTOMS AND EXCISE  
KING'S BEAM HOUSE, MARK LANE  
LONDON EC3R 7HE

~~01-626 1515~~  
382 5101

FROM: W F McGUIGAN

DATE: 15 January 1987

1 A/C  
all  
min of meeting  
W F

Minister of State

cc PS/Chancellor  
PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Romanski  
Mr Cropper  
Mr Ross Goobey  
Mr Tyrie

### BUDGET MEETING : THE JOCKEY CLUB

I attach briefing for your meeting with the Jockey Club on 20 January 1987.

The deputation will seek abolition of the on-course betting duty. A full brief in standard format has been provided although, of course, a decision has already been taken to abolish the on-course duty in the forthcoming Budget.

I shall be available for support.

W F McGUIGAN

---

Internal circ: CPS, Mr Jefferson Smith, Mr Heron, Mr Knox, Mr Wilmott,  
Mr Bone.

## MINISTER OF STATE'S MEETING WITH THE JOCKEY CLUB DEPUTATION ON 20 JANUARY 1987

### ORGANISATION

The deputation will be led by **Lord Fairhaven, Senior Steward of the Jockey Club** and **Mr Christopher Foster, Secretary.**

They will be accompanied by:-

- (a) **Sir Ian Trethowan, Chairman of the Horserace Betting Levy Board.** The Levy Board provides substantial financial support (about £20 m pa) to the racing industry from income mainly derived from the levy on off-course bookmakers' turnover.
- (b) **Sir Nevil Macready, Chairman of the Horseracing Advisory Council,** an umbrella organisation financed by the Levy Board which formulates policy and provides channels of communication between the racing authorities and the many different sectors of the industry.

### OBJECT OF MEETING

The **deputation will seek abolition of the on-course betting duty.** The meeting has been requested by Lord Fairhaven, Senior Steward of the Jockey Club, who seeks to amplify the representations made in the Jockey Club letter of 25 November 1986. The Horseracing Advisory Council submitted a memorandum to the Chancellor on 12 December supporting the Jockey Club's representations. The National Association of Bookmakers also wrote in support of the Jockey Club's representations by their letter dated 8 December.

### SUMMARY OF WRITTEN REPRESENTATIONS

#### JOCKEY CLUB

The Jockey Club has long sought abolition of the on-course duty. They are now particularly concerned that the daily live television service from tracks to betting shops to be introduced in early 1987 will reduce racecourse attendances and weaken the on-course betting market which sets the starting prices for off-course betting. They

claim that whereas off-course turnover has been stimulated recently by allowing television and refreshments to be provided in betting shops, on-course turnover has fallen during the same period. They argue that improvements to racecourse facilities and duty free on-course betting would enable the industry to compete with other spectator sports and the off-course betting competition, which would in turn strengthen the on-course betting market on which off-course turnover, betting levy, and the bulk of the duty yield, depends. Finally they say that abolition would remove the problem of how to curb illegal on-course betting and they urge help for the on-course market if only to safeguard off-course betting and the duty yield.

### **HORSERACING ADVISORY COUNCIL**

The HAC supports the Jockey Club case and basically puts forward the same arguments for abolition, including competition from off-course betting, the recent fall in turnover and illegal betting.

### **NATIONAL ASSOCIATION OF BOOKMAKERS**

The NAB also supports the Jockey Club case and stresses the importance of strengthening the on-course market by attracting more spectators to bet at the courses. They argue that on-course turnover will be adversely affected by live television coverage and that a weak starting price market can only result in off-course bettors losing confidence in the system to the detriment of off-course betting turnover and the duty yield. They claim that abolition or even reduction of the on-course duty is necessary to increase racecourse attendances, strengthen the on-course market, and stimulate off-course betting.

### **BACKGROUND INFORMATION**

The current duty rates are 4% of stakes for on-course bets and 8% for off-course bets. The differential, which recognises the importance of the on-course market in determining starting price odds, was introduced in 1970 when the general rate was 5%. The last increase in the off-course rate from 7.1/2% - 8% took place in 1981. On-course duty was reduced from 5% to 4% in 1972.



## GENERAL BETTING DUTY RECEIPTS

(Forecast 1986/87)	On-course	£ 20 m
	Off-course	<u>£320 m</u>
	TOTAL	£340 m
Turnover (Forecast 1986/87)	On-course	£ 500 m
	Off-course	<u>£4000 m</u>
	TOTAL	£4500 m

On-course betting accounts for less than 6% of total revenue and around 11% of total turnover.

### POINTS LIKELY TO BE RAISED

**Turnover.** The Jockey Club in arguing for abolition will claim that off-course turnover has grown by around 7% since television was allowed in betting shops in March 1986 whereas on-course turnover has fallen by 5% in the same period. They argue that the resultant increase in revenue (around £20 m) will compensate for any duty lost by the abolition of on-course duty. They fear that this trend will continue unless racing receives some measure of duty relief. However, their on-course turnover figures, although based on Customs and Excise duty statistics, are misleading. On-course bookmakers were transferred from weekly to monthly duty payments from 30 March 1986 with a resultant duty deferment of some £0.6 m from this financial year to 1987/88. When this is taken into account duty and turnover have remained at the same level as last year in money terms but have fallen in real terms. Off-course duty has risen by just under 7% in money terms in the same period. In recent years turnover has fallen in real terms both on and off-course, with on-course turnover falling faster despite the fact that duty increases were confined to off-course betting.

**Attendances.** In arguing for abolition the deputation may refer to increases in attendances and betting turnover following the 1972 duty reduction. However, there were also increases in attendances in 1971 and in 1980, years when there was no duty change, and attendances have fallen in other years despite unchanged rates.

**Sunday Racing.** The Jockey Club complain that, unlike competing sports, they are unable to hold their main fixtures on Sundays when there is a high level of demand from the public for leisure opportunities. The Jockey Club and the Horserace Totalisator Board have persistently advocated Sunday racing as a remedy for declining track attendances. The main obstacles to Sunday racing are religious opposition and the question of whether Sunday betting should be legalised. The Jockey Club favour legalising off-course betting on Sundays in addition to on-course betting if this means allowing Sunday racing. They may take this opportunity to press their case for Sunday racing with the Treasury. The decision is essentially one for the Home Office and they are in the lead in discussions.

**Illegal betting.** They will argue that the incidence of illegal on-course betting is increasing and that the problem would be removed by abolition of on-course betting duty. The Betting Office Licencees Association (BOLA) argues, however, that illegal bookmakers, operating without overheads, would continue to operate outside that market; and a duty differential of 10% (including levy deductions) between on and off-course would be an incentive to represent off-course transactions as on-course business. They would now not oppose abolition of on-course betting, provided Customs continue to control on-course bookmakers.

#### **POINTS TO BE RAISED**

No points of substance.

The deputation could be asked whether they see the danger of off-course bets being represented as on-course bets to be an obstacle to abolition.



*For who help the business? Has much for us to raise? The Gov/MSD control: how big? cigs?*

*Page 1 of 27*

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

Copy No 1 of 27

KNOX  
To  
C/EX  
15/1

From: B H KNOX  
Date: 15 January 1987

CHANCELLOR

cc  
Chief Secretary  
Financial Secretary  
Economic Secretary  
Minister of State  
Sir P Middleton  
Sir T Burns  
Mr F E R Butler  
Sir G Littler  
Mr Cassell  
Mr Monck  
Mr A Wilson  
Mr Sedgwick  
Mr Scholar  
Mr Odling Smee  
Miss Sinclair  
Miss Evans  
Mr Cropper  
Mr Tyrie  
Mr Ross Goobey  
PS/Inland Revenue

Ch  
Also below are  
① papers on partial exemption & brewers  
② review of structure of made-wine  
- you asked to be recommended to raise  
VED & fuel duties papers separated below  
under

EXCISE DUTIES

This note updates my submissions of 18 December and 8 January in the light of the year-on-year RPI figure for December 1986. It gives the revenue implications of precise revalorisation for all the main excise duties, as well as an illustrative package taking account of preferences which you expressed both before and at Chevening. There is a revised ready-reckoner in the annex. FP Division are minuting you separately about the balance of motoring taxation.

Internal distribution: CPS, Mr Jefferson Smith, Mr Wilmott, Mr Bone, Mrs Hamill

RESTRUCTURING OF  
THE WINE AND MADE-WINE  
DUTIES

BUDGET SECRET

Copy 2 of 10  
PUD

BARNES  
→ PS/MST  
13/3



FROM: P D P BARNES

DATE: 13 MARCH 1987

PS/MINISTER OF STATE

cc PS/Chancellor  
PS/Chief Secretary  
PS/Financial Secretary  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr Jefferson-Smith C&E

*1 agm*

RESTRUCTURING OF THE WINE AND MADE-WINE DUTIES

The Economic Secretary has seen Mr Jefferson-Smith's submission to the Minister of State of 12 March.

2. The Economic Secretary thinks that as a matter of principle we ought not to have arranged PQs tabled before the Budget on Budget matters.

*h*

P D P BARNES  
Private Secretary

# BUDGET SECRET

2. The revalorisation factor is 3.7 per cent. Revalorisation across the board produces the following results:

## REVALORISATION AT 3.7%

	Price change including VAT on typical item (1)	Yield (2)		RPI impact effect (4) %
		1987-88 (3) £m	1988-89 £m	
Beer	0.8p per pint	65	70	0.04
Cider	0.4p per pint	neg	neg	neg
Wine - table wine	2.9p per 70 cl	15	15	0.02
- sherry	5.0p per 70 cl )	5	5	neg
- port	5.8p per 70 cl )			
Spirits	20.1p per 75 cl	25	30	0.03
Tobacco - cigarettes (5)	3.4p per 20 KS	90	100	0.1
- pipe	2.7p per 25 gram	neg	neg	neg
- cigars	1.9p per 5 whiffs	5	5	nil
Petrol	3.7p per gallon	185	205	0.09
Derv (6)	3.2p per gallon	40	45	(see note 7)
VED - cars	£3.70 per year	75	80	0.03
- other		20	20	nil
Minor duties (8)		5	5	neg
<b>TOTAL</b>		<b>530</b>	<b>580</b>	<b>0.31</b>

(1) VAT payable in addition to the duty except in the case of VED.

(2) Rounded to nearest £5 million.

(3) Assuming mid-March Budget.

(4) Rounded to 2 decimal places. Total ignores "neg" entries.

(5) Includes hand-rolling tobacco.

(6) Most derv consumers can reclaim VAT.

Revenue estimates assume 9% offset for bus fuel grants.

(7) The RPI weight for Derv is not yet known, but impact effect likely to be negligible.

(8) Minor oils, matches and mechanical lighters, gaming machine licences.

# BUDGET SECRET

# BUDGET SECRET

3. A drinking and smoking package similar to that in my submission of 8 January (ie standstill on spirits, under-indexation of remaining drinks, standstill on cigars and pipe tobacco, all balanced by over-indexation of cigarettes) is set out below. The overall RPI impact effect is to all intents the same as if each component of the package had been precisely revalorised. Variants may be constructed by using the building-blocks in the annex.

	REVALORISATION 3.70%		PACKAGE 3.0%, EXCEPT <del>SPIRITS</del> <sup>CIDER</sup> , PIPE TOBACCO AND CIGARS, OFFSET BY CIGARETTES		SCORECARD <i>ie diff betwee first two</i>	
	1987-88	1988-89	1987-88	1988-89	1987-88	1988-89
<b>ALCOHOL</b>						
Beer	65	70	50	55	-15	-15
Cider	neg	neg	neg	neg	nil	nil
Spirits	25	30	<del>20</del>	<del>25</del>	-25	-30
Wine	20	20	15	15	-5	-5
Total	110	120	<del>65</del> 85	<del>70</del> 95	-45	-50
<b>TOBACCO</b>						
Cigarettes	90	100	<del>120</del> 140	<del>130</del> 155	<del>30</del> 50	<del>30</del> 55
Cigars and Pipe Tobacco	5	5	0	0	-5	-5
TOTAL	205	225	205	225	0	0

*7 w/1 on cigs*

*32 on spirits, plus  
'Spirits' 20/25,  
incl cigs 120/130*

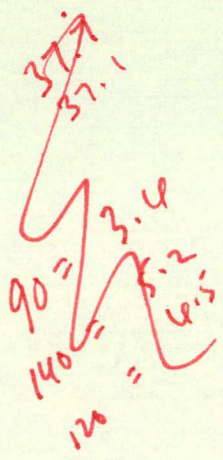
PRICE INCREASES IN PENCE

	REVALORISATION (3.7%)	PACKAGE
Beer (per pint)	0.8	0.6
Cider (per pint)	0.4	0.3
Spirits (per 75 cl)	20.1	nil
Wine (per 70 cl)	2.9	2.4
Cigarettes (per 20 KS)	3.4	5.2
		(Duty increase = 5.6%)
Cigars (per 5 whiffs)	1.9	nil
Pipe Tobacco (per 25 grams)	2.7	nil

*plus 4.5*

*Bryce Knox*

B H KNOX



## ALL SPECIFIC DUTIES INCREASES BY 1%

	Price change including VAT VAT on typical item (1)	Yield		RPI impact effect (3) %
		1987-88 (2) £m	1988-89 £m	
Beer	0.2p per pint	17	19	0.01
Cider	0.1p per pint	neg	neg	neg
Wine - table wine	0.8p per 70 cl	5	5	0.01
- sherry	1.4p per 70 cl )	neg	neg	neg
- port	1.6p per 70 cl )			
Spirits	5.4p per 75 cl	7	8	0.01
Tobacco - cigarettes (4)	0.9p per 20 KS	26	28	0.03
- pipe	0.7 per 25 gram	neg	neg	neg
- cigars	0.5p per 5 whiffs	neg	neg	nil
Petrol	1.0 per gallon	51	56	0.02
Derv (5)	0.9p per gallon	13	14	(see note 6)
VED - cars	£1.00 per year	21	21	0.01
- other		5	5	nil
Minor duties (7)		1	1	neg
TOTAL		146	157	0.09

(1) VAT payable in addition to the duty except in the case of VED.

(2) Assuming mid-March Budget.

(3) Rounded to 2 decimal places. Total ignores "neg" entries.

(4) Includes hand-rolling tobacco.

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Revenue estimates assume 9% offset for bus fuel grants.

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(7) Minor oils, matches and mechanical lighters, gaming machine licences.





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

FROM: B H KNOX

DATE: 8 January 1987

CHANCELLOR

*9/ Answering KNOX  
 washers on C&E paper  
 See also M&S's comments  
 on minor clerical errors*

cc: Chief Secretary  
 Financial Secretary  
 Economic Secretary  
 Minister of State  
 Sir P Middleton  
 Sir T Burns  
 Mr Cassell  
 Mr Scholar  
 Miss Sinclair  
 Mr Cropper  
 Mr Tyrie  
 Mr Ross Goobey  
 PS/Inland Revenue

BUDGET 1987 - EXCISE DUTIES

Cathy Ryding's minute of 2 January recorded your comments on my paper of 18 December. You may find the following clarifications helpful before Chevening.

Tobacco

2. As you noted, since my submission two cigarette companies have announced price cuts for some brands instead of their usual seasonal increases. We have been doing some work on the possible implications for Budget decisions and I am minuting you separately. We have noted your views on cigars.

RPI

3. Lorry VED is not in the RPI, nor are we aware of any plans for it to be included (it is not a normal item of family expenditure). We do not yet know what weight the Department of Employment will finally give to deriv. They will have to decide in the next couple of weeks but all the indications are that it will be small enough for any conceivable increase in the duty to have a negligible impact effect on the RPI.

/4. It may

Internal distribution:

CPS Mr Jefferson Smith Mr Wilmott Mr Bone Mrs Hamill

KNOX  
 to  
 CH/EX  
 8/1

4. It may be useful if I spell out the meaning of 'negligible' here. In our calculations of RPI effects we work to three places of decimals. In our submissions to you these are rounded to two places, with the result that anything with an impact effect of less than 0.005 per cent is scored as negligible. Public presentation of RPI figures is conventionally to one place of decimals.

#### Derv

5. The individual components of the possible increase in pump price for derv are as follows :-

	<u>Pence per gallon</u>		
	<u>Duty</u>	<u>VAT*</u>	<u>Total</u>
Switch from VED (£100m off VED, lorry neutral - ie £125m net yield after bus fuel grants)	8.2	1.2	9.4
Revalorisation	2.4	0.4	2.8
Recoupment from VED non-revalorisation	0.9	0.1	1.0
Totals	<u>11.5</u>	<u>1.7</u>	<u>13.2</u>

\* Most derv users can reclaim VAT

As I said in my submission the UK's derv duty is already very much at the top end of the Community scale. Increases of 12p or 13p are indeed large and can only make such comparisons look worse. However, the point is that the bulk would come from a switch in the burden from the standing charge to the running cost, with the remainder from maintaining the real value of the duty. It is essentially a matter for political judgment whether the shift could be publicly justified.

#### Alcohol

6. A revenue shortfall is in prospect if you are aiming for a revenue yield equivalent to across-the-board revalorisation but wish to under-index one group. Perhaps the first question to be addressed is whether you are in fact seeking such a revenue yield.

/7. If you are,

7. If you are, and if you wish to finance some leniency on drinks, then, as you suggest, cigarettes and/or petrol (though not presumably, in the light of your comments, derv) are the likeliest candidates for over-indexation. A variety of packages can be constructed and we shall be happy to provide them when we have a steer but the following may be a helpful illustration. It combines a stand-still on spirits with under-indexation of the remaining drinks, balanced by over-indexation of cigarettes. The RPI impact effect is similar to revalorisation.

	<u>Revalorisation</u> 3.25%		<u>Package</u> 2.5% except spirits, offset by tobacco		<u>Scorecard</u>	
	1987-88	1988-89	1987-88	1988-89	1987-88	1988-89
Beer	55	60	45	45	-10	-15
Cider	neg	neg	neg	neg	nil	nil
Spirits	25	25	0	0	-25	-25
Wine	15	20	10	15	- 5	- 5
Total drinks	95	105	55	60	-40	-45
Tobacco	85	90	125	135	40	45
Overall totals	180	195	180	195	0	0

PRICE INCREASE IN PENCE

	<u>Revalorisation</u> 3.25%	<u>Package</u> 2.5% except spirits, offset by tobacco
Beer per pint	0.7	0.5
Cider per pint	0.3	0.3
Spirits per 75cl	17.7	nil
Wine per 70cl	2.6	2.0
Cigarettes per 20KS	3.0	4.4 (Duty increase = 4.75%)

Annex A (ii) of my earlier submission gives a ready-reckoner which will enable you to consider variations.

8. As the oil companies have recently announced an increase of about 7p in the pump price of petrol to take effect later this

/month

month, you may feel that, whatever the taxable capacity, you would rather not add arbitrarily to petrol duty. A modest over-indexation of cigarette duty on the other hand might be more politically palatable, though we would not recommend that the balance be skewed too far.

*Bryce Knox*

B H KNOX



MS  
 ✓ PG  
 187

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

Copy No 6 of 27

M/S 15 JAN 1987 - 23

From: B H KNOX  
 Date: 15 January 1987

CHANCELLOR

cc

Chief Secretary  
 Financial Secretary  
 Economic Secretary  
 Minister of State  
 Sir P Middleton  
 Sir T Burns  
 Mr F E R Butler  
 Sir G Littler  
 Mr Cassell  
 Mr Monck  
 Mr A Wilson  
 Mr Sedgwick  
 Mr Scholar  
 Mr Odling Smee  
 Miss Sinclair  
 Miss Evans  
 Mr Cropper  
 Mr Tyrie  
 Mr Ross Goobey  
 PS/Inland Revenue

## EXCISE DUTIES

This note updates my submissions of 18 December and 8 January in the light of the year-on-year RPI figure for December 1986. It gives the revenue implications of precise revalorisation for all the main excise duties, as well as an illustrative package taking account of preferences which you expressed both before and at Chevening. There is a revised ready-reckoner in the annex. FP Division are minuting you separately about the balance of motoring taxation.

---

Internal distribution: CPS, Mr Jefferson Smith, Mr Wilmott, Mr Bone, Mrs Hamill

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REVALORISATION AT 3.7%

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- sherry	5.0p per 70 cl )	5	5	neg
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- (5) Includes hand-rolling tobacco.
- (6) Most derv consumers can reclaim VAT. Revenue estimates assume 9% offset for bus fuel grants.
- (7) The RPI weight for Derv is not yet known, but impact effect likely to be negligible.
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3. A drinking and smoking package similar to that in my submission of 8 January (ie standstill on spirits, under-indexation of remaining drinks, standstill on cigars and pipe tobacco, all balanced by over-indexation of cigarettes) is set out below. The overall RPI impact effect is to all intents the same as if each component of the package had been precisely revalorised. Variants may be constructed by using the building-blocks in the annex.

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	1987-88	1988-89	1987-88	1988-89	1987-88	1988-89
<b>ALCOHOL</b>						
Beer	65	70	50	55	-15	-15
Cider	neg	neg	neg	neg	nil	nil
Spirits	25	30	0	0	-25	-30
Wine	20	20	15	15	- 5	- 5
Total	110	120	65 85	70 95	-45	-50
<b>TOBACCO</b>						
Cigarettes	90	100	120 140	130 155	50	55
Cigars and Pipe Tobacco	5	5	0	0	- 5	- 5
TOTAL	205	225	205	225	0	0

BUDGET SECRET

## PRICE INCREASES IN PENCE

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Beer (per pint)	0.8	0.6
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Spirits (per 75 cl)	20.1	nil
Wine (per 70 cl)	2.9	2.4
Cigarettes (per 20 KS)	3.4	5.2
		(Duty increase = 5.6%)
Cigars (per 5 whiffs)	1.9	nil
Pipe Tobacco (per 25 grams)	2.7	nil

*Bryce Knox*

B H KNOX



## ALL SPECIFIC DUTIES INCREASES BY 1%

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- pipe	0.7 per 25 gram	neg	neg	neg
- cigars	0.5p per 5 whiffs	neg	neg	nil
Petrol	1.0 per gallon	51	56	0.02
Derv (5)	0.9p per gallon	13	14	(see note 6)
VED - cars	£1.00 per year	21	21	0.01
- other		5	5	nil
Minor duties (7)		1	1	neg
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Revenue estimates assume 9% offset for bus fuel grants.

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(7) Minor oils, matches and mechanical lighters, gaming machine licences.

cc PS/bhancellor RWP  
 PS/CST  
 PS/FST PS/C&E  
 Miss Sinclair Mr Bone -  
 Mr Walters C&E  
 Miss Wallis  
 MCV



Treasury Chambers, Parliament Street, SW1P 3AG

Lord Newall  
 Chairman  
 British Greyhound Racing Board  
 24-28 Oval Road  
 LONDON  
 NW1 7DA

20 January 1987

*Dear Francis*

Thank you for your letter of 7 January, which enclosed your Budget representations.

I would be delighted to meet a deputation from The British Greyhound Racing Board. I have asked my office to be in touch with the details.

*I  
 have even*

*Pm*

**PETER BROOKE**



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

Pse

From: P Jefferson Smith

Date: 20 January 1987

MINISTER OF STATE

cc PS/Chancellor  
 Mr Scholar  
 Miss Sinclair  
 Mr Graham  
 (Parly. Counsel)

**MARINE DIESEL OIL USED IN PLEASURE CRAFT : STARTER NO. 24**

1. Your Private Secretary's note of 7 January 1987 to Mr Knox recorded your view that there is a strong case against going the full distance i.e. raising the duty on marine diesel to the level of duty on diesel for road use (derv), but that a modest increase might be attractive.

2. In legislative terms the mid-way course would be more difficult since it would mean setting another rate of rebate. But this would not be a decisive difficulty. The real objections are practical, in that it would pose even more administrative and control problems for the oil trade and ourselves than a full increase. At present diesel delivered at the rebated duty rate has to be chemically marked and dyed to enable our testing units to detect and prove misuse. An additional duty rate would require a different chemical marker and dye to be added to marine diesel. Such a measure could be introduced only after extensive research and agreement with the oil industry. The industry would also have to provide separate storage facilities and make special delivery arrangements for the separately marked marine diesel.

Internal circulation:

CPS	Solicitor	Mr McGuigan	Mr Boardman
Mr Knox	Mr Butt	Mr Wilmott	

198/1/87

3. A modest increase might also attract criticism in Parliament. The boating community is usually seen as a "well-off" section of the population and it would probably be said that if any change were to be made their boats would be better subjects for the full derv rate than lorries hauling food and essential industrial products, as well as public service vehicles such as ambulances and fire engines.

4. The sole advantage of an intermediate rate seems to be as a demonstration of willingness to tackle an undertaxed area. But disadvantages are so great that we would suggest that this would be the worst of the available possibilities. The real choice remains in our view either imposing the full derv rate on marine diesel or, in view of the small yield and all the difficulties, keeping to the status quo.

MW

P Jefferson Smith

CONFIDENTIAL

pps in?  
[Signature]



FROM: S P Judge

DATE: 21 January 1987

MR JEFFERSON SMITH - C&E

cc PS/Chancellor

Mr Scholar

Miss Sinclair

Mr Graham - Parly Counsel

PS/Customs & Excise

MARINE DIESEL OIL USED IN PLEASURE CRAFT: STARTER No 24

*below*

The Minister of State has seen your submission of 20 January, and agrees with you that the only sensible options are to impose the full derv rate on marine diesel or to maintain the status quo. As he has already decided against the former (my note of 7 January to Mr Knox) this means that this starter can now be dropped.

[Handwritten initials]

S P JUDGE  
Private Secretary

From: P TREVETT  
Date: 22 January 1987

*put Papers  
Please*



HM CUSTOMS AND EXCISE  
VAT CONTROL DIVISION D  
ALEXANDER HOUSE 21 VICTORIA AVENUE  
SOUTHEND-ON-SEA X SS99 1AJ  
TELEPHONE SOUTHEND-ON-SEA (0702) 348944 ext

Minister of State

cc PS/Chancellor  
PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr Jenkins  
Parliamentary Counsel

**FINANCE BILL 1987 STARTER NO 18: VAT REGISTRATION OF OVERSEAS TRADERS**

1. In his note of 7 January Simon Judge has said that you are inclined to leave this starter in.
2. This starter was concerned primarily with correcting a technical flaw in existing legislation and thereby closing a theoretical tax loophole. At present we have no evidence that this loophole is being used by overseas traders and any tax loss, which may be occurring, must therefore be minimal.
3. This starter does not now fit with our major proposals for this year's Finance Bill, as they have developed since the preparation of the original starters list either in the context of tax avoidance or assisting small businesses. With your agreement we would therefore propose not to proceed with it this year, but hold it over for a future year when its inclusion would be more appropriate.

P TREVETT

---

Internal distribution

CPS  
Mr Knox  
The Solicitor  
Mr Howard

Mr Butt  
Mr McFarlane  
Mr Wilmott  
Mr Ritchie

BUDGET - CONFIDENTIAL



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

*c/see also submission on  
VAT relief for purchases  
by mountain rescue  
associations at A*

From: P Jefferson Smith  
Date: 29 January 1987

MINISTER OF STATE

cc PS/Chancellor  
Miss Sinclair  
Mr Romanski  
Mr Cropper  
PS/Inland Revenue

*Subject to  
MST's views,  
but see memo  
of James  
CR 29  
X + Mountain  
rescue as  
Budget  
Lobby  
mini-package*

BUDGET REPRESENTATIONS FROM THE CHARITIES VAT AND TAX REFORM GROUP

JEFFERSON  
SMITH  
TO  
MST  
29/1

1. You asked (Mr Judge's note of 15 January) for advice on whether any of the CVTRG's proposals were suitable for implementing in this year's Budget.

2. There are good arguments against giving any concessions to charities this year. Charities have been generously treated in successive Budgets over the past few years, and the Chancellor made it clear that last year's package was to be regarded as exceptional. To make a regular policy of offering some minor concessions in each Budget arouses expectations that must eventually be disappointed, and also brings us closer to the day when the EC begins to take an unwelcome interest in our extensions of the zero rate in this area.

3. The main argument for any measures for charities this year would arise if there are to be substantial income tax cuts in the Budget. Reductions in income tax automatically reduce charities' income from covenanted donations. One possible palliative for this would be, as the CVTRG suggest (para 10 of their paper), a transitional relief of the kind allowed in 1973. The Inland Revenue (who have contributed to this section of our brief) recommend against this: the circumstances in 1973 (a major restructuring of the income tax system) were

Internal Circulation:

CPS

Mr Knox

Mr Wilmott

Ms Barrett

quite exceptional and similar relief was not given to charities following the income tax cuts of 1979. Last year's direct tax concessions to encourage charitable giving were substantial; you will no doubt want to assess their full effect before introducing further measures. A transitional relief in any case has only a temporary effect; it does not solve charities' underlying financing problem.

4. VAT concessions are not a substitute for loss of income tax relief on covenanted income: they do not necessarily benefit the same charities, nor do they bear any relationship to a charity's level of public support. Whatever the decision is on the basic rate of income tax, we would recommend against any substantial package on the VAT side this year; if, for presentational reasons, you wished to offer some minor sweeteners, there might be advantages in presenting this as a tidying up exercise after last year's package. The note attached analyses in more detail the specific proposals made by the CVTRG. A concession on drugs and, perhaps, welfare vehicles for hospices (as well as perhaps bathrooms in communal homes) could form the basis of a restricted package if you thought one appropriate.

5. We also need at some time to give statutory effect to two extra-statutory concessions introduced since last year's Budget. One was for the installation of individual bathroom and toilet facilities for the disabled residents of a charity-owned home; the other for goods donated for export by a charity. This could be done simultaneously with any new measures decided on.

6. We would be grateful for early guidance on whether the Order on mountain rescue equipment, already prepared, is to be held over until the Budget.

PS

P Jefferson Smith



**BUDGET MEASURES PROPOSED BY CHARITIES VAT AND TAX REFORM GROUP**

1. Drugs (paragraph 4)

The CVTRG complain that the relief for medicinal products introduced in last year's Budget is of very limited use to medical research charities, because most of the chemical products which they use for research are not medicines as defined by the Medicines Act (ie capable of being administered to patients or animals). Ideally, what they would like is a relief for all drugs used in medical research.

The reason for not introducing a general relief for drugs last year was that the Government Chemist advised that the term was not capable of precise definition: it denotes any substance which has a physiological effect (eg common salt). If further relief is to be given to medical research charities, it would have to be, as the CVTRG suggest, by means of a list of the individual substances to be relieved: the aim would be to cover all those in common use in current medical research work. If you would like us to investigate this option further, we would be grateful for authority to consult in confidence with DHSS and the Government Chemist.

The present relief for medicinal products is confined to charities engaged in the care and treatment of patients or in medical research. It would be for consideration whether a relief for individual drugs could (or should) be restricted in the same way, or whether it might also be extended to include non-profit-making research bodies (most, if not all, of which are funded by public money).

✓ The cost of a relief would depend on the range of chemicals to be covered, and whether it was decided to include the non-charitable research bodies. A comprehensive relief might cost in the order of £3 million.

2. Group 16 Relief (paragraph 5)

Most of the items mentioned here (syringes, tissue culture dishes, test tubes) are in our view already covered by the zero-rating provisions for medical and scientific equipment used for medical research (Items 4-6 of Group 16). We have asked the CVTRG to investigate further the precise nature of the problem.

One category of goods not at present covered by Group 16 are autoclaves (machines for sterilising medical and laboratory equipment). A VAT Tribunal about two years ago upheld our view that these are not in themselves medical or scientific equipment, and therefore are not zero-rated. It would be possible to relieve machines of this type by adding 'sterilising equipment' to the list of other types of equipment entitled to relief, and the revenue cost would probably be small. But to concede here would be one step further towards conceding on the laundry and catering equipment mentioned at para 6 below and on end use relief generally. Such concessions only add to the administrative burdens.

3. Building Costs (paragraph 6)

The CVTRG's primary request is for complete relief for all building alterations for social welfare charities providing day care or residential facilities. There can be no doubt that VAT does represent a heavy burden on charities in this particular field: we believe that their figure of £6M may be a substantial under-estimate. Nevertheless, we recommend against any concession: it would be costly, would be divisive as between charities, could provoke infraction proceedings from the EC, and would make it difficult to resist demands for similar reliefs for the disabled in their own homes.

The CVTRG also suggest four less comprehensive measures in this area:-

(a) Relief for professional fees (architects', surveyors', etc). The CVTRG want relief both for new work (already zero-rated) and alterations (zero-rated if their primary recommendation is accepted). Professional fees in building work have been standard-rated since the inception of the tax; there has been no relief for charities or anyone else. It is possible to avoid tax by arranging for the professional to make his supply through the builder who is providing the zero-rated construction work (or himself to provide the construction services as well as professional advice), but the charities say that they do not find it practicable to operate in this way. We recommend against any relief here, not least because it would invite claims for similar treatment from other (non-charitable) groups.

(b) Relief for bathrooms etc in communal homes. The provision of appropriate toilet and bathroom facilities is already zero-rated for handicapped people in their own homes, and, with your authority, we made an extra-statutory concession last year to cover the individual bathrooms being built for the residents in a residential home run by the British Limbless Ex-Servicemen's Association. The CVTRG want a general relief to be applied to both communal and individual bathroom and toilet facilities in charity residential homes. There is some logic in this argument, and, while we have no reliable estimate of the revenue cost, it would probably not exceed £1-2M. We ought to legislate soon to cover the extra-statutory concession; it is for consideration whether the statutory relief ought to extend also to communal facilities.

(c) Building work necessitated by statutory requirements. The relief sought here is both for charities and for private individuals who are disabled. It would cover a wide variety of circumstances and would be very costly in revenue terms. It could well attract unfavourable attention from the EC and we

recommend against any relief along these lines.

(d) Any building work needed to improve access or mobility for disabled people. The existing reliefs (for ramps, lifts and the widening of doors and passageways) are defined in specific terms, and cover the most obvious problems of access. A relief along the lines suggested by the CVTRG could be argued to cover virtually any alteration made to a handicapped person's or charity home, and would be very expensive in revenue terms. We recommend against any general relief. If you wished, for presentational reasons, to make any further concessions in this area, we would suggest that it be in the form of a specific relief (eg for adaptations to kitchens).

4. Welfare vehicles for hospices (paragraph 7.1-2)

The proposal is that last year's concession for passenger vehicles (capable of carrying between 6 and 50 passengers) for charities caring for the blind, deaf and mentally handicapped be extended to hospices. We have our doubts as to how often such vehicles are actually used by hospices (who are more likely to use ambulances or volunteers' cars), and to grant a concession would probably be the prelude to pressures for similar relief for ordinary cars. Nonetheless, it is difficult to defend the exclusion of hospices from the list of charities benefitting from this relief and the revenue cost would be small. This is a concession which you may think it worthwhile to make.

5. Wireless for the bedridden (paragraph 7.3-5)

The original reliefs for talking newspapers and wireless sets for the blind were intended primarily as some measure of compensation for their inability to benefit from the zero-rate for newspapers and books. The same arguments do not apply to wirelesses and cassette recorders for the bedridden, and to grant a concession here would invite pressures for further reliefs, for example, from the hospital broadcasting associations, who are already campaigning for relief

## BUDGET - CONFIDENTIAL

from VAT on their purchases. The cost of a concession specifically for wireless for the bedridden would probably be small, but we recommend against it because of the likely repercussions.

### 6. Laundry and catering equipment (paragraph 7.6)

Relief here would be a further step toward relieving all the general-purpose purchases of hospital and social welfare charities. The CVTRG argue that the specialised heavy-duty washing machines needed in hospitals or residential homes are easily distinguishable from others (we are not clear what kind of catering equipment they have in mind), and claim that a relief need not be repercussive. A concession, however, would be likely to lead to claims for similar treatment from homes or hospitals who, for cost or other reasons, used ordinary washing machines, and it could invite pressure also from private individuals caring for a permanently sick or incontinent person in their own homes. We recommend against any relief.

### 7. Fund-raising events (paragraph 8)

We are not aware of any impending Tribunal cases on this issue. We have always argued that it is not necessary for the UK to implement the exemption in the Directive (which covers fund-raising events by political parties, trades unions and sports clubs as well as medical, educational, welfare and cultural charities) because the high level of our registration threshold means that smallscale activities are automatically excluded from tax. The Directive permits exemption for fund-raising events only if the fund-raising activities do not distort competition with ordinary commercial businesses; largescale regular events could well do this. It is in any case open to charities to organise their fund-raising events in such a way (eg by running different events in the names of different individual members) as to avoid tax on all but the very largest. We would be reluctant to recommend any new relief in this area without stronger evidence that the existing rules (which have been in force since the inception of the tax) are not working satisfactorily.

8. Transitional tax relief (paragraph 10.11-2)

The transitional relief granted in 1973 was to meet exceptional circumstances: a major restructuring of the income tax system meant a substantial reduction in the rate deducted from covenant payments. No similar relief was given in 1979, when the basic rate of income tax was reduced from 33% to 30%; it was argued that the tax cuts would enable donors to afford to give more. Last year's direct tax concessions to charities were very generous, and are expected to generate substantial new income for them. (The cost was put at £60M last year but this will obviously depend on the public response.) There is also the general point that it is mildly bizarre that the Government should be expected to provide compensation for having reduced tax rates; this is of course a weakness of any system of 'tax expenditures'. The Inland Revenue recommend against any transitional relief of the kind suggested.

9. Community Charge (paragraph 10.3)

Strictly speaking, this is not a question for the Budget. We understand that no special relief is intended for charity residential homes. The new Community Charge is to be a charge to individuals, not property; responsibility for paying it would rest with the residents, not the charity.

UNCLASSIFIED



FROM: CATHY RYDING  
DATE: 2 February 1987

PS/CUSTOMS &amp; EXCISE

cc PS/Minister of State  
Sir P Middleton  
Mr Cassell  
Mr Scholar  
Miss Sinclair  
Mr Romanski  
Mrs Hamill - C&E  
Mr Brennan - C&E

**DUTY RATES**

To confirm the message I gave you over the phone this morning, the Chancellor would be grateful for a note examining movements in duty rates in real terms over the period 1978-79 to 1986-87 inclusive for each of the following:

1. Beer
2. Wine
3. Spirits
4. All alcoholic drinks
5. Petrol
6. Cigarettes
7. All tobacco
8. VED
9. All specific duties

Figures should be calculated using the RPI and not the GDP deflator. The Chancellor is interested in movements over the whole of this Government and, in particular, comparisons of the first term of the Government with the second term. It would be helpful to have this note as soon as possible.

A handwritten signature in blue ink, appearing to be 'CR'.

CATHY RYDING

CR  
6  
PS/CIE  
2/2

CONFIDENTIAL



*RWD*

FROM: CATHY RYDING  
DATE: 2 February 1987

PS/MINISTER OF STATE

cc: PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Scholar  
Miss Sinclair  
Mr Romanski  
Mr Cropper  
Mr Jefferson Smith - C&E  
Mr Cropper  
Mr Ross Goobey  
Mr Tyrie  
PS/C&E  
PS/IR

*CR  
To  
S/MST  
2/2*

**BUDGET REPRESENTATIONS FROM THE CHARITIES VAT AND TAX REFORM GROUP**

The Chancellor has seen Mr Jefferson Smith's minute to the Minister of State of 29 January.

2. The Chancellor has commented that subject to the Minister of State's views, he would be inclined to favour a concession on drugs and, perhaps, welfare vehicles for hospices (as well as perhaps bathrooms in communal homes) and mountain rescue as a Budget lollipop mini-package.

*CR*

CATHY RYDING



BUDGET REP. FROM CHARITIES VAT AND TAX REFORM GROUP

BUDGET CONFIDENTIAL

1. ALG  
2. Budget  
O/View  
BF 5/2



FROM: S P Judge

DATE: 3 February 1987

MR JEFFERSON SMITH - C&E

- cc PS/Chancellor
- PS/Chief Secretary
- PS/Financial Secretary
- PS/Economic Secretary
- Mr Scholar
- Miss Sinclair
- Mr Romanski
- Mr Cropper
- Mr Ross Goobey
- Mr Tyrie
- PS/Customs & Excise
- PS/Inland Revenue

PS/MST  
to  
JEFFERSON  
SMITH  
3/2

**BUDGET REPRESENTATIONS FROM THE CHARITIES VAT AND TAX REFORM GROUP**

The Minister of State has seen your submission of 29 January, and Cathy Ryding's note of 2 February to me. The Budget package should contain the following elements:

- i. Mountain rescue associations (your notes of 12 and 20 January);
- ii. the extra-statutory concession in paragraph 5 of your note, for goods donated for export by a charity;
- iii. the other extra-statutory concession, for the installation of individual bathroom and toilet facilities for disabled residents of charity-owned homes - extended (paragraph 3 (b) of the paper attached to your submission) to relieve communal facilities in charity homes;
- iv. welfare vehicles for hospices (paragraph 4 of your attachment);
- v. the drugs package described in paragraph 1 of your attachment. The Minister of State is content for you to consult DHSS and the Government Chemist.

I think the only remaining issue is whether the drugs concession should apply to non-charitable and non-profit-making research

**BUDGET CONFIDENTIAL**

bodies (which the Minister assumes includes MRC establishments). He would like to know what representations we have received on this, and what proportion of the comprehensive relief would go to non-charitable bodies. I would be grateful for a short note on this.

A handwritten signature in black ink, appearing to be 'S P JUDGE', written in a cursive style.

**S P JUDGE**  
Private Secretary



Many thanks.

Useful background.

Please contact & check  
for accuracy, a statement  
at  Public Law (or

no form of no releases):

"This means that, over the  
past ~~several~~ <sup>years</sup> so far,

the duties on both   
petrol will have broadly  
kept pace with inflation,

the duty on cigarettes will  
have risen by some 20% on  
real terms,  the specific

duty on a whole will have  
risen by some 5% more than  
inflation." Mr.

P.S. I am, necessarily,

shortly surprised

by the work ~~of~~ @ X.

MS



H.M. CUSTOMS AND EXCISE  
KING'S BEAM HOUSE, MARK LANE  
LONDON EC3R 7HE  
01-626 1515

CHANCELLOR

*Ch*  
*Confirms that, even*  
*with no realisation, you*  
*will still (just) be ahead*  
*over your period as Chancellor.*

From: P G WILMOTT

Date: 4 FEBRUARY 1987

cc Minister of State  
Sir P Middleton  
Mr Cassell  
Mr Scholar  
Miss Sinclair  
Mr Romanski

DUTY RATES

*AA*

WILMOTT  
to  
CH/EX  
4/2

1. Ms Ryding's note of 2 February asked for a note examining movements in excise duty rates from 1978-79 to 1986-87.
2. The annexed table shows how the specific duties have changed over the period. To produce the aggregate indices (all alcohol; all tobacco; all specific duties) we weighted the individual duties by net receipts year-by-year. We tried other approaches (eg the relative weights at the beginning and end of the periods) and found they made little difference. But because there was some difference, the aggregate indices are best regarded as broad indications of the overall trends.
3. Over the whole period of the Government, specific duties have gone up by some 40 per cent overall. This is largely attributable to large real increases in cigarette duty (up by around three quarters) and petrol duty (up by a half). The drinks duties have roughly held their own: movements in the main revenue raisers have broadly cancelled out (beer duty has risen by a quarter and spirits duty fallen by over a fifth). Table wine duty has dropped by nearly 30 per cent and cider duty has gone up by over a half. Other notable changes include pipes and cigars (duties down and up respectively by about a fifth) and derv (up by a tenth - markedly less than petrol).

Internal circulation: CPS, Mr Knox, Mr Jefferson Smith, Mr Whitmore,  
Mr McGuigan, Mrs Hamill, Mr Bone, Mr Brennan.

4. Some changes are attributable mainly to the Government's first term: the rises in the beer and petrol duties, for example, were largely accomplished by the 1983 Budget. Others fall into the second term: the drop in table wine duty and the rise in cider duty, for instance. A third group has followed a more consistent trend over the whole period: eg spirits and fortified wines. Perhaps the most striking feature is the big jump in the overall index attributable to the 1981 Budget, with significant rises in the duties on beer, tobacco and petrol. This largely explains why overall some three quarters of the increase in the specific duties occurred during the Government's first term.



P G WILMOTT



**MINUTES OF A MEETING HELD AT**  
**4.30 PM ON WEDNESDAY 4 FEBRUARY**  
**IN HM TREASURY**

Those Present:	Mr Metcalfe)	
Chancellor	Mr Jones )	NLVA
Minister of State	Mr Edwards )	
Mr Stern	Mr Overton )	
Mr Jefferson-Smith - C+E	Mr Michael Colvin MP	

**NATIONAL LICENSE VICTUALLERS ASSOCIATION (NLVA):**  
**BUDGET REPRESENTATION**

The NLVA said they welcomed the stand still on alcohol duty in the last Budget, but they had been extremely annoyed with the Brewers for increasing prices. They hoped that it would be possible to leave the duty on alcohol unchanged again in this Budget. They also urged the Chancellor not to increase the license duty on gaming machines. They supported the Brewers protest against the application of the VAT input tax changes to tide house rentals.

**Duty Increases**

2. The NLVA had been very annoyed with the Brewers for increasing prices after the last Budget. The Chancellor said that he had also been surprised. He had seen the Brewers before the last Budget and they had said that consumption was suffering and that this due to price. They had asked for no increase in duty, but had then more than cancelled out the benefit by increasing prices. This did not throw a favourable light on their arguments.

3. Mr Colvin said that there was a strong movement who would like to see alcohol priced out of the market altogether. They would doubtless be bringing pressures to bear on the Chancellor.



### Gaming Machine Licence Duty

3. The NLVA said that any increase in the licence duty on gaming machines could not be recovered by changing the stake or the payout of the machine as this would reduce its attractiveness. Many public houses in rural areas were only viable because of profits from gaming machines. The Minister of State said that he thought that there had been a recent increases in prize money. The NLVA said that the limit on prize money had been increased by £1. However, their competitors in clubs had been allowed to increase their maximum payout by £50. Competition from clubs both in this area and because they were able to subsidise drink prices was a serious threat. The Chancellor noted that the limit on prices was an issue for the Home Office, and not for him. The Minister of State asked whether the NLVA were able to produce any detailed figures explaining why gaming machines were not viable. The NVLA said that they were not, but revenue had dropped substantially recently.

### VAT Input Tax Changes

4. The NLVA said that the proposed VAT input tax changes would fall on tenants. The cost of repairs was normally recovered by increasing rent over a period of time. The tenant would be unable to recover this because of customer resistance to price increases, and would have to foot the bill himself. The Chancellor said that he was very conscious of the problem and the Minister of State and Mr Jefferson-Smith had been talking to the Brewers to try and find a solution. Mr Jefferson-Smith said that he had seen the Brewers recently and had put to them a specific proposal which he hoped would be satisfactory. The Minister of State would be seeing the Brewers next week.





5. The NLVA said that their Licensee Paper had stated that they would be meeting the Chancellor. The Chancellor said that it was important that they did not say anything more than this.

CR

CATHY RYDING

5 February 1987

Circulation:-

Those present from HMT and C&E  
PS/CST  
PS/FST  
PS/EST  
Mr Scholar  
Miss Sinclair  
Mr Romanski  
Mr Cropper  
PS/C+E



*CR*  
FROM: CATHY RYDING  
DATE: 5 February 1987

MR P G WILMOTT

cc Minister of State  
Sir P Middleton  
Mr Cassell  
Mr Scholar  
Miss Sinclair  
Mr Romanski

*CR*  
*to*  
*WILMOTT*  
*5/2*

**DUTY RATES**

The Chancellor was most grateful for your minute of 4 February.

2. The Chancellor was slightly surprised by the rise in the index for all specifics between 1985-86 and 1986-87.

A handwritten signature in cursive script, appearing to be "CR".

CATHY RYDING



FROM: CATHY RYDING  
DATE: 5 February 1987

CR  
To  
SCHOLAR  
5/2

MR SCHOLAR

**DUTY RATES**

You will have seen Mr Wilmott's minute to the Chancellor of 4 February examining movements in excise duty rates from 1978-79 to 1986-87.

2. The Chancellor would be grateful if you could concoct and check for accuracy a sentence along the following lines for use in the event of no revalorisation:

"This means that, over this Parliament so far, the duties on beer and petrol will have broadly kept pace with inflation, the duty on cigarettes will have risen by some 20 per cent in real terms, and the specific duties as a whole will have risen by around 5 per cent more than inflation."

CR

CATHY RYDING

SECRET AND PERSONAL

DUTY RATES

Paper P...

SCHOLAR

to  
Oct 26  
10/2

Alex - does this  
next week's  
meeting

FROM: M C SCHOLAR  
DATE: 10 FEBRUARY 1987

*prop*

CHANCELLOR OF THE EXCHEQUER

DUTY RATES

*Prop for Future  
Duty on a  
monies*

*Mark's proposal -  
(Psr) with annex  
attached*

Cathy Ryding's minute of 5 February asked me to check for accuracy some material on the path of the specific duties over this Parliament.

2. Mr Wilmott's minute to you of 4 February on movements in excise duty rates compared duty rates deflated by the difference between the average RPI for 1983-84 and that for September 1986. This does not seem an entirely satisfactory basis for the comparison you wish you make. Mr Wilmott, at my request, reworked the figures in his note - copy attached - deflating by the difference between the June 1983 and the December 1986 RPI. (Clearly, for the Budget Statement we will need to bring in the RPI increase, whatever it is, between December 1986 and February 1987.)

3. On this basis we can now say - and would be able to say in the Budget - that over this Parliament so far beer and petrol duties have broadly kept pace with inflation; that cigarette duty will have risen by about 20 per cent in real terms; and that for specific duties as a whole there will have been a real increase of about 4 per cent.

*Prop let  
me have this ASAP.  
2. Prop reminds me of  
comparable figs for  
beer & petrol (May 1979 - June 1983)  
Wh. & SWS of course include VAT  
3. Prop circulate answers  
to all memos & advices  
MUS*

M C SCHOLAR

*P.S. Had to  
make  
you a inclusion of VAT  
difference for  
VAT was  
included? I  
don't know  
if it is  
of course to  
include*

*I do not think that (ii) is on: it is a matter of either (i) (after 1988) or you as planned.*

**BUDGET CONFIDENTIAL**



FROM: S P Judge

DATE: 11 February 1987

MR JEFFERSON SMITH - C&E

cc PS/Chancellor

PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Sir Peter Middleton  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr Ross Goobey  
Mr Tyrie

PS/Customs & Excise

PS/Inland Revenue  
Mr Corlett - IR

*Ch  
X below could be a  
v expensive way of getting  
a 2nd payroll giving agency  
AA*

#### POOL BETTING DUTY AND LITTLEWOODS

As you may know, it is likely that Littlewoods will agree to provide, in competition with the Charities Aid Foundation, a charitable payroll giving service.

The Minister of State is concerned whether, in the circumstances, the agreed pool betting duty restructuring is politic (Annex B of Mr Knox's submission of 14 November). He appreciates that Littlewoods are doing very well at the moment, and that their co-operation over charitable giving is not unconnected with their nervousness about possible national lotteries.

The Minister would be grateful for your best advice on whether Littlewoods are expecting the planned duty increase. If they are resigned to it, all well and good.

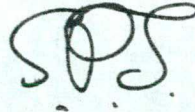
If they are not, the Minister thinks that further thought will be needed. Two options are:

- i. not to proceed with the restructuring this year;
- ii. to cut duty on the small firms, but not increase that on the large ones like Littlewoods. This would cause the package to no longer be revenue neutral; it would be helpful

**BUDGET CONFIDENTIAL**

to know what the shortfall would be and whether it could be made up on other betting duties.

I would be grateful for an urgent note on this issue, which I hope is clear.

A handwritten signature in black ink, consisting of the letters 'S', 'P', and 'J' in a stylized, cursive script.

**S P JUDGE**  
Private Secretary

BUDGET CONFIDENTIAL



FROM: S P Judge

DATE: 11 February 1987

APS/CHANCELLOR OF THE EXCHEQUER

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr ROSS Goobey  
Mr Tyrrie  
PS/Customs & Excise

C/content with X?

CE 11/2

OK

GAMING MACHINE DUTY

Following the meeting with the National Licensed Victuallers Association on 4 February, the Minister of State had a brief word with Mr Jefferson Smith and Mr Cropper about this yesterday, in the margins of another meeting.

The Minister of State referred to the NLVA's claims that returns from gaming machines were falling, and that pubs were treated unfairly by the Home Office in comparison with clubs. He wanted to be certain that the Budget proposals were not unfairly clumsy.

Mr Jefferson Smith said the NLVA had not backed their contention with any facts. They would not tell Customs how much they make from machines: many Brewers shared profits with licencees, with obvious scope for income tax evasion. But the Gaming Board felt that the rate of return on machines had increased. Also, the number of limited prize (AWP) machines had been steadily increasing since the last duty increase in the 1982 Budget - by 11.5%, 4% and 15.8% in the three successive years to 1 October 1986. The number of machines will drop following a duty increase: the Minister of State agreed that this was no reason to shrink from revalorisation.

X | The Minister of State therefore concludes that the Budget proposal (set out in Mr McGuigan's submission of 18 December) should stand. Does the Chancellor agree?

S.P.J.

S P JUDGE  
Private Secretary

## BUDGET CONFIDENTIAL



FROM: A C S ALLAN  
DATE: 12 February 1987

PS/MINISTER OF STATE

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Sir P Middleton  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr Ross Goobey  
Mr Tyrie  
PS/C&E  
Mr Jefferson Smith - C&E  
PS/Inland Revenue  
Mr Corlett - IR

**POOL BETTING DUTY AND LITTLEWOODS**

The Chancellor has seen your minute of 11 February to Mr Jefferson Smith. He does not think that the Minister of State's fallback option (ii) is on: if Littlewoods are not expecting the planned duty increase, he feels the choice will be between either the Minister's option (i) (defer to 1988), or going ahead as planned anyway.

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

A C S ALLAN



'COOLERS'

BUDGET SECRET

Rup

EXTRACT FROM  
BRYCE KNOX 12/2/87  
~~12/2/87~~

Implementation

21. If you agree to these changes, they would operate from 6.00 pm on Budget Day.

Low Strength Mixed Drinks

22. This is less contentious and difficult. The proposal is to create a new duty band to cater for the growing category of low strength drinks, for which the present duty structures in respect of their components does not adequately provide. The proposal is to introduce a new structure for coolers and similar mixed drinks containing between 1.2% and 5.5% alcohol, with the duty charged per degree of alcohol at a rate set at a level per degree of approximately one fifteenth of the table wine duty.

23. Traditional beer-based products such as shandy and lager and lime would bear beer duty and not the new duty rate, but with no additional duty charge on the non-alcoholic ingredients. This would be less favourable than allowing them to be taxed in the new mixed drinks category, but is necessary to prevent avoidance by the addition to beer of small quantities of non-beer additives. Informal soundings of the Brewers' Society suggest they will go along with this.

24. The revenue effect of these proposals would be negligible.

25. Because consultations with the trade will be needed on the workings of the new regime and existing subordinate legislation will have to be amended, we recommend that although the changes would be included in the Finance Bill, they should be brought into effect by a Commencement Order later in the year.

Spoke to Mr. H...  
Mr. H...?

Bryce Knox

B H KNOX

Oh  
I think you want  
to raise this  
duty  
24/2

CONFIDENTIAL

EXTRACT FROM JEFFERSON SMITH  
6/11/86.

Low-strength drinks

14. This is a growth area. The drinks are predominantly wine plus fruit juice ('coolers'). The duty structure effectively precludes imported 'coolers' and beer-based and spirit-based coolers from the UK market. There are also anomalies in the treatment of low-strength beer and partially fermented grape juice. In the discussion paper we floated the idea that there should be a new band of wine/made-wine duty for low-strength products at a flat rate of 50% of the full rate of duty on light wine/made-wine. As a result of the representations we have received we now suggest a structure which would apply to mixed drinks containing between 1.2% and 5.5% alcohol; be charged according to the strength of the product (per degree); and approximate to the effective rate of duty on a cooler using duty paid made-wine as an alcoholic ingredient. Such a structure would minimise the potential for distortion of the low-alcohol drinks market and would find favour with the health lobby because it would not discriminate against lower alcohol products. But there are problems which would need further discussion with the trade.

15. In reacting to the discussion paper the Brewers' Society said that they had also been considering the implications of removing the 1030° lower limit for beer duty. Despite preliminary indications of being in favour, the Society have now come down firmly against. They say that removal of the limit could seriously damage the image of beer and consequently the current beer market. There are persuasive arguments on competition, freedom of choice and social grounds for removing the limit; but abolition could be difficult to carry through against sustained opposition from the major brewers. There are enough difficulties with the brewers over VAT partial exemption to point against opening up a second front.

*pur*

FROM: CATHY RYDING

DATE: 12 February 1987

PS/MINISTER OF STATE

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr Ross Goobey  
Mr Tyrie  
PS/C&E

**GAMING MACHINE DUTY**

The Chancellor has seen your minute of 11 February.

2. The Chancellor agrees with the Minister of State that the Budget proposal (set out in Mr McGuigan's submission of 18 December) should stand.

*CR*

CATHY RYDING



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

From: P Jefferson Smith

Date: 13 February 1987

MINISTER OF STATE

*Subject to HSI's  
views, I wd favour  
difficult to structure to 1988, all the  
& very work @ all the  
year in*

cc **Chancellor**  
Chief Secretary  
Financial Secretary  
Economic Secretary  
Sir Peter Middleton  
Sir Terence Burns  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr Ross Goobey  
Mr Tyrie  
PS/Inland Revenue  
Mr Corlett - IR

#### POOL BETTING DUTY AND LITTLEWOODS

1. In answer to Mr Judge's minute of 11 February, we had not been aware of Littlewood's possible involvement in a charitable payroll giving service.
2. The Pool Promoters Association has made no Budget representations this year. They are almost certainly not expecting an increase in the overall incidence of the duty. Although Zettlers have pressed for restructuring in the past, the duty structure is of such long standing that it is unlikely to have occurred to Littlewoods or Vernons that restructuring is being seriously considered.
3. The industry is small, and there are plenty of published figures. Littlewoods will have no difficulty in working out that they will be the only losers from the restructuring. Vernons will pay marginally less; Zettlers and everyone smaller will gain. But while Littlewoods may well complain, we think they will have no

#### Internal circulation:

CPS	Solicitor	Mr Heron
Mr Knox	Mr McGuigan	Mr Wilmott

# BUDGET - CONFIDENTIAL

difficulty in coping with the increase, of about £3 million a year. This must be seen in relation to the following annual figures:

Littlewoods:	total stakes	£413m
	of which, expenses and profits	£123m
	duty	£176m
	prize fund	£115m

The £3 million will in practice come off the prize fund, reducing it by about 3%, or £65,000 out of a weekly prize fund of £2 million. Vernons prize fund, the next largest, is £30 million a year out of total stakes of £117 million.

4. Viewed in isolation therefore there seems no reason why the restructuring should not go ahead as planned. But I understand from Inland Revenue that the Littlewoods main Board has decided that it will have to commit in round terms £500,000 to the setting up costs of the payroll giving service.

5. We think that your fall-back solution (to which the Chancellor has indicated that he is not attracted) runs into difficulties in finding alternatives for the revenue lost. If you wanted to cut the duty on smaller firms while making no overall increase on Littlewoods, the top rate of duty would have to be kept at 42½%, thus giving all promoters including Littlewoods the benefit of the reduced rates. On our proposed scales, the duty loss would be just under £5 million. We suggest that this could not be made up from general betting duty or gaming machines, which form a balanced package on their own. Bingo is sluggish and not in any case an attractive option for offsetting a benefit to the pools promoters. This leaves gaming. The London clubs are returning healthy profits, but their fortunes are very uncertain, since they depend heavily on the attraction of foreign gamblers to London. Even if the top duty rate was increased from 33⅓% to 40%, the extra yield would be only £1 million a year. There is therefore no sensible target for recoupment of the £5 million which would be lost from a pools restructuring which did not increase the burden on Littlewoods. As

BUDGET - CONFIDENTIAL

this amount of duty is so small in overall Budget terms, we suggest it is not worth tinkering with other duties to recoup it.

6. We suggest therefore that if you want to go ahead with the restructuring this year, it should either be

- (a) on the basis already planned, on the grounds that however unpleasant the surprise to Littlewoods, they can well stand the increase, or
- (b) the top rate should be kept at  $42\frac{1}{2}\%$ , so as to involve no increase to Littlewoods, but with no recoupment from other betting and gaming duties.

ph ✓

P Jefferson Smith



FROM: CATHY RYDING  
DATE: 16 February 1987

PS/MINISTER OF STATE

cc Chief Secretary  
Financial Secretary  
Economic Secretary  
Sir P Middleton  
Sir T Burns  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr Ross Goobey  
Mr Tyrie  
PS/Inland Revenue  
Mr Corlett - IR  
Mr Jefferson Smith - C&E  
PS/C&E

POOL BETTING DUTY AND LITTLEWOODS

The Chancellor has seen Mr Jefferson Smith's minute to the Minister of State of 13 February.

2. The Chancellor has commented that subject to the Minister of State's views, he would favour deferring the planned restructuring until 1988, and doing nothing at all this year.

CR

CATHY RYDING



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

*Handwritten notes in red ink:*  
Handwritten notes in red ink, including "MST" and "clear presentation for X".

From: P Jefferson Smith  
Date: 18 February 1987

MINISTER OF STATE

cc PS/Chancellor  
Mr Scholar  
Ms Sinclair  
Mr Cropper  
Mr Jenkins  
(Parly Counsel)

VAT : SALES OF HOLIDAY PACKAGES BY TOUR OPERATORS (STARTER No. 4)

1. Following my submissions of 29 October, 7 November and 13 November last, it was agreed to go ahead with this starter in the 1987 Bill with the scheme coming into effect from 1 April 1988.

X

2. We have now reached agreement with Parliamentary Counsel on the enabling clause. I attach a copy. You will see that it is admirably short and uncomplicated. It gives power to legislate for the detail of the scheme by or under a Treasury Order subject to the negative resolution procedure.

3. We do not expect the fact that part of tour operators' added value on holiday packages to Community destinations is to be taxed for the first time will be particularly controversial in itself. Indeed MPs representing UK resorts and tourist areas may welcome it as a small but overdue adjustment of what some of their constituents see as the imbalance in taxation between UK nationals choosing to take their holidays overseas and those choosing to holiday at home. However there might be some sniping about the legislative means chosen. It could be said that:

Internal Circulation:

CPS                      Mr Wilmott              Mr Nissen  
Mr Knox                Mr Cockerell            Mr Tracey



- (i) the Treasury Order should require an affirmative resolution;
- (ii) too much is being left to secondary legislation for a scheme which imposes tax; or
- (iii) there should not be any powers of sub-delegation "under the Order".

There are good answers to all these points. The House is having an opportunity to vote on the principle in the Clause. It does not need to take a second affirmative vote when the Order is laid. Because the essence of the scheme is only to tax a small part of each transaction, the detailed rules - given the wide variety of circumstances that have to be taken into account - are inevitably going to involve lengthy and complicated drafting. This is far better suited to secondary legislation backed up by a Public Notice or VAT leaflet written in non-legal language.

4. I should be grateful for confirmation that you are content for us to proceed on the basis of the clause as drafted.

Ph ✓

P. Jefferson Smith.

11 February 1987

**Tour operators**

4.-(1) After section 37 of the Value Added Tax Act 1983 there shall be added -

**"Tour Operators**

37A.-( 1) The Treasury may by order modify the application of this Act in relation to supplies of goods or services by tour operators or in relation to such of those supplies as may be determined by or under the order.

(2) Without prejudice to the generality of subsection (1) above, an order under this section may make provision -

(a) for two or more supplies of goods or services by a tour operator to be treated as a single supply of services;

(b) for the value of that supply to be ascertained, in such manner as may be determined by or under the order, by reference to the difference between sums paid or payable to and sums paid or payable by the tour operator;

(c) for account to be taken, in determining the tax chargeable on that supply, of the different rates of tax that would have been applicable apart from this section;

(d) excluding any body corporate from the application of section 29 above;

(e) as to the time when a supply is to be treated as taking place.

(3) In this section "tour operator" includes a travel agent acting as principal and any other person providing for the benefit of travellers services of any kind commonly provided by tour operators or travel agents.

(4) Section 45(3) below shall not apply to an order under this section, notwithstanding that it makes provision for excluding any tax from credit under section 14 above."

(2) In section 45 of that Act, at the beginning of subsection (4) there shall be inserted the words "Subject to section 37A(4) above".

BUDGET CONFIDENTIAL



FROM: Minister of State

DATE: 18 February 1987

CHANCELLOR

- cc Chief Secretary
- Financial Secretary
- Economic Secretary
- Mr Scholar
- Mr Romanski
- Mr Cropper
- Mr Ross Goobey
- Mr Tyrie
- PS/Customs & Excise
- Mr Jefferson Smith - C&E

*OK. This Budget  
passed for Budget  
Spice will have  
to be complete  
drafted  
given  
more  
p. v*

UNLEADED PETROL: STARTER No 5

At Prayers last Friday I was asked to investigate whether the duty differential currently proposed (5p a gallon) is sufficient to encourage the use of unleaded petrol.

I have looked at the papers again, particularly Mr Jefferson Smith's submission of 28 October. I accept his contention that a 5p differential will enable us to make a robust statement that "unleaded petrol should be cheaper at the pump than 4\* leaded petrol".

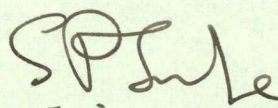
It is clear that, apart from Conoco (a small company), the trade does not want unleaded petrol to have a major price advantage at the pump. It would cause production problems for refiners, with recriminations between the Government and oil companies and motorists about who was to blame. It would also increase the risk that people would harm their cars by using incorrect but cheaper fuel. Moreover no Jaguar and Austin Rover cars can run on unleaded petrol at the moment, except for two recent Rovers.

Although the revenue cost of a wider differential would be minimal in the first year, as unleaded petrol catches on the cost could become substantial.

Mr Jefferson Smith's submission of 28 October argued against a power to alter the differential between Budgets by Statutory

Instrument. We accepted that advice, but you could emphasise in the Budget Speech the close attention you will be paying to market developments when you come to make your annual decision on the differential. The EEC Directive requiring lead-free fuel to "be widely available" does not apply until January 1989. DOE will then be responsible for deciding if the UK has complied with the Directive and what, if any, action they need to take. So there is at least another Budget in which to take further steps to encourage lead-free petrol by fiscal means.

Overall, I conclude that we should not change our decision.



**P** PETER BROOKE

(Approved by the Minister of State and signed in his absence)

*Ruf*



H.M. CUSTOMS AND EXCISE  
KING'S BEAM HOUSE, MARK LANE  
LONDON EC3R 7HE

01-261515  
382 5101

1. Mr Jefferson Smith *AM 19/2*

FROM: W F MCGUIGAN

2. Minister of State

DATE: 19 February 1987

*✓* The MST thought it was worth investigating this possibility. may raise at Prayers tomorrow

- cc PS Chancellor
- PS Chief Secretary / *FST have our copy.*
- PS Financial Secretary
- PS Economic Secretary
- Sir Peter Middleton
- Mr Terence Burns
- Mr Cassell
- Mr Scholar
- Miss Sinclair
- Mr Cropper
- Mr Ross Goobey
- Mr Tyrie
- Mr Graham - Parly Counsel

*Must  
Copy CR 19/2*

FINANCE BILL 1987 : POOL BETTING DUTY

1. Your private secretary conveyed to us your request to consider a graduated scale of pool betting duty which would result in a cost to the revenue of up to £2 million but which would give revenue neutrality to Littlewoods. He suggested the following rates:-

ON THE FIRST £200,000 OF WEEKLY TURNOVER	33 1/3%
ON THE NEXT £400,000 OF WEEKLY TURNOVER	40%
ON THE REMAINDER	43%

2. The effects of such a scale on the various pools should be approximately:

Internal Circulation

- CPS
- MR KNOX
- MR JEFFERSON SMITH
- SOLICITOR
- MR BREUER
- MR WILMOTT
- MR HERON

PROMOTER	1987/88		1987/88		COST(+) OR SAVING (-) TO POOLS COMPANY
	PROJECTED DUTY AT CURRENT RATE		PROJECTED DUTY (ABOVE SCHEME)		
	RATE	DUTY £m pa	EFFECTIVE OVERALL RATE	DUTY £m pa	£ million pa
1. LITTLEWOODS	42.5%	£205.063	42.66%	£205.871	+0.808
2. VERNONS	42.5%	57.927	41.78%	56.953	-0.974
3. ZETTERS	42.5%	9.090	36.59%	7.834	-1.256
4. CHARITY POOLS	33 1/3%	2.480	33 1/3	2.480	NIL
5. MINOR POOLS	42.5%	0.170	33 1/3	0.140	-0.030
REVENUE COST					£1.452

As Littlewoods would pay some £0.8m more the scheme does not meet one of your objectives.

3. We have not been able to devise a three-rate scheme which would achieve your desired result and yet have sensible rates or bands.

4. You may however wish to consider the following alternative which we think meets your requirements:

ON THE FIRST £250,000 OF WEEKLY TURNOVER	33 1/3%
ON THE REMAINDER	42 3/4%

The effects of this scale on the pools companies should be approximately:

PROMOTER	1987/88		1987/88		COST(+) OR SAVING (-) TO POOLS COMPANY
	PROJECTED DUTY AT CURRENT RATE		PROJECTED DUTY (ABOVE SCHEME)		
	RATE	DUTY £m pa	EFFECTIVE DUTY OVERALL RATE	DUTY £m pa	£ million pa
1. LITTLEWOODS	42.5%	205.063	42.5%	205.070	+ 0.007
2. VERNONS	42.5%	57.927	41.8%	57.018	- 0.909
3. ZETTERS	42.5%	9.090	36.8%	7.890	- 1.200
4. CHARITY POOLS	33 1/3%	2.480	33 1/3%	2.480	NIL
5. OTHER POOLS	42.5%	0.170	33 1/3%	0.140	- <u>0.030</u>

REVENUE COST'      £2.132

5. Although at first sight the scheme gives no relief to the charity pools the retention of the present preferential rate which was to be withdrawn at the end of this Parliament could be presented as a concession to charities.



W F MCGUIGAN

RF



FROM: CATHY RYDING  
DATE: 19 February 1987

PS/MINISTER OF STATE

cc Chief Secretary  
Financial Secretary  
Economic Secretary  
Mr Scholar  
Mr Romanski  
Mr Cropper  
Mr Ross Goobey  
Mr Tyrie  
  
PS/C&E  
Mr Jefferson Smith - C&E

**UNLEADED PETROL: STARTER NO.5**

The Chancellor was grateful for the Minister of State's minute of 18 February.

2. The Chancellor agrees with the Minister of State's conclusion that we should not change our decision.
3. The Chancellor has commented that this passage of the Budget Speech will need to be carefully drafted to get the most out of it.

CR

CATHY RYDING





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

From: P Jefferson Smith

Date: 20 February 1987

MINISTER OF STATE

cc PS/Chancellor  
 PS/Chief Secretary  
 PS/Financial Secretary  
 PS/Economic Secretary  
 Mr Scholar  
 Miss Sinclair  
 Mr Romanski  
 Mr Cropper  
 Mr Ross Goobey  
 Mr Tyrie  
 PS/Inland Revenue

DRUGS USED IN MEDICAL RESEARCH

1. Mr Judge's note of 3 February authorised us to consult with DHSS and the Government Chemist about the formulation of a VAT relief for drugs used in medical research, and also asked for advice on whether the relief should be extended to non-charitable bodies.

2. The DHSS and Government Chemist officials we have consulted advise against the approach suggested by the CVTRG and in my previous minute : that of listing the individual drugs eligible for relief. Such a list would be formidably long (individual descriptions would run into the thousands), and almost certainly far from comprehensive. They believe that the only practicable option is to draft the relief in general terms (eg 'substances used directly in synthesis and testing in medical research') and to rely on the end use criterion to exclude anything (eg household cleaning materials used in the laboratory) which is not immediately relevant to the research experiments. There are obvious difficulties of policing with this approach, but, if the object is to give charities an appreciable measure of relief in their medical research programmes, we do not see any viable alternative.

Internal circulation:

CPS	Mr Wilmott	Mr Nissen
Mr Knox	Ms Barrett	Mr Monk

3. The Association of Medical Research Charities, a body representing the top 35 charities in this field, state that approximately £100 million was spent by their members on medical research in 1985, and we estimate that the cost of a general relief for the independent medical research charities (under this heading we would include animal charities) would be around £1.5 million (the CVTRG's representations imply a slightly lower figure). This does not, however, include work done in the universities, which are also charities, and which receive money from both Government and industrial sources to carry out medical research.

4. The main agency for distributing public funds for medical research is the Medical Research Council. The MRC runs 56 of its own research establishments, and also funds a large amount of different research projects in hospitals, medical schools and universities. In addition, it pays for various academic fellowships and industrial consultancies, and is involved in some international projects. Its total budget in 1985/6 was around £130 million. We do not know how much additional money universities and others are able to attract from industrial sponsors; DES have no central figures.

5. Overall, therefore, it looks as if a relief for universities, hospitals and non-profit-making research bodies would cost an additional £1.5 - 2 million. It would be very difficult to exclude universities and private hospitals with charitable status from any relief for charities; the question must therefore be whether the relief should also extend to publicly funded hospitals and non-profit-making research associations. There have been no representations on this point, and, perhaps more surprisingly, no complaints that they were excluded from the relief for medicinal products introduced last year. It would be odd, moreover, to grant them relief for substances used in medical research without extending to them also the relief for medicinal products. For research associations this might be inexpensive, but to relieve the medicines bill of NHS hospitals must be ruled out on grounds of cost, quite apart from the argument that

the Government funding system is designed to cover the cost of VAT anyway. We recommend therefore that the new relief, like last year's, be confined to charities. If serious pressure does develop to include other non-profit-making bodies, it would be possible to look at the question again.

6. We think the overall cost of a relief confined to charities (including universities) would therefore be of the order of £2 million. The cost of the whole charities package in the minute of 3 February would be a little under £5 million.

ph ←

P Jefferson Smith



FROM: CATHY RYDING  
DATE: 20 February 1987

*Handwritten initials*

PS/MINISTER OF STATE

cc Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr Jefferson Smith - C&E  
PS/C&E  
Mr Jenkins - Parly Counsel

**VAT: SALES OF HOLIDAY PACKAGES BY TOUR OPERATORS (STARTER NO.4)**

The Chancellor has seen Mr Jefferson Smith's minute to the Minister of State of 18 February.

2. The Chancellor has commented that it would be useful for the Minister of State to be given close precedents for the power to legislate for the detail of the scheme by or under a Treasury Order subject to the negative resolution procedure, mentioned in paragraph 2.

*C.R.*

CATHY RYDING



FROM: S P Judge

DATE: 25 February 1987

MR JEFFERSON SMITH - C&amp;E

cc PS/Chancellor  
 PS/Chief Secretary  
 PS/Financial Secretary  
 PS/Economic Secretary  
 Sir Peter Middleton  
 Sir Terence Burns  
 Mr Cassell  
 Mr Scholar  
 Miss Sinclair  
 Mr Cropper  
 Mr Ross Goobey  
 Mr Tyrie  
 PS/Customs & Excise  
 Mr McGuigan - C&E

## FINANCE BILL 1987: POOL BETTING DUTY

As you know, it was decided at Monday's overview to drop this starter. This is just to record that the Minister of State thinks that this issue should be looked at again for the 1988 Finance Bill.

For the record, the Minister asked what the effect would be of increasing the top rate of the option set out in paragraph 4 of Mr McGuigan's note of 19 February from 42½% to 43%. Mr Heron gave me the following figures:

	COST(+) OR SAVING (-) TO POOLS COMPANY
	£ million pa
LITTLEWOODS	+ 1.18
VERNONS	- 0.60
ZETTERS	- 1.18
CHARITIES	Nil
MINOR POOLS	- 0.03

The total revenue cost of this option is therefore £0.6 million.

The Minister was very grateful for all the work you have done on this.

S P JUDGE  
 Private Secretary

BUDGET CONFIDENTIAL

RP



FROM: S P Judge

DATE: 25 February 1987

MR JEFFERSON SMITH - C&E

cc ~~PS/Chancellor~~  
PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Scholar  
Miss Sinclair  
Mr Romanski  
Mr Cropper  
Mr Ross Goobey  
Mr Tyrie  
PS/Inland Revenue  
PS/Customs & Excise

DRUGS USED IN MEDICAL RESEARCH

The Minister of State has seen your submission of 20 February, and instinctively agrees with your advice to confine the relief to charities. He is clear that excluding publicly funded hospitals and non-profit-making research associations would exclude MRC institutes, but not (of course) research funded by them but undertaken by charitable institutions. He can see a logical defence against any representations on the MRC's behalf.

S P J

S P JUDGE  
Private Secretary



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

FROM: B H KNOX

DATE: 25 February 1987

CHANCELLOR

cc: Chief Secretary  
Financial Secretary  
Economic Secretary  
Minister of State  
Sir P Middleton  
Sir T Burns  
Mr F E R Butler  
Sir G Littler  
Mr Cassell  
Mr Monck  
Mr Wilson  
Mr Sedgwick  
Mr Scholar  
Mr Odling-Smee  
Miss Evans  
Mr Cropper  
Mr Tyrie  
Mr Ross Goobey  
Mr Battishill, IR  
Mr Isaac, IR  
Mr Painter, IR

*CL*  
*For overviews a Monday*  
*Conan*  
*AA*

RESTRUCTURING OF THE WINE AND MADE-WINE DUTIES

It was agreed at the overview meeting on 16 February that if there was no revalorisation of excise duties it would be presentationally much easier not to proceed with the restructuring of the wine duties. We were asked for a note.

2. The proposed restructuring falls into two distinct parts. The first, and more important, is that affecting fortified wines; and the second is the introduction of a new duty band for low-strength mixed drinks ("coolers"). Either or both could be introduced if there were no revalorisation of the drinks duties.

/Fortified Wines

Internal distribution:

CPS Mr Jefferson Smith Mr Whitmore Mr Wilmott  
Mr Tullberg

KNOX  
CHIX  
25/2

Fortified Wines

3. The main reason for the proposed package is the complaint by the Spanish sherry producers that the existing structure illegally discriminates against Spanish sherry. The producers appear to be waiting to see what is in the Budget and Finance Bill. If there is no response to their complaint they will almost certainly act.

4. They could complain to the Commission and this would be likely to lead to the Commission taking infraction proceedings against the UK. The Foreign Office and the Law Officers could be expected to oppose defending a court case which we would be likely to lose. This suggests that if the restructuring is not done now, it should be postponed rather than cancelled, ie, it would be playing for time in the knowledge that restructuring would be a strong starter for next year's Budget. There would be the advantage in taking this course that it would gain time for the British wine makers to adapt. But there would be difficulty in putting up a respectable defence, and the possible embarrassment of capitulating as soon as the first shot was fired.

5. However, there is an alternative, and more problematic, course which the sherry producers or UK shippers might take. They could bring an action in the UK courts in which case the timescale might be considerably reduced, particularly if the Court decided the issue themselves without submitting it to the European Court of Justice for a preliminary ruling. Our legal advice is that we would not have a realistic chance of successfully defending the current position, and if the Law Officers find that there is no case to argue in the UK's defence, normal policy would be to try and avoid the case coming to hearing. In this respect the need to legislate by Finance Act is a serious timing constraint. There are many uncertainties. We do not know whether the Spanish interests have realised that this course is available: we thought it probable that wine importers might take this route at the time of the wine/beer infractions, though in the event none did. Nor do we know whether the UK Court would refer the case to the

/European Court



European Court. Whilst there is a chance that the complainants will not go to a UK Court, and even if they did they would not necessarily obtain a judgment before next year's Finance Bill, a decision not to legislate now involves a perceptible risk.

#### Low Strength Mixed Drinks

6. We regard it as highly desirable to tackle the inadequacy of the current duty structure to provide equitable treatment for the growth areas of coolers and similar low-strength mixed drinks, and to head off complaints from the Commission or importers that the present regime is discriminatory. However, the market for these low-strength mixed drinks has not taken off in the way that it has in America, although a good summer could see further growth with a resultant increase in pressure for change. It is possible that there will be some pressure from trade associations and their members who had hoped to gain from the changes, in particular the spirits industry, but we do not envisage any serious difficulty if the introduction of the new duty band were not included in this year's Finance Bill.

#### Conclusions

7. Even if there were no revalorisation, either or both parts of the proposed restructuring could be implemented. There are clear presentational reasons for not restructuring the fortified wines in the absence of a change to the present duty rates. However, the changes are sensible in their own right and there is something to be said for legislating now, while the initiative still rests with the UK Government, rather than wait until it starts slipping away. No change would almost certainly lead to action by the Spanish sherry producers. If they took the European Commission route we could gain time without undue difficulty, but if they were sharp enough to realise the possible benefits of action in a UK court there would be the risk of an adverse judgment before we could legislate in a Finance Act. Although it would be desirable to introduce a new duty band for low-strength mixed drinks this year, there is no compelling reason to do so.

/8. If restructuring

8. If restructuring were postponed there would be certain presentational problems in view of the discussion paper circulated last June and the subsequent consultations with the trade. There would have to be some announcement, preferably low key and perhaps by means of an arranged PQ. Such an announcement could say that despite extensive consultations it had not been practicable to find a solution which did not have serious drawbacks. At a time when the trade are benefiting from the decision not to increase the drinks duties for a second successive year, it had been decided it was not appropriate to disturb the existing structure and relativities. However, Ministers had asked Customs to continue to examine the problems with a view to finding an acceptable solution.

*Bryce Knox*

B H KNOX



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

*pus*

From: B H KNOX

Date: 12 FEBRUARY 1987

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary  
 Financial Secretary  
 Economic Secretary  
 Minister of State  
 Sir P Middleton  
 Sir T Burns  
 Sir G Littler  
 Mr F E R Butler  
 Mr A Wilson  
 Mr Cassell  
 Mr Monck  
 Mr Sedgwick  
 Mr Odling-Smee  
 Mr Scholar  
 Miss Sinclair  
 Miss Evans  
 Mr Cropper  
 Mr Tyrie  
 Mr Ross Goobey  
 PS/Inland Revenue

*W. M. K. & P. S.*

EXCISE DUTIES

1. This submission rounds up some points to be taken into account in reaching decisions on an excise duty package. They are concerned essentially with the effects on the RPI of different options, and with the issue of wine duty restructuring.

*OK* | 2. Ideally we should like firm decisions on all duty rates by 27 February, although we see no great difficulty in waiting until the overview on Monday 2 March. Thereafter there is an increasing risk of error if more than one or two items remain undecided. It is possible as a contingency to print and

KNOX  
 → CH/EX  
 142

Internal distribution: CPS, Mr Jefferson Smith, Mr Wilmott, Mr Whitmore, Mr McGuigan, Mr Bone, Mrs Hamill.

distribute documentation on specific alternatives, the degree of risk depending on how complicated the changes are and the amount of time given to mount the exercise. If a last minute change were necessary there would be scope for reviewing decisions as late as 3 or even 2 days before the Budget. This particularly applies to tobacco, for which duty changes do not take effect until the Friday after the Budget, affecting relatively few traders. For the other excise duties very late changes could be managed if the decision was between specified alternatives eg 5p or 6p on petrol. We counsel against late decisions or changes for alcoholic drinks, especially this year because of the complexity of the restructuring package and the associated documentation.

#### RPI effects of the Budget

3. The overall impact effect of last year's Budget was 0.6 per cent. This will of course be dropping out of any year-on-year comparison when any changes from this year are registering. The scorecard package at the moment has an effect of 0.45 per cent (0.30 per cent from excise duties), which for public presentation would be rounded to one place of decimals, ie 0.5 per cent. Simple revalorisation would have an impact effect of 0.31 per cent, which (at 0.3 per cent) is what is assumed in the forecast base.

4. If you are concerned to bring down the RPI impact effect of the Budget on the excise side, there are various possibilities. Clearly, to minimise the real impact of the Budget on inflation, a no-change option is best. And, depending on the importance you attach to this point, manipulating duty changes to take advantage of differences between real impact figures and those announced publicly may not be attractive. But, assuming that the non-excise impact effects remain at 0.15 per cent (which, in terms of public presentation, sets an RPI "floor" of 0.2 per cent), there is some room for manoeuvre on the excise duties within the publicly-announced impact figure. It is set out in the following table:

*Surely it is the true impact on the RPI we're interested in, not what we publish as the (rounded) impact?*

*g. Am. 11!*

## BUDGET SECRET

	<u>RPI impact effect of Budget (to 1 decimal place)</u>	<u>maximum impact effect (to 2 decimal places)</u>	<u>constant non-excise effect</u>	<u>maximum excise impact effect</u>
A	0.2	0.24	0.15	0.09
B	0.3	0.34	0.15	0.19
C	0.4	0.44	0.15	0.29
D	0.5	0.54	0.15	0.39

5. Of these D allows you to go slightly beyond simple revalorisation, for example by shading up the increase on cigarettes. C is just below the existing package, which, you will recall, has a scorecard cost in both years of £20 million. This could be manipulated, eg by reducing the spirits duty increase slightly, to 1.5 per cent, with an additional scorecard cost of £10 million in 1987-88 and £15 million in 1988-89. A and B, however, would necessitate a more fundamental rethink of the package.

6. We suggest that consideration of any package which aims at less than revalorisation should start with cigarettes, because this is the area where anything less than revalorisation is likely to create more political problems than otherwise. You have had strong pleas from the industry for a year's standstill; but it is notable that when MPs for manufacturing constituencies saw the Minister of State, they reinterpreted this as a plea for no more than revalorisation. The health interests would strongly criticise anything less than revalorisation. We therefore suggest that, if you were looking for a package to fit either line A or line B in the above table, cigarettes should be its main focus.

7. Option A limits the scope for action considerably (to rather less than one-third revalorisation across-the-board, for example). A VED standstill cannot be financed by over-indexing the oils duties, since the current favoured VED/petrol/derv option has an RPI impact effect of 0.12 per cent. You may consider it unattractive to spread duty rises generally across the excise products, since this permits only very small changes in individual rates (eg,

0.2p on a pint of beer). It might therefore be preferable, in line with paragraph 6, to load the whole of the excise increase on to cigarettes. This would still amount to less than revalorisation for that duty: the rate would go up by 3.5 per cent, with a price rise of 3.2p for twenty cigarettes. The scorecard cost of the whole package would be £435 million in 1987-88 and £480 million in 1988-89.

8. To achieve B, you could for example fully revalorise cigarette duty, and in addition roughly half-revalorise (ie increase by 2 per cent) the duties on alcoholic drinks (other than spirits and cider), petrol and derv (but not VED). This would produce the following result:

[practical alternatives:  
sk → still  
unlower cigs only  
0.15 a RPI  
0.25 a RPI  
diff in cost: £90m / £100m ]

**BUDGET SECRET**

	Price change including VAT on typical item (1)	Scorecard		RPI
		1987-88 £m	1988-89 £m	impact effect (2) %
Beer	0.4p per pint	- 25	- 30	0.02
Cider	No change	- neg	- neg	nil
Wine (3)	1.6p per 70cl table wine	- 10	- 10	0.01
Spirits	No change	- 25	- 30	nil
Tobacco (4)	3.4p per 20 KS	0	0	0.10
Petrol	2.0p per gallon	- 85	- 95	0.05
Derv (5)	1.7p per gallon	- 20	- 20	(see note 6)
VED - cars	No change	- 75	- 80	nil
- other (7)	No change	- 15	- 15	nil
Minor duties (8)	No change	- 5	- 5	nil
<b>TOTAL</b>		<b>- 260</b>	<b>- 285</b>	<b>0.18</b>

neg = negligible

- (1) VAT payable in addition to the duty except in the case of VED.
- (2) Based on December RPI.  
Rounded to 2 decimal places.
- (3) Re-structuring of wine duties not taken into account.
- (4) Cigarettes, HRT and cigars increased.
- (5) Most derv consumers can reclaim VAT.  
Revenue estimates assume 9% offset for bus fuel grants.
- (6) RPI weight for derv not yet known, but impact effect likely to be negligible.
- (7) No change in main lorry and most other VED rates costs £20m, offset by £5m gain from increases on farmers' lorries and trade licences, and creation of new tax class for recovery vehicles.
- (8) Minor oils, matches & mechanical lighters.

9. To help you evaluate the consequences for the RPI of different possibilities, I attach a ready-reckoner of revenue and price effects for an impact effect per duty of 0.01 per cent. The aggregate results from using such a table are of course imprecise, and we should need to provide detailed costings of any preferred option. A similar health warning attaches, a fortiori, to other costings and options in this part of the submission, not least because of possible changes in the RPI itself.

Restructuring of the wine duties

10. A decision to proceed with a restructuring of the wine duties needs to be seen against the background of the overall shape of the excise package (as determined in the light of the considerations set out above). In particular, you will wish to consider the presentational implications of making these technical (and RPI- and revenue-neutral) adjustments if otherwise the drinks duties are to remain unchanged. The disadvantage of not proceeding with adjustments this year is that the Spanish sherry interests could be expected to resort to legal proceedings in which the Government's case would be so poor that the Law Officers would probably resist even attempting a defence.

*discuss*  
*don't AS make?*  
*the new will you?*

11. Detailed submissions were made to the Minister of State on 6 November and 8 January. He agreed to the proposals outlined below (Mr Judge's minute of 29 December). Informal soundings of officials of other Departments suggest that they would be acceptable as "least bad" solutions.

Fortified Wines

12. The proposal is to create a new duty band for fortified wines and made-wines between 13% and 15%. The duty on these wines and the higher strength fortified wines should be adjusted so as to be more proportionate to strength both in relation to each other and to table wines. The changes should be phased in, but there is no need to commit yourself at this stage beyond the initial step. The existing duty structure and differentials and the changes proposed for 1987, which would go about a third of the way, are as follows:



BUDGET SECRET

Strength

Differentials over table wine  
(duty and associated VAT in p. per  
70 cl bottle)

	<u>Now</u>	<u>Proposed change</u>
Table wines up to 15%	-	-
Fortified wines 13-15%	-	+4
Wines 15-18%	+57	-8
Wines 18-22%	+78	-8

13. As part of the proposals, the prohibition on blending of duty paid wines, introduced in 1985, would be reversed.

14. Those affected by the increase would include all the main vermouths, British sherry, Cyprus sherry and fortified wines such as ginger wine. The main beneficiaries of the decrease would be Spanish sherry and port. For British sherries made by blending high and low strength made-wines, the cut in the 15-18% rate would approximately halve the increase resulting from the new 13-15% band.

15. The purpose of the proposal is to demonstrate to the Spanish sherry producers that we are taking effective steps to answer their complaint against our discriminatory duty structure so as to stave off legal action, while minimising the impact on British and Cyprus sherries but nevertheless giving a warning. Because of the latter point, and the sensitivities of the Italians to anything that might be construed as an attack on vermouth, we would recommend against any differential for 13-15% fortified wines which went above 4p.

16. The case for making a cut in the duty on Spanish sherry (and consequently port) is that it would be a direct benefit to the Spanish complainants, who might otherwise feel that they had gained too little; that it would mitigate the impact of the 13-15% increase on British sherry producers; and that it would start to tackle the present excessive differential between higher strength fortified wines and table wines. Against that, an absolute cut might be presentationally difficult, and could offend the spirits industry. Nevertheless, we suggest that the package should be taken as a whole, particularly if it is wished to present it as revenue neutral. The formula of putting half as much on 13-15% fortified wines as is taken off the higher strength wines achieves this neutrality.

17. The restructuring can be linked with any revalorisation of wine duty rates or none. If linked with revalorisation, the increase on 13-15% fortified wines becomes 4p plus the revalorisation increase; the decrease for higher strength wines becomes 8p minus the revalorisation increase. The resulting figures could be helpfully rounded to whole or half pence per bottle; we would make recommendations in the light of whatever package was decided on.

*or  
disposal?* / /

18. In the event of no revalorisation, the restructuring would stand out on its own. We suggest that it would be all the more necessary to present it as revenue neutral, and a sensible administrative response to changing trade patterns which required revision of the duty relativities.

#### Sparkling Wine

19. This is not something mentioned in previous papers, but it may be worth considering now.

*how ??* /

20. Sparkling wines are taxed at a rate some 65 per cent higher than that on table wine (the absolute difference, including consequential VAT, is 51p on a 70 cl bottle). Revalorisation has increased this differential over the years in nominal terms, but the 1984 Budget increased it sharply in real terms by cutting the table wine duty. By itself the sparkling wine duty is a modest revenue-raiser (£41 million in 1985/86, or under 7 per cent of wine duty receipts, excluding made-wine), but sales are buoyant and the EC beer/wine constraint does not apply. If the duty on fortified wines of 13-15% is increased, over and above any other Budget changes, by 4p a bottle, you might like to consider if it was presentationally helpful for sparkling wine - seen as a luxury product - to bear the same increase. This would amount to a 3 per cent rise in the duty, which the market should stand without difficulty, and would raise an extra £1 million. There appears to be a very small amount of sparkling wine above 15%, at present taxed at the same rate as still wine. To avoid this falling below the rate for sparkling wine up to 15%, the up to 15% rate should be extended to all sparkling wines.

Implementation

21. If you agree to these changes, they would operate from 6.00 pm on Budget Day.

Low Strength Mixed Drinks

22. This is less contentious and difficult. The proposal is to create a new duty band to cater for the growing category of low strength drinks, for which the present duty structures in respect of their components does not adequately provide. The proposal is to introduce a new structure for coolers and similar mixed drinks containing between 1.2% and 5.5% alcohol, with the duty charged per degree of alcohol at a rate set at a level per degree of approximately one fifteenth of the table wine duty.

23. Traditional beer-based products such as shandy and lager and lime would bear beer duty and not the new duty rate, but with no additional duty charge on the non-alcoholic ingredients. This would be less favourable than allowing them to be taxed in the new mixed drinks category, but is necessary to prevent avoidance by the addition to beer of small quantities of non-beer additives. Informal soundings of the Brewers' Society suggest they will go along with this.

24. The revenue effect of these proposals would be negligible.

25. Because consultations with the trade will be needed on the workings of the new regime and existing subordinate legislation will have to be amended, we recommend that although the changes would be included in the Finance Bill, they should be brought into effect by a Commencement Order later in the year.

*Shandy  
or  
w. H. W.?*

Bryce Knox

B H KNOX

**BUDGET SECRET**

**READY RECKONER: RPI IMPACT EFFECTS OF 0.01% FOR MAIN DUTIES**

The larger the increases, the less accurate is this ready reckoner.

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	Price change including VAT on typical item (1)	Yield (2)		RPI impact effect (3)
		1987-88 £m	1988-89 £m	
Beer	0.2p per pint	14	14	0.01
Wine (4)	1.3p per 70cl table wine	8	9	0.01
Spirits	7.1p per 75cl	9	10	0.01
Tobacco (5)	0.4p per 20 KS	11	11	0.01
Petrol	0.4p per gallon	20	22	0.01
VED on cars	£1.10 per year	23	23	0.01

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(1) VAT payable in addition to the duty except in the case of VED.

(2) Rounded to nearest £1m. To obtain overall scorecard cost, total individual yields and subtract from £525 million (1987-88) and £575 million (1988-89).

(3) Based on December RPI.  
Rounded to 2 decimal places.

(4) Revenue and RPI effects assume same percentage increase on all wines.

(5) Revenue and RPI effects assume same percentage increase on all tobacco products, except pipe tobacco.



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

From: P Jefferson Smith

Date: 26 February 1987

PS/MINISTER OF STATE

cc PS/Chancellor  
 Mr Scholar  
 Miss Sinclair  
 Mr Jenkins  
 (Parly Counsel)

VAT : SALES OF HOLIDAY PACKAGES BY TOUR OPERATORS (STARTER NO. 4)

1. Ms Ryding's minute of 20 February refers.
2. The tour operators' scheme, and Article 26 of the Sixth Directive under which it is required, is sui generis. Thus there are no exact precedents. But within VAT law, there are several examples of a general principle being established in primary law, with the details being filled in by or under subordinate legislation. This is the case with the schemes for second hand goods and for dealings on the terminal markets, and with the special schemes for retailers.
3. Perhaps the second hand goods schemes are nearest to the tour operators schemes in conceptual terms. The value for tax in these schemes is also based on the difference between buying in and selling prices. These schemes are imposed by Treasury Order made under section 18 of the VAT Act 1983. Such an Order requires only a negative resolution. The schemes are subject to "such other conditions [being] satisfied as may be specified in the Order or as may be imposed by the Commissioners in pursuance of the Order". The Terminal Market Scheme is underpinned by Treasury Order (negative

---

**Internal circulation:**

CPS	Solicitor	Mr Wilmott
Mr Knox	Mr Howard	Mr Tracey

resolution) made under section 34 of the Act and the Order may make provision for "modifying the provisions of this Act in their application to dealings on terminal markets . . . . subject to such conditions as may be specified [in the Order]".

4. So far as the special retail schemes are concerned, their purpose is not so much to modify the basic VAT rules on supply, tax value etc. but to lay down detailed rules to enable retailers to ascertain what the total tax value of their supplies is in each tax period. These detailed rules are set out in Notices or Leaflets published under authority of Commissioners' regulations made under paragraph 2 of Schedule 7 to the VAT Act. These regulations are subject to the negative procedure.

5. It could be objected that all these are examples of relieving provisions, whereas the tour operators provision is a taxing measure. The answer is as indicated in my previous note: it is the clause that is really the taxing measure, not the Order which it enables. But for examples of statutory instruments which can raise additional tax and are subject to the negative procedure, it is possible to cite Commissioners' regulations governing the machinery of the tax. In 1984, the postponed accounting system for imports was withdrawn by such regulations. Also in 1984, and again this year, the partial exemption rules were or will be modified by negative procedure regulations. In the case of partial exemption, the fact that the negative procedure applies has attracted criticism, mainly outside Parliament. But it has not led to any concrete move, e.g. by a Committee Stage new clause moved by the Opposition or Government backbenchers, to impose an affirmative resolution requirement.

*PH*

P Jefferson Smith


 COPY NO 16 OF 18
 1. Andrew
2 pup

FROM: A C S ALLAN

DATE: 4 March 1987

PS/MINISTER OF STATE

 cc PS/Chief Secretary  
 PS/Financial Secretary  
 PS/Economic Secretary  
 Sir P Middleton  
 Sir T Burns  
 Mr Cassell  
 Mr Scholar  
 Mr Culpin  
 Miss O'Mara  
 Miss Sinclair  
 PS/C&E  
 Mr Knox - C&E  
 Mr Jefferson Smith - C&E  
 Mr Wilmott - C&E

 ACSA  
 To  
 PS/MAST  
 4/3
**EXCISE DUTIES**

The Chancellor feels it is very important to work out carefully our line on non-revalorisation of excise duties. He would be grateful if the Minister of State could prepare a suitable note.

2. He feels that the line "we don't need the money" will need to be used with great care. There are obvious awkwardnesses with eg prescription charges. He doubts it will be useable in the House of Commons; and outside, it may need to be turned into something a little softer, like "it would not have been appropriate given the overall shape of the Budget". It will be a line that men in the street may use among themselves in discussing why we did not raise excise duties; but it is a difficult one for us to use directly.

3. There is scope for using the line that the particular profile of inflation expected this year - the "hump" or "blip" - makes it sensible for us to take special action so as to minimise any damage to inflationary expectations etc. But this also needs to be used with care.



4. The most important argument will be the point that taking all of the specific duties together, the rates have increased (slightly) in real terms during the Chancellor's period in office. The "broad presumption" of indexation is not one which applies to any single year. Mr Scholar and Mr Wilmott can help write the numbers on this.

5. A related argument is that in this Budget there is still a net shift from direct to indirect taxation. Perhaps FP could provide the Minister of State with the figures needed to back this up.

ACSA

A C S ALLAN





Ch

May want to raise  
this @ 3PM meeting  
(before separate needs a  
presentation later this week).

discussed - but  
10/5/11  
assess  
Seofon

AA

\* x  
agreed



FROM: S P JUDGE

DATE: 6 March 1987

PRINCIPAL PRIVATE SECRETARY

- cc Chief Secretary
- Financial Secretary
- Economic Secretary
- Sir P Middleton
- Sir T Burns
- Mr Cassell
- Mr Scholar
- Mr Culpin
- Miss O'Mara
- Mr Pickering
- Miss Sinclair
- Mr Mowl
- Mr Romanski
- Mr Cropper
- Mr Tyrie
- PS/C&E
- Mr Knox - C&E
- Mr Jefferson Smith - C&E
- Mr Wilmott - C&E

*I am not proposing this. We already have a head of products which I will be doing. @ say say the press.*

*Ch  
Want for X, but must A  
this is too negative.*

*This is AA  
not on a point  
Budget: had it with  
some for the  
to be had  
further further.*

15/MST  
to  
ACSA  
613

**EXCISE DUTIES: PRESENTATION**

The Minister of State discussed your note of 4 March this afternoon with Mr Knox, Mr Wilmott, Mr Mowl, Mr Romanski, Mr Pickering and Mr Tyrie. The Minister of State asked officials to revise the Budget Brief on this subject; EB will submit this to Ministers as soon as possible. But the Minister thought the Chancellor would welcome an indication of the general line that emerged.

2. Mr Mowl confirmed that unfortunately the proportion of revenue from indirect taxes was expected to fall as a result of the Budget, from 52.8 per cent to 52.6 per cent. Mr Romanski thought that personal taxes would show a shift to indirect; the Minister of State agreed that we could not lead with this, but it was a usable defensive line.

3. Mr Wilmott said that Customs were re-working the indices of real values of duty rates; the all-alcohol index was likely to be below the pre-1979 Election level. The Minister of State thought

*PSR for  
mt  
8th June  
ASPP*

*not what  
to last  
show  
evk  
1983  
psych  
to this  
check*



*we shall almost certainly be forced to do so (eg by PQs)*

this would cause problems, although the indices would not be published (partly because of the difficulties with comparing weights). Mr Wilmott said the Government could refer to the cut in wine duty caused by the European Court decision; say that beer duty had been put up steadily (referring to DHSS evidence that most alcohol-related health problems are associated with beer) and (with care) refer to the employment and export impact of decisions on spirits.

4. It is helpful that there is no consistent story to tell on excise duties over recent years; even so, awkward questions could be asked about why the Government had over-indexed in the last Parliament and barely kept pace with inflation in this one.

5. Mr Tyrie expected three main lines of attack:

- Health. Why was the Government ignoring the evidence?
- Inflation. Why was the Government massaging the RPI figures?
- Electioneering. The Opposition might claim that income tax cuts had minimal employment benefit, and by binding income tax cuts and excise duty freezes together, claim that this was clearly a pre-Election Budget.

A first - if rather irrelevant - response is to say "as with all other taxes, Labour want to put excise duties up". It would be useful to have a list of Labour MPs who had made Budget representations for duty standstills, on behalf of local manufacturers.

6. The "inflation" point would be shown to be false if the Election was not until October, but would be more in June. Mr Tyrie said that reference should be made to Mr Hattersley's earlier forecasts, which had most often been wrong on growth, and note that most City forecasts were similar to the Government's. The Minister of State asked for the briefing to mention outside inflation

*This list  
is  
to  
be  
made  
in  
the  
briefing*


*awkward*

forecasts. Mr Tyrie thought a general "I do not need to take lectures from Honourable Gentlemen opposite about inflation" line would be useful.

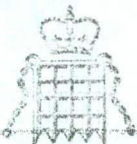
7. The main problem is with spirits. The "jobs and exports" line could be used against the Government in future. The Minister of State agreed that there was a robust line on wine, and asked for the briefing to mention the enormous growth in production of English table wine. Mr Wilmott thought the main point to make about the duty decisions was that they were good for ordinary people and the trades concerned; the only problem would be with the health lobbies.

8. Customs expected continued growth in the imports of cheap cigarettes, so that provides no defence of the duty standstill, save that the trade has asked for it. There was no evidence that British manufacturers would take advantage of the duty standstill to actually start competing in this market.

9. The Minister of State would be grateful for the Chancellor's comments on this proposed line.



S P JUDGE  
Private Secretary



H.M. CUSTOMS AND EXCISE  
KING'S BEAM HOUSE, MARK LANE  
LONDON EC4A 3DF

Please Dial my Extension Direct:  
Use Code (01)-382 followed by  
Extension Number 5...023

From P G WILMOTT

Date 6 MARCH 1987

1. Mr ~~Knox~~ BK 6/3
2. Minister of State

cc **Chancellor**  
Chief Secretary  
Mr Scholar  
Miss Sinclair  
Miss O'Mara  
Mr Culpin  
Mr Romanski  
Mr Walters

**BUDGET PRESS NOTICES**

This note submits our notices for your approval.

2. As last year, there are notices for all those items included in the Speech or FSBR (the latter includes some minor items requiring Resolutions). This year we have six notices on VAT (small businesses, partial exemption, imported services, registration threshold, charities and tour operators) and two on excise duties (betting and gaming and unleaded petrol). The Chief Secretary has asked (Miss Rutter's minute of 4 March) to see notices affecting business.
3. You may recall that conventionally our notices on Budget measures tend to be confined to bald statements of the changes, the political gloss being given elsewhere on Budget publicity.

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Internal distribution: CPS, Mr Knox, Mr Jefferson Smith,  
Mr Howard, Mr Bone.

Timing

4. We are planning to start printing press notices on Tuesday 10 March, to fit in with the FP's timetable. We shall need to know that you are content with them by that morning.



P G WILMOTT



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

From: P Jefferson Smith

Date: 6 March 1987

MINISTER OF STATE

*Resist with strong  
to ensure X  
2. What is the value added  
of the new services  
to the business  
and how?*

cc PS/Chancellor  
Mr Scholar  
Miss Sinclair  
Mr Ilett  
Mr Dyer  
Mr Cropper  
Mr Jenkins  
(Parly Counsel)

VAT TAX AVOIDANCE : STARTER NO. 6

1. Although the VAT tax avoidance package is directed essentially at the problem of over-deduction of input tax, it involves a complex and long package of legislation. This note outlines what is involved and reports on the present state of the work. It is mainly for information, but seeks a decision on the proposed treatment of services in relation to capital issues (paragraphs 9 to 12).

The Legislation

2. As foreshadowed in the Chancellor's announcement on 19 December, the legislation will be partly primary and partly secondary. Drafting is either complete or at a very advanced stage. The primary legislation will be in Budget Resolutions and Finance Bill clauses as follows. (In each case the title is that appearing in Counsel's latest draft of the Budget Resolution.)

(a) Value Added Tax (Credit for Input Tax)

This Resolution and clause will have seven provisions amending Section 15 of the VAT Act 1983. These are the key provisions, since they limit recovery of input tax to that which is properly

Internal Circulation:

CPS	Solicitor	Mr Nissen	Ms Barrett	Mr Michie
Mr Knox	Mr Butt	Mr E Taylor	Mr Wilmott	

attributable to taxable supplies, extending the vires of the Commissioners' regulation making powers to allow practical effect to be given to the principle. Because there would otherwise be a restriction of an existing right which is properly allowable under the Sixth Directive, input tax recovery is allowed in relation to certain supplies made overseas or in a UK warehouse.

(b) Value Added Tax (Supplies to Groups)

This adds a new section to the VAT Act, providing that a partly exempt group of companies registered as such for VAT purposes can be required to account for VAT on acquisition of business assets or transfer of a business as a going concern. The provision is long and complex, but is needed to block an easy and well known avoidance device.

(c) Value Added Tax (Valuation)

A brief provision allowing exempt supplies between connected parties to be valued at open market value.

(d) Value Added Tax (Issue of Securities)

A brief provision, exempting the service of making arrangements, including underwriting, for capital issues.

3. All these provisions are drafted to come into effect from 1 April. In addition, there will be

(e) Value Added Tax (Supplies Abroad etc)

A short resolution is required to pave the way for a Finance Bill clause allowing for registration of businesses not making taxable supplies within the UK to enable them to recover input tax in relation to the overseas supplies mentioned at (a). The Resolution is needed because an existing relief will be repealed: we are looking at ways of ensuring that the Resolution is not so wide as to undermine the restrictions in the amendment of the law resolution.



## BUDGET - CONFIDENTIAL

(f) A Finance Bill clause (a resolution is not required) allowing appeals to Tribunals in disputes over apportionments of input tax for partial exemption purposes.

4. Items (b) and (c) require derogations under Article 27 of the Sixth Directive. The two months period for Member States to raise any objections expires on 12 April; in the event of no objections, the Commission has undertaken to date the derogations from 1 April.

5. The secondary legislation will take the form of Commissioners' Regulations made under Section 15 of the VAT Act as extended by the Resolution at 2(a). The final text is going to the printer; as earlier reported, we would propose to issue the draft informally on Budget Day, and make and lay immediately following the Budget Debates, i.e. on passing of the Resolution.

6. Making a statutory instrument under the cover of a Budget Resolution operating under the Provisional Collection of Taxes Act is a highly unusual procedure. In fact, there appears to be only one precedent, a provision introduced in the 1984 Budget to allow relief from duty and VAT in respect of imported legacies. However Parliamentary Counsel advises that the PCTA can be used in this way. We have also shown the Regulations in draft to Speaker's Counsel and explained about the proposed use of the PCTA. He accepts that a PCTA Resolution will provide a sufficient basis for the Regulations. Inevitably, they will be in breach of the twenty-one day rule. Speaker's Counsel gave us no indication on the point, but we imagine that the Select Committee on Statutory Instruments might well report the use of the PCTA for the Regulations to the House as involving an unusual use of powers.

7. The text of the Resolutions is in the first print which Counsel circulated yesterday. If you would like to see the draft Regulations would your Secretary please let me know.

## BUDGET - CONFIDENTIAL

8. All these items will be covered as a single item in the FSBR and will be the subject of a Budget Day press notice.

### X Capital Issues

9. During our consultations with interested bodies the point was made that the new input tax rules would put a serious additional burden on the raising of capital, because input tax relating to issue of shares or other exempt securities would no longer be eligible for deduction. It was also claimed that, as a result of our failure to implement the exemption for financial services in the VAT Sixth Directive (from which we have a derogation), some of the business of issuing Eurobonds might go offshore to Holland. The Chancellor therefore undertook, in the announcement of 19 December, to consider the possibility of exempting services in relation to capital issues. The Sixth Directive permits exemption for 'transactions, including negotiation' in relation to securities: we would see this as covering, for example, underwriting and the actual management of a new issue, but not legal or accountancy advice in relation to it.

10. We sent a circular letter to the main bodies likely to be interested, asking for their views on extending exemption to underwriting and the making of arrangements for capital issues. The response has been mixed. About half of those who have replied are in favour of the proposal. There is, however, a strong body of opinion, led and possibly orchestrated by the British Bankers Association, who argue that it does not go far enough. The exclusion of legal and accountancy services will, they claim, still leave a heavy burden of sticking tax on companies' raising of capital, and there is a danger that issues may in future be organised offshore in order to avoid VAT. The objectors do not want legal and accountancy services also exempted (this would make many lawyers and accountants partially exempt, with all the attendant complications); instead, they propose that the new partial exemption rules should be adapted in order to allow tax related to capital issues to be in principle deductible.

## BUDGET - CONFIDENTIAL

11. The British Bankers Association do of course have a major interest in the proposal, in that their members stand to lose a substantial proportion of input tax. It cannot be denied that, even with the exemption of the services proposed, more tax will stick in connection with capital issues than did before. Whether companies planning issues will in fact find it worth their while to involve overseas agencies or companies (e.g. in Luxembourg or the Channel Islands) in organising the issues is open to question (partly exempt traders, who already suffer some restriction on their right to deduct, have not yet tried to do so), but it is a possibility that must be recognised, and which the Bank of England think may be a significant one. To go along the lines suggested by the objectors, however, and allow tax related to capital issues to be deductible would depart from the basic principles on which the present package is based, which are to relate input tax recovery strictly to taxable outputs, and would make it considerably more difficult to resist all the other claims for special treatment which are bound to be made in connection with the package.

12. Even if it were to be conceded that the proposed exemption for making of arrangements and underwriting does not go far enough, it would be impossible in the time now available to work out before the Budget any further relief which was practical and did not have repercussions. We recommend therefore that, despite the objections of the BBA and others, we go ahead with the exemption as drafted, recognising that it will give only a partial relief from the additional input tax burden which will be incurred in this area. If this does in the future give rise to a real and imminent threat of significant numbers of issues being organised offshore, the possibility of remedial action to allow more extensive deduction in this area still remains. But the arguments for offering a further concession at this stage or not proven.

ph ✓

P Jefferson Smith



FROM: CATHY RYDING

DATE: 9 March 1987

PS/MINISTER OF STATE

cc Mr Scholar  
Miss Sinclair  
Mr Ilett  
Mr Dyer  
Mr Cropper  
Mr Jenkins - Parly Counsel  
Mr Jefferson Smith - C&E  
PS/C&E

**VAT TAX AVOIDANCE: STARTER NO.6**

The Chancellor has seen Mr Jefferson Smith's minute to the Minister of State of 6 March.

2. The Chancellor has commented that the Economic Secretary will obviously be considering the proposed treatment of services in relation to capital issues (paragraphs 9-12).
3. The Chancellor would be grateful to know the latest state of play on the brewers and their tied houses.

A handwritten signature in cursive script, appearing to be 'CR'.

CATHY RYDING



FROM: A C S ALLAN

DATE: 9 MARCH 1987

MR WILMOTT - C&amp;E

cc PS/Minister of State  
Sir P Middleton  
Mr Cassell  
Mr Scholar  
Miss Sinclair  
Mr Romanski

**EXCISE DUTY RATES**

I understand that you are reworking the figures for the real level of excise duties since 1979.

2. You earlier supplied (via Mr Scholar) figures deflated by the difference between the June 1983 and December 1986 RPI. The Chancellor would be grateful if you could update the figures to include the latest estimate of the February RPI. And if you could do similar figures for the previous Parliament (ie May 1979 to June 1983).

3. He feels the changes should take on board the effects of the VAT increase in June 1979. He assumes that the inclusion of VAT would not make any difference a year in which VAT was unchanged. If this is not true the effects should be included in the tables.

4. He would be grateful if the results could be circulated to all Ministers and advisers.

ACSA

A C S ALLAN

BUDGET SECRET



Copy No. 21 of 22.

FROM: A C S ALLAN

DATE: 9 MARCH 1987

PS/MINISTER OF STATE

- cc Chief Secretary
- Financial Secretary
- Economic Secretary
- Sir P Middleton
- Sir T Burns
- Mr Cassell
- Mr Scholar
- Mr Culpin
- Miss O'Mara
- Mr Pickering
- Miss Sinclair
- Mr Mowl
- Mr Romanski
- Mr Cropper
- Mr Tyrie
- PS/C&E
- Mr Knox - C&E
- Mr Jefferson-Smith - C&E
- Mr Wilmott - C&E

ACSA  
to  
PSMET  
9/3

*For Budget  
Presentation meeting  
folder*

**EXCISE DUTIES: PRESENTATION**

The Chancellor was grateful for your minute of 6 March. He will want to discuss this further with the Minister of State and others at a meeting on presentation.

2. He noted that, at the Minister of State's meeting, Mr Mowl said that the proportion of revenue from indirect taxes was expected to fall as a result of the Budget. This is surely not a result of the Budget: had it not been for the Budget the percentage would have fallen further. I should be grateful if Mr Mowl could provide the necessary figures.

3. He would be grateful to see Mr Wilmott's reworking of the indices of the real value of duty rates as soon as possible.

BUDGET SECRET



4. He would also be grateful if Mr Tyrie could draw up the list of Labour MPs who have made representations for duty standstills: it will include Mr Blair.

ACSA

A C S ALLAN

BUDGET SECRET



FROM: S P Judge

DATE: 9 March 1987

PS/CHANCELLOR OF THE EXCHEQUER

cc PS/Chief Secretary

Mr Scholar

Miss Sinclair

Miss O'Mara

Mr Culpin

Mr Romanski

Mr Walters

PS/Customs & Excise

Mr Knox - C&E

Mr Jefferson Smith - C&E

Mr Howard - C&E

Mr Bone - C&E

*A few dozen matters, some basically I agree with the MST. However re Y, it is essential that the head of the matter is (b) that an appeal arrangement (whether to be made or not) as referred to in No Press Notice.*

*with I have marked a text*  
Fairly detailed comments from MST, all of which seem fine. The only point I think you need focus on is Y over the page. I think the presentational aspects are best left to HMT. Content?

CR 913

**BUDGET PRESS NOTICES**

The Minister of State has seen Mr Wilmott's submission of 6 March. This minute records his views on the press releases as currently drafted; if the Chancellor is content then I will ask Customs to redraft accordingly.

Customs confirmed that they would not wish to issue a press release on excise duties. They prefer to concentrate on the factual aspects of the changes, and leave the presentational slants to the Treasury, drawing on the Budget Brief.

VAT: Small Business Review (16/87): the Minister expects that "exposed" in paragraphs 4, 8 etc is technically correct, but thinks that "published" would do just as well.

*yes*

Paragraph 5, line 2: insert ", " after "and".

*yes*

Paragraph 6, line 5: replace "and," with ": **T**hey".

*yes*

Paragraph 7: insert "also" after "scheme" and replace "proposal" with "proposed".

*?*

Paragraph 8: insert comma after "clause".



Paragraph 10, line 5: the Minister thought that the announcement of the deferment was unduly *defensive*, and suggests replacing "have to" with "need to", or (preferably) *omitting it altogether*.

Paragraph 12: the Minister thinks that the fifth change ("de-registered businesses will not be liable to registration only because of turnover before deregistration") needs to be made clearer. The test is whether a person on the Clapham omnibus will understand it.

Retail schemes: I think that the sixth change "Regulation 3...." should also be indented. The Minister suggests replacing "for clarification purposes" with "to improve clarity". The Minister suggests that the sentence on revenue effects should start "It is estimated that cash accounting will cost £100 million ...".

In the background notes, the Minister would be grateful if Customs could change "hon" to "Hon".

*302\**  
Yes  
VAT: Input Tax: origin and scope of the right to deduct (17/87): the Minister found the title of this press notice somewhat indigestible, and suggests that it be relegated to a sub-title below a somewhat shorter main title. The Minister notes that the section on deductible input tax does not cover the main presentational points (businesses have had lots of notice; special *agreement* with the brewers; many firms will continue on existing special methods; existing accounting information will be used; not as bad as predicted for small businesses). He is content with this, given that they are intended as primarily technical notices.

Are you content?  
The Minister thought that the section on the regulations (last page) should have appended ", and are available in the interim in the Library of the House", as defensive briefing.

VAT on services imported by unregistered businesses (18/87): the Minister suggests inserting "to" after "and" on line 3 of

BUDGET SECRET

the second paragraph, and "and" before "professional" on line 4 of the following paragraph.

Registration and deregistration (19/87): insert a comma after line 4 of (b)(ii). - to after "£21,300"

Betting and gaming duties (23/87): the Minister of State would be grateful if Customs could check that the section on on-course betting duty (which refers to its being **abolished**) is consistent with the technical decision to set a **zero rate** of duty.

I apologise for the rather disjointed nature of this note, which is caused by the need to get comments to Customs by close tonight.

S.P.J.

S P JUDGE  
Private Secretary



COPY NO 15 OF 15 COPIES

FROM: CATHY RYDING

DATE: 9 March 1987

PS/MINISTER OF STATE

cc PS/Chief Secretary

Mr Scholar

Miss Sinclair

Miss O'Mara

Mr Culpin

Mr Romanski

Mr Walters

PS/C&amp;E

Mr Knox - C&amp;E

Mr Jefferson Smith - C&amp;E

Mr Howard - C&amp;E

Mr Bone - C&amp;E

**BUDGET PRESS NOTICES**

The Chancellor has seen Mr Wilmott's minute to the Minister of State of 6 March attaching draft Budget press notices, and your minute to me of 9 March detailing the Minister of State's comments.

2. The Chancellor had a few additional changes, which are detailed below, but basically he agreed with the Minister of State's suggestions. However, on the Minister's comments on VAT: imput tax: original and scope of the right to deduct (17/87) the Chancellor thinks that it is essential (a) that the heading is made much clearer and (b) that any special arrangements (whether for brewers or anyone else) are referred to in the Press Notice.

3. The Chancellor had the following additional detailed comments on the Press Notices:-

VAT: Small Business Review

Paragraph 1, line 2: Replace "News" with "Press".



Paragraph 6, line 5: Redraft to read "a year instead of the present four. They would make 9 equal payments on account,".

Paragraph 7, line 1: The Minister suggested inserting "also," after "scheme", but the Chancellor would prefer "too".

Paragraph 10 on Default interest and penalty for serious misdeclaration: Delete.

Paragraph 12, indent 5: The Chancellor suggests redrafting as follows:-

"turnover before deregistration will not render deregistered businesses liable to registration."

VAT: Registration of deductible input tax: etc (17/87) - (b). The Chancellor thinks that the Press Notice should spell out what is *Zero Group 15 Item 2 of the 1983 Vat Act* .

CR

CATHY RYDING

CR 4/3

pur.

**Covering BUDGET CONFIDENTIAL**

*9/1'm afraid this page was left out of the bunch of press notices you saw this afternoon. Content?*

**From: MISS A T CUNNINGHAM**

**Date: 9 MARCH 1987**

**Minister of State**

CR 913

*OK*

- cc **Chancellor**
- Chief Secretary**
- Mr Scholar**
- Miss Sinclair**
- Miss O'Mara**
- Mr Culpin**
- Mr Romanski**
- Mr Walters**

**B U D G E T P R E S S N O T I C E S**

The attached sheet was omitted from Press Notice No 16/87 'VAT: Small Business Review' (circulated on Friday 6 March from Mr Wilmott, C&E). This page is to become page 5 of Notice No 16/87.

I apologise profusely for this omission and hope that the inconvenience caused was minimal.

*A Cunningham.*

**MISS A T CUNNINGHAM**  
**Personal Secretary**

**9 March 1987**

---

**Internal distribution: CPS, Mr Knox, Mr Jefferson Smith, Mr Howard, Mr Wilmott, Mr Bone.**

As proposed in the consultation paper, this new scheme will operate in the same way as the old adaptation except that the calculation of expected selling prices of only standard-rated goods received for resale will be required.

The lower annual turnover limit for Scheme G will be abolished, while the 1/8th uplift, having been reviewed, will remain unchanged.

The "How to work Scheme J" pamphlet will be amended to include the available scheme J adaptations.

This is in line with the proposal in the consultation paper.

The "standard" method of reckoning gross takings will remain unchanged for the present.

After considering the representations about this proposal, Ministers have decided that it should not be proceeded with for the present. The use of the "standard" method will, however, form part of a future review on the use of retail schemes by large businesses.

**Use of retail schemes will be withdrawn from non-retailers.**

Persons affected should consider whether they can use the scheme of cash accounting to be introduced on 1 October 1987.

**Use of retail schemes in respect of non-retail supplies will be withdrawn.**

Those persons making both retail and non-retail supplies will be able to use retail schemes for their retail supplies only.

**Clearer guidance on the rules for permitted mixtures of retail schemes will be given in Notice 727, VAT Retail Schemes.**

This is in line with the proposals in the consultation paper.



FROM: A C S ALLAN  
DATE: 9 MARCH 1987

MR WILMOTT - C&E

cc PS/Minister of State  
Sir P Middleton  
Mr Cassell  
Mr Scholar  
Miss Sinclair  
Mr Romanski

### EXCISE DUTY RATES

I understand that you are reworking the figures for the real level of excise duties since 1979.

2. You earlier supplied (via Mr Scholar) figures deflated by the difference between the June 1983 and December 1986 RPI. The Chancellor would be grateful if you could update the figures to include the latest estimate of the February RPI. And if you could do similar figures for the previous Parliament (ie May 1979 to June 1983).

3. He feels the changes should take on board the effects of the VAT increase in June 1979. He assumes that the inclusion of VAT would not make any difference a year in which VAT was unchanged. If this is not true the effects should be included in the tables.

4. He would be grateful if the results could be circulated to all Ministers and advisers.

ACSA

A C S ALLAN

BUDGET CONFIDENTIAL



FROM: S P Judge

DATE: 9 March 1987

BIF  
113

PS/ECONOMIC SECRETARY

cc PS/Chancellor

Mr Scholar

Miss Sinclair

Mr Ilett

Mr Cropper

PS/Customs & Excise

Mr Jefferson Smith - C&E

VAT TAX AVOIDANCE: STARTER No 6: PARTLY EXEMPT TRADERS

Both the Minister of State and the Chancellor (Cathy Ryding's note of 9 March, attached) have asked that the Economic Secretary consider the proposed treatment of services in relation to capital issues. This is covered in paragraphs 9-12 of Mr Jefferson Smith's submission of 6 March, of which I attach a copy.

The present situation is as follows. If a firm - eg ICI - decides to raise money by issuing shares or Eurobonds, this issue is an exempt supply. ICI will buy in services - eg underwriting, management (share registers etc), legal and accountancy advice. They will pay input VAT at 15 per cent on all these services. In theory, as these inputs are related to an exempt output, the input tax should not be recoverable. But in practice it often is.

The Chancellor's announcement before Christmas explained how this loophole would be closed. To mitigate the impact on those issuing capital, he proposed to exempt underwriting and management services. This would reduce the amount of input VAT ICI would have to pay in the first place, and hence mitigate the impact of the modifications to the rules. As the suppliers of such services (banks, etc) are usually partly exempt anyway, this would not cause any new problems for them (or significantly affect their input tax position).

However, this still leaves capital issuers worse off. One way to avoid this would be to extend the exemption to legal and



**BUDGET CONFIDENTIAL**

accountancy services. But this would mean that lawyers and accountants became for the first time partly exempt traders - with some of their services (house conveyancing) being taxable and others (advice to issuers of capital) being exempt. This would be a most unwelcome complication.

Many objectors - especially the British Bankers Association - have instead proposed an alteration to the new rules to allow tax related to capital issues to be "in principle deductible". Customs do not think this can be done without putting at risk a substantial amount of the revenue from the main reforms (£300 million).

The Minister of State is therefore minded to concur with Customs, but would be grateful for the Economic Secretary's views on the likely scale of "offshore drift" - capital issuers avoiding input VAT on legal and accountancy advice by procuring it through agencies based in, eg, Luxembourg or the Channel Islands. I had a brief word with Mr Ilett about this this morning; his initial reaction was that any drift was likely to be slow. And, as Mr Jefferson Smith mentions at the end of his submission, this can be kept under review in the future, and modifications introduced if necessary.

The Minister of State would be most grateful for the Economic Secretary's comments.

*SPJ*

**S P JUDGE**  
Private Secretary



*Revised  
PH*

*Thanks.  
Apt: psr draft  
a show passag  
for the 27  
(Giles) 27 in a new 537A  
to make a clean we  
have looked off  
the brewers &  
New (17) houses*

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

FROM: P JEFFERSON SMITH  
9 March 1987

PS/CHANCELLOR

cc: PS/Minister of State  
Mr Scholar  
Miss Sinclair

**VAT TAX AVOIDANCES : STARTER NO 6**

1. The Chancellor asked the state of play on brewers and their tied houses (paragraph 3 of your note of 9 March to PS/Minister of State).
2. We have reached agreement with the Brewers' Society, confirmed by an exchange of letters last week. Brewers will recover 85% of their input tax incurred on their tied estate and all the input tax on fittings and dispensing equipment. With a proviso respecting the EC infraction proceedings, the agreement will stand for three years. If any brewer does not wish to abide by the agreement, we would be free to propose an alternative basis, but in the case of a smaller brewer we would take into account figures which might point to a more favourable recovery fraction than 85%.
3. The effect will be to confine the impact of the VAT changes on the brewers to less than £10 million. We expect no direct impact on beer prices. The brewers are generally well satisfied: indeed the danger is that they may express their satisfaction in such a way as to embarrass us in dealings with other bodies which it would be less easy to treat as special cases.

*PH*

P JEFFERSON SMITH

Internal distribution: CPS  
Mr Knox  
Mr E Taylor  
Mr Michie

136/3/87

FROM: COLIN MOWL  
DATE: 10 March 1987

PPS/CHANCELLOR

*An important cancelled  
by Mr Mowl.  
Reference to products unit.*

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
PS/Minister of State  
Sir P Middleton  
Sir T Burns  
Mr Cassell  
Mr Scholar  
Mr Culpin  
Miss O'Mara  
Mr Pickering  
Miss Sinclair  
Mr Romanski  
Mr Cropper  
Mr Tyrie

PS/C&E  
Mr Knox - C&E  
Mr Jefferson-Smith - C&E  
Mr Wilmott - C&E

MOWL  
To  
ACSA  
10/3

#### EXCISE DUTIES

Your minute of 9 March asked me to provide figures for the proportion of indirect taxes in total revenues, indicating the effects of the Budget. The table below sets out the relevant figures.

	1986-87	1987-88	
		Forecast	Revalorisation only
Total taxes and NICs (£b)	146.1	156.4	159.1
Indirect taxes (£b)	77.2	82.6	83.0
Share of indirect taxes (%)	52.8	52.8	52.1

2. At the Minister of State's meeting I said, on the basis of the forecast as it then stood, that the share of indirect taxes was forecast to fall slightly in 1987-88 compared with

BUDGET SECRET

1986-87. On the latest figures shown above, the share of indirect taxes is expected to be the same in 1987-88 as in 1986-87. The Chancellor is quite correct however in stating that had it not been for the Budget the share of indirect taxes would have fallen further. The final column of the table shows the projected share on the assumptions that both direct and indirect taxes are revalorised in 1987-88 and that there are no other tax changes. On this basis the share of indirect taxes is forecast to fall in 1987-88. The explanation is that the proportionate reduction in direct taxes in the Budget is bigger than the proportionate reduction in indirect taxes.

*Colin Mowl*

COLIN MOWL



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

FROM: P JEFFERSON SMITH  
10 March 1987

MINISTER OF STATE

cc: PS/Chancellor  
Mr Scholar  
Miss Sinclair  
Mr Cropper

*Ch*  
*OK, though top of*  
*tail should be a bit less*  
*grudgingly*

*X is a quick*  
*response*

**BUDGET 1987 : ON-COURSE BETTING DUTY**

Your private secretary's note of 4 February 1987 recorded your agreement to the sending by you of a very strong letter to the racing authorities after the Chancellor's announcement of abolition of the on-course duty. The letter would emphasise the need for firm policing, coupled with very firm penalties against offenders. You were prepared to hint that the duty would be re-imposed if abuse got out of hand. A draft is attached. Depending on the addressee, it will need to be edited, but it is submitted now to see whether it has your general approval. If so, we would then prepare "tailored" drafts, for you to send immediately after the Budget Speech.

Although the letter would be from you to each of the bodies, and would not be published by us, it is reasonably certainly to leak to the press. One of the recipients, for example, has a column in Sporting Life. But we see no harm in this.

My submission of 2 February also informed you that it was our intention to abolish the duty by making it a 'nil' rate, thus enabling us to continue to exercise control over on-course

---

Internal circulation: CPS  
Mr Knox  
Mr McGuigan  
Mr Heron  
Mr Bone

BUDGET CONFIDENTIAL

X | betting. Parliamentary Counsel has advised that it would be preferable to delete the present taxing provision on on-course bets, and to introduce a new provision for continuation of control. This does the same thing more elegantly.

Ph L

P JEFFERSON SMITH

BUDGET CONFIDENTIAL

ON COURSE BETTING : DRAFT LETTER TO RACING AUTHORITIES

You now know that this year the Chancellor was able to accept the case for abolition of the on-course betting duty. I sincerely hope that this will produce the benefits to racing that were put to me [when I met you and other representatives of.....]

One point which gave us some concern when we were considering the case for abolition, and still does, is the possibility of substantially increased evasion of the off-course duty through the misrepresentation of such bets as on-course. The incentive to do this is, of course, now much greater. Whilst most on-course bookmakers will continue to observe the rules, a minority may seek to increase their turnover by exploiting the duty differential between on and off-course betting. Quite apart from the loss to the revenue, which could be substantial and could increase as time passes, I do not think that this would be good for the reputation of racing.

Customs will continue to exercise control at race courses and dog tracks but the need for efficient use of their resources is such that checks must be few and cannot be increased. Co-operation between Customs and racing authorities is now good and I am sure that will continue. However, in the new situation I am personally asking you to re-examine and, where possible, intensify your own security arrangements. The use of cellular telephones on race courses is one area which may need examination. I realise that proving offences is particularly difficult in relation to illegal betting, but I think that you should make it plain to all who are professionally involved in the sport the serious view which the racing authorities will take of offences, and the penalties which they are prepared to impose. The loss of pitches, for example, is a penalty that should deter most of those who might be tempted to offend.

BUDGET CONFIDENTIAL

I shall be asking Customs to contact [you] over the next few months to discuss what is possible. I shall also ask them to report back to me and to keep me informed of any evidence that abolition is becoming subject to abuse.

I am sure that the industry will make the most of this opportunity to prosper and I wish it well. I do emphasise, however, that the opportunity carries with it the need to ensure that it is not abused by the few. The last thing either of us would want is for the tax differential to be so exploited that the loss to the revenue from the off-course duty should become unacceptable.

PETER BROOKE



C.

PS/mST has had a go at a redraft of the section on Brewers - the mST himself is not available until 5pmish. I've highlighted the bits I think we should have.  
Content?

OK m

→ CE 1013

Cathy

**PRAMERS**

you\*

I have had a go at a redraft.  
Could stop at (\*)? Two possible endings - I prefer the second. Customs have not cleared it but I don't imagine any probs. The word 'special' is notable by its absence.

Customs will continue to allow alternative methods of apportioning input tax to be used, provided they are practical, accurate and fair. (\*) In particular, an agreement has [recently] been reached with representatives of the brewing industry which takes account of [the large amount of input tax they incur in relation to tied houses.] [the unusual ~~the~~ circumstances of their tied property estates].

C/ Reused C&E press notices below.

Changes have been marked.

You might like to look at the highlighted sections at X to make sure you are happy. Also at Y, you suggested "Press" but customs prefer "News" because that's what the headed paper that this is printed on says. <sup>EE</sup> P/B

BUDGET

SECRET

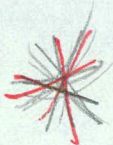


Cathy

I attach the revised C+E press release;  
all markings are mine - changes are  
sidelined.

I think this meets CX's + MST's  
comments but will peruse again this  
afternoon -

D  
10/7



Only the problem.  
X seems to imply that we are  
not to do special deals, etc  
in line with the  
business, with an  
ask's us. This  
for which. I will be  
if MST can be  
grateful  
MST is  
looking at  
this

CLASSIFICATION: BUDGET SECRET

SECURE FAX NO: COES/3

OUTGOING SECURE FAX

FROM P. G. WILMOTT'S, COE

Chairman's Office, HM Customs and Excise, Room 454  
King's Beam House, 39-41 Mark Lane, LONDON EC3R 7HE)  
(Fax No. 2913 5048 Operation 2913 5013,  
2913, 5024

TO Simon Judge..... Department Treasury (MST)

Date 10/3/87..... Time 11:55 am.....

No of pages following .....

Copy will also be sent by post Yes   
No

RECEIPT OF THIS TRANSMISSION  
MUST BE SENT

This material must be handled in accordance with the security instructions applicable to the classification.

CLASSIFICATION: .....

No 16/87

17 MARCH 1987

**VAT: SMALL BUSINESS REVIEW**

In his Budget today, the Chancellor of the Exchequer announced a VAT package designed to assist small businesses. This <sup>+</sup> News Release sets out full details of the package and changes to the original proposals contained in the consultation paper "VAT: Small Business Review" (issued October 1986).

**Cash accounting**

(+ the banner says  
"Customs + Excise News Release")

The Chancellor of the Exchequer announced an optional scheme, open to all businesses with turnovers below £250,000, whereby VAT would be accounted for on the basis of cash paid and received.

This scheme improves considerably on that proposed in the consultation paper in which the suggested turnover level was £100,000. Provided the necessary derogation under article 27 of the EC 6th VAT Directive can be obtained, it will be introduced on 1 October 1987.

The Finance Bill will contain an enabling clause and draft regulations will be published in May to coincide with the Standing Committee's consideration of the Bill.

Businesses wanting to use the scheme will be required to make an application to their local VAT office and, once approved, to remain in the scheme for 2 years. A leaflet explaining how the scheme will work will be available from local VAT offices in May. Further information explaining how to apply will be sent out with VAT returns in the summer.

### Annual accounting

The Chancellor of the Exchequer announced an optional scheme of annual accounting. This scheme would be available to all businesses which regularly pay tax, have been registered for at least one year and have turnovers below £250,000. Businesses choosing to use the scheme would make only one VAT return a year instead of the present four. They would make 9 equal payments on account, by direct debit, and a tenth balancing payment with their annual return.

This scheme, too, improves considerably on that proposed in the consultation paper in which the suggested turnover limit was £100,000. It will be introduced in the summer of 1988 when the necessary computer reprogramming has been completed.

The Finance Bill will contain the necessary enabling clause, and draft regulations will be published in the spring of 1988.

A leaflet explaining how the scheme will work will be available from local VAT offices in June. Invitations to use annual accounting will be included in this autumn's VAT notes.

[ Deleted paragraph ]

### Records and accounts

As announced in HM Customs and Excise News Release number 4.87 "VAT: Preservation of Records", KMG Thomson McLintock have been appointed to conduct a review of the maintenance and preservation of VAT records and are due to report by the end of May.

The proposal to engage an independent consultant to conduct such a review was announced in Chapter 3 of the consultation paper.

### Registration and deregistration requirements

The Chancellor of the Exchequer announced that the time for notification to be registered for VAT was to be extended to 30 days; this is one of several changes which are:

time to notify liability to register extended to 30 days;

eligibility to deregister to be based on future turnover only;

turnover for deregistration to be tax inclusive;

notification of cessation of trade increased to 30 days;

? SPS } once deregistered, businesses will not have to re-register [on the basis] of turnover prior to deregistration. as a result

These changes will have effect from Royal Assent to the 1987 Finance Act.

The only modification made to the original proposals was, for technical reasons, the substitution of "30 days" for "1 month". In practice this will not be detrimental, as a fixed period of 30 days gives certainty, whereas a calendar month varies from 28 days to 31 days.

#### Discretionary registration

The discretionary registration of businesses with turnovers below the registration threshold will continue unchanged. (It had been suggested in the consultation paper that businesses below the registration threshold should not be permitted to register, or remain registered for VAT.)

#### Retail schemes

The Chancellor of the Exchequer announced changes to the special schemes for retailers. These are:

A new scheme, to be called Scheme B1, will be introduced as an alternative to Scheme B.

This new scheme will not have a "50% rule", and no turnover restrictions will apply, but it will involve an annual stock adjustment.



Scheme B itself will remain unchanged.

Another adaptation to Scheme B, to be called Scheme B2, will be introduced to replace the existing "Adaptation 1".

This new scheme will no longer have a fixed mark-up of 14% applying to all zero-rated goods received for resale; instead various increased but fixed mark-ups will be applied based on types of zero-rated goods. An annual turnover restriction of £500,000 per annum will apply, in line with the proposal in the consultation paper.

The annual turnover limit for Scheme C will be increased to £90,000, while some of the fixed mark-ups applied to the different trade classifications will be revised.

As a result of representations made, some of the revised fixed mark-ups proposed in the consultation paper will be reduced.

The annual turnover limit for Scheme D will be increased to £500,000.

This is in line with the proposal in the consultation paper.

The current "Adaptation 2" will be replaced by an adaptation to Scheme E, to be called Scheme E1.

As proposed in the consultation paper, this new scheme will operate in the same way as the old adaptation except that the calculation of expected selling prices of only standard-rated goods received for resale will be required.

The lower annual turnover limit for Scheme G will be abolished, while the 1/8th uplift, having been reviewed, will remain unchanged.

The "How to work Scheme J" pamphlet will be amended to include the available scheme J adaptations.

This is in line with the proposal in the consultation paper.

The "standard" method of reckoning gross takings will remain unchanged for the present.

After considering the representations about this proposal, Ministers have decided that it should not be proceeded with for the present. The use of the "standard" method will, however, form part of a future review on the use of retail schemes by large businesses.

Use of retail schemes will be withdrawn from non-retailers.

Persons affected should consider whether they can use the scheme of cash accounting to be introduced on 1 October 1987.

Use of retail schemes in respect of non-retail supplies will be withdrawn.

Those persons making both retail and non-retail supplies will be able to use retail schemes for their retail supplies only.

Clearer guidance on the rules for permitted mixtures of retail schemes will be given in Notice 727, VAT Retail Schemes.

This is in line with the proposals in the consultation paper.

*(I was right!)*  
Regulation 3 of the Retailers Regulations, which gives the Commissioners powers to refuse the use of retail schemes, will be amended to improve clarity.

This is in line with the proposal in the consultation paper.

It is planned that all the changes concerning retail schemes will have effect as from 1 October 1987. For "non-retailers" currently using retail schemes, a period of grace will be allowed to enable them to make the necessary adjustments to their accounting systems. Further information on the changes will be available from local VAT offices in May, and new retail scheme notices will be published before September.

### Revenue effect of the package

It is estimated that the total cost of these proposals will be £115 million in 1987-88 and £60 million in 1988-89.

### BACKGROUND NOTES

On 24 October 1986, the Minister of State at the Treasury, the Hon Peter Brooke MP, announced the publication by HM Customs and Excise of a consultation paper "VAT: Small Business Review", which contained a package of value added tax proposals designed to help small businesses. At the same time a question and answer leaflet was sent to a representative sample of 5,000 small businesses.

In total 192 responses were received to the consultation paper and 1,256 responses to the leaflet. The overwhelming majority of respondents welcomed both the small business review itself and the opportunity to participate. While generally supportive of the majority of the proposals the responses also made suggestions for improvement and change.

[ Customs and Excise are grateful . . . . ]

?  
S.S. 10/3  
ISSUED BY: THE PRESS AND INFORMATION OFFICE, HM CUSTOMS AND EXCISE, KING'S BEAM HOUSE, MARK LANE, LONDON EC3R 7HE  
TELEPHONE: 01-382 5468/5469/5470/5471

No 17/87

17 MARCH 1987

~

VAT: RESTRICTION OF DEDUCTIBLE INPUT TAX AND RELATED MATTERS

In his Budget Statement, the Chancellor of the Exchequer announced a package of measures designed to prevent distortion to trade and to combat VAT avoidance. Most of these measures follow from the consultation document issued by Customs and Excise on 7 August 1986, entitled "VAT: Input Tax: Origin and Scope of the Right to Deduct". The Chancellor announced in Parliament on 19 December the changes he intended to introduce. The principal measures are:

(a) Deductible Input Tax

From 1 April 1987 a VAT registered business will only be able to recover as input tax that VAT attributable to:

- business taxable supplies;
- business supplies which are outside the scope of UK VAT because they take place outside the UK but which would have been either standard or zero-rated supplies if they had been made in the UK;
- business supplies of warehoused goods which are disregarded under section 35 of the VAT Act 1983.

VAT input tax on overheads, including research and development, is deductible in full provided such expenses are used to support the taxable supplies of the business: only if such expenses were used to support non-taxable activities would a restriction on recovery on input tax apply.

NB  
X

One of the main effects of the changes will be to prevent the recovery of VAT input tax in relation to future exempt supplies: in the past some businesses have taken advantage of weaknesses in the current partial exemption rules and by carefully timing when exempt supplies are made have recovered input tax to which they are not, in principle, entitled. Many other businesses have not sought to take advantage of these weaknesses and as a result have been placed at a competitive disadvantage.

Section 15 of the VAT Act 1983 (as amended) permits Customs and Excise to make regulations to secure a fair and reasonable attribution of input tax to taxable supplies and to adjust input tax which has been wrongly attributed.

A revised edition of Notice 706 'Partial Exemption' gives full details of the new partial exemption 'de minimis' rules and of a new standard method for apportioning input tax.

*Commit 15*  
 NEW!  
 X  
 Customs will allow alternatives to the "standard method" of apportioning input tax provided they are practical, accurate and fair (agreement has, for example, been reached with representatives of the brewing ~~and oil~~ industry~~ies~~ on a special method for calculating input tax in relation to tied properties).

[ C+E are deleting unfortunate reference to oil industry ! ]

- (b) Registration of traders making overseas supplies and repeal of Zero Rate Group 15 Item 2 of the VAT Act 1983; registration of traders making supplies of warehoused goods.

+ } From Royal Assent Item 2 of, and Note 1 to, Zero Rate Group 15 (supplies from the UK by a person operating both inside and outside the UK to his place of business outside the UK) will be repealed. Many businesses which were registered for VAT because they were making supplies which were zero-rated under Item 2 will remain eligible for registration under the new arrangements set out below.

Schedule 1 to the VAT Act 1983 will be amended from Royal Assent to enable businesses which make no taxable supplies in the UK but make overseas business supplies which are outside the scope of UK VAT (but which would have been either standard or zero-rated supplies if they had been made in

+ 1 hope the Chancellor understands this!

the UK), and businesses which make business supplies of warehoused goods which are disregarded under section 35 of the Act, to apply for VAT registration so as to recover the input tax attributable to such supplies.

Businesses affected by these changes must review their eligibility to remain VAT registered. Should they be eligible and wish their VAT registration to continue, they should make written application to their local VAT office: businesses no longer eligible must apply for deregistration.

(c) Exemption of services related to capital issues

\* From 1 April 1987, the making of arrangements for and the underwriting of capital issues will be exempt from VAT.

(d) Acquisition of a business as a going concern by a partly exempt VAT group

From 1 April 1987 a new provision will come into effect under which partly exempt companies VAT grouped under section 29 of the VAT Act 1983 may, in certain circumstances, be required to treat the acquisition of business assets on the transfer of a business or part of a business as a going concern, as both a supply by and to the representative member of the VAT group. The representative member will be required to account for VAT on a supply of any chargeable assets transferred and can recover input tax in accordance with its normal partial exemption method in the tax period in which the assets are acquired.

(e) Valuation of exempt supplies

The provisions of the VAT Act 1983 governing the valuation of certain transactions not made in open market conditions will be extended to cover exempt supplies. This change is necessary to prevent the distortion of certain partial exemption calculations. If there is no connection between the parties the value is the consideration paid, otherwise open market value applies.

\* EST holding a meeting on "offshore draft" implications;  
possible extension of exemption (to legal + accounting advice)  
or new rules ~~etc~~ will not be in Budget.

**REVENUE EFFECT**

It is estimated that the total package will prevent a revenue loss of £300 million in 1987-88.

**REGULATIONS**

A full copy of the regulations giving effect to certain of the changes outlined in (a) above has today been sent to all parties who have previously indicated a desire to receive these. Further copies can be obtained from:

HM Customs and Excise  
VAT Administration Directorate (VAD 6)  
Room 206  
Knollys House  
11 Byward Street  
LONDON  
EC3R 5AY

The regulations will be laid in the House of Commons at the end of the Budget debate and are available in the interim in the Library of the House.

**PUBLIC NOTICES**

The revised partial exemption Notice 706 and copies of Budget Notices (BN 3/87 and 4/87) covering the following points are available from local VAT offices:

- VAT: restriction of input tax; registration of overseas traders and repeal of zero rate Group 15 Item 2; registration of traders making supplies of warehoused goods; exemption of certain services related to capital issues.
- VAT: acquisition of a business as a going concern by a partly exempt VAT group.

x

run on?

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HOUSE, MARK LANE, LONDON EC3R 7HE

**TELEPHONE:** 01-382 5468/5469/5470/5471





H.M. CUSTOMS AND EXCISE  
KING'S BEAM HOUSE, MARK LANE  
LONDON EC3R 7HE

Please Dial my Extension Direct:  
Use Code (01)-382 followed by  
Extension Number 5.023...

From: P G WILMOTT

Date: 11 MARCH 1987

CHANCELLOR

cc Chief Secretary  
Financial Secretary  
Minister of State  
Economic Secretary  
Sir P Middleton  
Mr Cassell  
Mr Scholar  
Miss Sinclair  
Miss O'Mara  
Mr Culpin  
Mr Romanski  
Mr Cropper  
Mr Ross Goobey  
Mr Tyrie

Ch  
Good stuff here.  
AA

EXCISE DUTY RATES

1. You asked for reworked figures on the real value of the excise duty rates since 1979 (Mr Allan's minute of 9 March).
2. I attach tables showing the changes in the real values of the duty rates (both with and without consequential VAT) since 1979, covering the first and second Conservative Governments separately as well as the period as a whole. For comparison, I also attach tables showing what happened between 1974 and 1979.
3. Table 1 shows how the real values of the duties have changed since 1979, based on the increase in the RPI between the last full

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Internal circulation: CPS, Mr Knox, Mr Jefferson Smith,  
Mr Bone, Mrs Hamill

WILMOTT  
TO  
CH/EX  
11/3

month of the Labour Government (April 1979) and the latest available figure (January 1987). (We have stuck with the January 1987 RPI figure because that is the latest firm figure publicly available, and will remain so, we understand, even on Budget Day; but, in any case, updating the comparison to a later date would alter the figures only very slightly, though in a downward direction.) Overall, including the minor duties not separately shown, the real value of the specific duties has risen by 32%. Of the main duties, all except those on spirits and wine have risen in real terms. The real value of wine duty has fallen because of the reduction in 1984 to comply with the EC beer/wine ruling.

4. Table 1A covers the same period as Table 1 but allows for the changes in VAT. In June 1979, the rate of VAT rose from 8% to 15% on all the main dutiable goods except petrol, and from 12.5% on petrol. VAT is not charged on VED. Allowing for these changes, the duties rose by 38% in real terms.

5. Tables 2 and 3 give the separate figures for the two sub-periods, 1979-1983 and 1983-1987. (Table 2A includes the effect of the 1979 VAT change; as there has been no VAT change affecting the excise duties since 1983, there is no Table 3A.) These show that the bulk of the real increase in duties took place between 1979 and 1983. Taking all the duties together, the figures are:

Real increase in duties:

	Without VAT	With VAT
1979-1983	27%	32%
1983-1987	3%	3%
<hr/>		
1979-1987	32%	38%

6. Looking at the record of the Labour administration is difficult because of the many changes in the tax structure over this period. Our best estimates are shown in Tables 4 and 4A and suggest that the real value of ~~the~~ duties - with or without VAT - fell by around 10% between 1974 and 1979. (The increased VAT on road fuels broadly offset the reduction on the other goods.)



P G WILMOTT

PapedPse



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

FROM: P JEFFERSON SMITH  
12 March 1987

MINISTER OF STATE

*1 wtd  
Knox  
Jaloff  
'Stam'*  
- Phoned through.

cc PS/Chancellor  
PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Scholar  
Miss Sinclair  
Mr Cropper

**RESTRUCTURING OF THE WINE AND MADE-WINE DUTIES**

1. At the overview meeting on 2 March it was decided that there should be no restructuring of the wine and made-wine duties this year.

2. In his minute of 25 February Mr Knox suggested that the announcement of such a decision should be low key and might take the form of an arranged PQ. There would be advantage in answering such a PQ as soon as practicable after the Budget; the drinks trade will inevitably want to know whether "no change" means "no restructuring" or whether there may be measures to come in the Finance Bill. We therefore suggest that the question should be put down on Monday 16 March and answered as soon as the Chancellor sits down on 17 March.

3. I attach a draft Question and Answer.

JEFFERSON SMITH  
→ MST  
12/3

*PJS*

P JEFFERSON SMITH

Internal distribution: CPS  
Mr Knox  
Mr Whitmore  
Mr Wilmott  
Mr Tullberg

218/3/87

BUDGET SECRET

DRAFT ARRANGED PQ

To ask Mr Chancellor of the Exchequer, what conclusion has been reached about the structure of the wine and made-wine duties following the consultation exercise carried out by HM Customs and Excise. .

The extensive consultation established that all the options for restructuring the wine and made-wine duties have ~~serious~~ drawbacks. In view of this, and with the drinks trade benefiting from a second successive duty standstill, my rt. hon. Friend has decided that it would not be appropriate to alter the existing structure and relativities this year. S



FROM: P D P BARNES

DATE: 12 March 1987

NOTE OF A MEETING HELD IN ROOM 51/2 TREASURY CHAMBERS AT 4.30 PM  
ON 11 MARCH

Those present: Economic Secretary  
Mr Cassell  
Miss Sinclair  
Mr Neilson  
Mr Ross Goobey  
Mr Jefferson-Smith - C&E  
Ms Barrett - C&E

*Spoken*  
*u* *2*

**VAT TAX AVOIDANCE: STARTER No.6**

Mr Jefferson-Smith explained that the provisions on partial VAT exemption were being changed to check the extent to which businesses were retaining the input tax that should be attributed to exempt supplies. Existing rules apportioned input tax by reference to outputs. This created the opportunity for firms artificially to inflate their taxable outputs and so recover more input tax than had been intended when the legislation had been enacted. The proposed change mostly affected conglomerates with a financial sector that could be grouped with a non-financial sector. The change was estimated to yield £300 million in the first year rising to £400 million in the second year.

2. Mr Jefferson-Smith explained that the change would affect the cost of securities issues since it would no longer be possible to recover the tax on the services of accountants and lawyers connected with an issue. The increase in costs would be greater as a percentage of a small issue and also greater for companies seeking a UK listing for the first time. For a £100 million issue the Bank had estimated that total cost might rise by about £50,000 (2-3% of total costs). For issues of around £500 million the bank thought that additional costs, which might be as high as £200,000, might result in the loss of some business from the UK.

BUDGET CONFIDENTIAL

3. Mr Jefferson-Smith said that the response to the Chancellor's announcement before Christmas of this intended change had been remarkably muted. He therefore thought, and others concurred, that the impact on the amount of business done in the UK was likely to be limited. Presentationally, the exemption of underwriting and management services from VAT would lessen the extent of any hostile reactions.

4. Summing up, the Economic Secretary said that he did not think that any special arrangements on VAT partial exemption should be made for capital issues at this stage.

RB

P D P BARNES  
Private Secretary

cc: Those present  
PS/Chancellor  
PS/Minister of State  
Mrs Lomax  
Mr Scholar  
Mr Cropper

BUDGET SECRET

RP



FROM: S P Judge

DATE: 13 March 1987

PARLIAMENTARY CLERK

cc PS/Chancellor  
PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
PS/Customs & Excise

JUDGE  
→ PARLY  
CLERK  
13/3

RESTRUCTURING OF WINE AND MADE-WINE DUTIES

I attach an arranged PQ and Answer, which the Chancellor and the Minister of State have approved.

The timing is most important: I would be grateful if the Question could be put down on Monday, and answered when the Chancellor has sat down on Tuesday.

S.P.J.

S P JUDGE  
Private Secretary



**BUDGET SECRET**

**DRAFT ARRANGED PQ**

To ask Mr Chancellor of the Exchequer, what conclusion has been reached about the structure of the wine and made-wine duties following the consultation exercise carried out by HM Customs and Excise.

**MINISTER OF STATE**

The extensive consultation established that all the options for restructuring the wine and made-wine duties have drawbacks. In view of this, and with the drinks trade benefiting from a second successive duty standstill, my Rt Hon Friend has decided that it would not be appropriate to alter the existing structure and relativities this year.

DRAFT  
ARRANGED  
PQ

RESTRUCTURING OF  
THE WINE AND MADE-WINE  
DUTIES

BUDGET SECRET

Copy 2 of 10  
P.D.P.



FROM: P D P BARNES

DATE: 13 MARCH 1987

PS/MINISTER OF STATE

cc PS/Chancellor  
PS/Chief Secretary  
PS/Financial Secretary  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr Jefferson-Smith C&E

*1 agm*

RESTRUCTURING OF THE WINE AND MADE-WINE DUTIES

The Economic Secretary has seen Mr Jefferson-Smith's submission to the Minister of State of 12 March.

2. The Economic Secretary thinks that as a matter of principle we ought not to have arranged PQs tabled before the Budget on Budget matters.

*P.D.P.*

P D P BARNES  
Private Secretary

RD



COPY NO. 10 OF 10.

FROM: CATHY RYDING  
DATE: 16 March 1987

PS/MINISTER OF STATE

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Scholar  
Miss Sinclair  
Mr Cropper  
Mr Jefferson Smith - C&E

**RESTRUCTURING OF THE WINE AND MADE-WINE DUTIES**

The Chancellor has seen PS/Economic Secretary's minute to you of 13 March.

2. The Chancellor agrees with the Economic Secretary that as a matter of principle we ought not to have arranged PQs tabled before the Budget on Budget matters.

CR

CATHY RYDING

**VAT: SMALL BUSINESS REVIEW**

In his Budget today, the Chancellor of the Exchequer announced a VAT package designed to assist small businesses. This <sup>Press</sup> News Release sets out full details of the package and changes to the original proposals contained in the consultation paper "VAT: Small Business Review" (issued October 1986).

**Cash accounting**

The Chancellor of the Exchequer announced an optional scheme, open to all businesses with turnovers below £250,000, whereby VAT would be accounted for on the basis of cash paid and received.

This scheme improves considerably on that proposed in the consultation paper in which the suggested turnover level was £100,000. Provided the necessary derogation under article 27 of the EC 6th VAT Directive can be obtained, it will be introduced on 1 October 1987.

The Finance Bill will contain an enabling clause and draft regulations will be <sup>published</sup> exposed in May to coincide with the Standing Committee's consideration of the Bill.

Businesses wanting to use the scheme will be required to make an application to their local VAT office and, once approved, to remain in the scheme for 2 years. A leaflet explaining how the scheme will work will be available from local VAT offices in May. Further information explaining how to apply will be sent out with VAT returns in the summer.

## Annual accounting

The Chancellor of the Exchequer announced an optional scheme of annual accounting. This scheme would be available to all businesses which regularly pay tax, have been registered for at least one year and have turnovers below £250,000. Businesses choosing to use the scheme would make only one VAT return a year instead of the present four, ~~and,~~ <sup>They</sup> would make 9 equal payments on account, by direct debit, and a tenth balancing payment with their annual return.

This scheme <sup>100,</sup> improves considerably on that <sup>proposed</sup> ~~proposal~~ in the consultation paper in which the suggested turnover limit was £100,000. It will be introduced in the Summer of 1988 when the necessary computer reprogramming has been completed.

The Finance Bill will contain the necessary enabling clause, and draft regulations will be ~~exposed~~ <sup>published</sup> in the Spring of 1988.

A leaflet explaining how the scheme will work will be available from local VAT offices in June. Invitations to use annual accounting will be included in this autumn's VAT notes.

## Default interest and penalty for serious misdeclaration

These measures, which would have completed the implementation of the Keith provisions enacted in the 1985 Finance Act, were to be introduced on 1 July 1988. In order that the schemes for cash accounting and annual accounting can be introduced at the earliest possible date the introduction of default interest and the penalty for serious misdeclaration will now have to be deferred until late 1989. (need to delete)

## Records and accounts

As announced in HM Customs and Excise News Release number 4.87 "VAT: Preservation of Records", KMG Thomson McLintock have been appointed to conduct a review of the maintenance and preservation of VAT records and are due to report by the end of May.

The proposal to engage an independent consultant to conduct such a review was announced in Chapter 3 of the consultation paper.

### Registration and deregistration requirements

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**time to notify liability to register extended to 30 days;**

**eligibility to deregister to be based on future turnover only;**

**turnover for deregistration to be tax inclusive;**

**notification of cessation of trade increased to 30 days;**

**deregistered businesses will not be liable to registration only because of turnover before deregistration, will not under ↓**

These changes will have effect from Royal Assent to the 1987 Finance Act.

The only modification made to the original proposals was, for technical reasons, the substitution of "30 days" for "1 month". In practice this will not be detrimental, as a fixed period of 30 days gives certainty, whereas a calendar month varies from 28 days to 31 days.

### Discretionary registration

The discretionary registration of businesses with turnovers below the registration threshold will continue unchanged. (It had been suggested in the consultation paper that businesses below the registration threshold should not be permitted to register, or remain registered for VAT.)

*is this  
what is  
intention?*

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**A new scheme, to be called Scheme B1, will be introduced as an alternative to Scheme B.**

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**The annual turnover limit for Scheme D will be increased to £500,000.**

This is in line with the proposal in the consultation paper.

**The current "Adaptation 2" will be replaced by an adaptation to Scheme E, to be called Scheme E1.**

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This is in line with the proposal in the consultation paper.

It is planned that all the changes concerning retail schemes will have effect as from 1 October 1987. For "non-retailers" currently using retail schemes, a period of grace will be allowed to enable them to make the necessary adjustments to their accounting systems. Further information on the changes will be available from local VAT offices in May, and new retail scheme notices will be published before September.

#### Revenue effect of the package

*[It is estimated that cash accounting will]*  
(Cash accounting will, it is estimated,) cost £100 million in 1987-88 and £10 million in 1988-89. Annual accounting will cost an estimated £25 million in 1988-89. Changes to the requirements for notifying liability to register are estimated to cost £15 million in 1987-88 and £25 million in 1988-89. Other provisions in the package are expected to have a negligible or nil cost effect.

#### **BACKGROUND NOTES**

On 24 October 1986, the Minister of State at the Treasury, the <sup>(Hon)</sup> Peter Brooke MP, announced the publication by HM Customs and Excise of a consultation paper "VAT: Small Business Review", which contained a package of value added tax proposals designed to help small businesses. At the same time a question and answer leaflet was sent to a representative sample of 5,000 small businesses.

In total 192 responses were received to the consultation paper and 1,256 responses to the leaflet. The overwhelming majority of respondents welcomed both the small business review itself and the opportunity to participate. While generally supportive of the majority of the proposals the responses also made suggestions for improvement and change.



**ISSUED BY:** THE PRESS AND INFORMATION OFFICE, HM CUSTOMS AND EXCISE, KING'S BEAM  
HOUSE, MARK LANE, LONDON EC3R 7HE

**TELEPHONE:** 01-382 5468/5469/5470/5471

**VAT: RESTRICTION OF DEDUCTIBLE INPUT TAX: REGISTRATION OF OVERSEAS TRADERS AND REPEAL OF ZERO RATE GROUP 15, ITEM 2; REGISTRATION OF TRADERS MAKING SUPPLIES OF WAREHOUSED GOODS; EXEMPTION OF CERTAIN SERVICES RELATED TO CAPITAL ISSUES; ACQUISITION OF A BUSINESS AS A GOING CONCERN BY A PARTLY EXEMPT VAT GROUP; VALUATION OF EXEMPT SUPPLIES.**

In his Budget Statement, the Chancellor of the Exchequer announced a package of measures designed to prevent distortion to trade and to combat VAT avoidance. Most of these measures follow from the consultation document issued by Customs and Excise on 7 August 1986, entitled "VAT: Input Tax: Origin and Scope of the Right to Deduct". The Chancellor announced in Parliament on 19 December the measures he intended to introduce. The principal changes are:

(a) Deductible Input Tax

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VAT input tax on overheads, including research and development, is deductible in full provided such expenses are used to support the taxable supplies of the business: only if such expenses were used to support non taxable activities would a restriction on recovery on input tax apply.

One of the main effects of the changes will be to prevent the recovery of VAT input tax in relation to future exempt supplies: in the past some businesses have taken advantage of weaknesses in the current partial exemption rules and by carefully timing when exempt supplies are made have recovered input tax to which they are not, in principle, entitled. Many other businesses have not sought to take advantage of these weaknesses and as a result have been placed at a competitive disadvantage.

Section 15 of the VAT Act 1983 (as amended) permits Customs and Excise to make regulations to secure a fair and reasonable attribution of input tax to taxable supplies and to adjust input tax which has been wrongly attributed.

A revised edition of Notice 706 'Partial Exemption' gives full details of the new partial exemption 'de minimis' rules and of a new standard method for apportioning input tax.

- Whole of Zero GP 15 Item 2  
of the 1983 VAT Act? Re Press  
Notice SW*
- (b) Registration of traders making overseas supplies and repeal of Zero Rate Group 15 Item 2 of the VAT Act 1983; registration of traders making supplies of warehoused goods.

From Royal Assent (subject to Parliamentary approval) Item 2 of, and Note 1 to, Zero Rate Group 15 will be repealed. Many businesses which were registered for VAT because they were making supplies which were zero-rated under Item 2 will remain eligible for registration under the new arrangements set out below.

Schedule 1 to the VAT Act 1983 will be amended from Royal Assent to enable businesses which make no taxable supplies in the UK but make overseas business supplies which are outside the scope of UK VAT (but which would have been either standard or zero-rated supplies if they had been made in the UK), and businesses which make business supplies of warehoused goods which are disregarded under section 35 of the Act, to apply for VAT registration so as to recover the input tax attributable to such supplies.

Businesses affected by these changes must review their eligibility to remain VAT registered. Should they be eligible and wish their VAT registration to continue, they should make written application to their local VAT office: businesses no longer eligible must apply for deregistration.

(c) Exemption of services related to capital issues

From 1 April 1987, the making of arrangements for and the underwriting of capital issues will be exempt from VAT.

(d) Acquisition of a business as a going concern by a partly exempt VAT group

From 1 April 1987 a new provision will come into effect under which partly exempt companies VAT grouped under section 29 of the VAT Act 1983 may, in certain circumstances, be required to treat the acquisition of business assets on the transfer of a business or part of a business as a going concern, as both a supply by and to the representative member of the VAT group. The representative member will be required to account for VAT on a supply of any chargeable assets transferred and can recover input tax in accordance with its normal partial exemption method in the tax period in which the assets are acquired.

(e) Valuation of exempt supplies

The provisions of the VAT Act 1983 governing the valuation of certain transactions not made in open market conditions will be extended to cover exempt supplies. This change is necessary to prevent the distortion of certain partial exemption calculations. If there is no connection between the parties the value is the consideration paid, otherwise open market value applies.

Revenue yield } <sup>effect</sup> CAPS NO LIND

It is estimated that the total package will prevent a revenue loss of £300 million in 1987-88.

Regulations CAPS. NO LIND

A full copy of the regulations giving effect to certain of the changes outlined in (a) above has today been sent to all parties who have previously indicated a desire to receive these. Further copies can be obtained from:

HM Customs and Excise  
VAT Administration Directorate (VAD 6)  
Room 206  
Knollys House  
11 Byward Street  
LONDON  
EC3R 5AY

The regulations will be laid in the House of Commons at the end of the Budget debate, and are available in the interim in the Library of the House.

PUBLIC                      CAP  
Budget Notices        NO LINE

The revised partial exemption Notice 706 and copies of Budget Notices (BN 3/87 and 4/87) covering the following points are available from local VAT offices:

- VAT: restriction of input tax; registration of overseas traders and repeal of zero rate Group 15 Item 2; registration of traders making supplies of warehoused goods; exemption of certain services related to capital issues.
- VAT: acquisition of a business as a going concern by a partly exempt VAT group.

**ISSUED BY:** THE PRESS AND INFORMATION OFFICE, HM CUSTOMS AND EXCISE, KING'S BEAM HOUSE, MARK LANE, LONDON EC3R 7HE

**TELEPHONE:** 01-382 5468/5469/5470/5471

**BUDGET 1987: VALUE ADDED TAX ON SERVICES IMPORTED BY UNREGISTERED BUSINESSES**

It was announced in the Budget today that the law will be changed to prevent the avoidance of VAT on imported services by exempt businesses.

At present, where for business purposes a registered trader buys in certain services from abroad, he has to treat them as if he had supplied them himself and charge himself tax. Businesses which are not registered because they deal wholly or mainly in exempt supplies do not, under existing law, have to count the cost of imported services as taxable turnover for the purposes of the quarterly or annual registration limits, and can thus avoid the need to register and account for VAT on the services in question. The proposed change in the law will close this loophole. As a result exempt businesses will have to register where the value of their taxable supplies and the cost of the relevant imported services together exceed the turnover limits. They will then pay the tax due on imported services and on any taxable supplies of their own in the same way as existing registered businesses already do.

**BACKGROUND NOTE**

Because of the loophole, exempt businesses have been able to import certain services VAT free and avoid the tax that they would have had to pay on identical services bought from UK registered traders. The imported services in question include advertising, data processing, <sup>and</sup> professional and consultancy services; there is evidence of avoidance particularly in relation to newspaper advertising ordered through agencies in the Channel Islands. The change (to section 7 of the VAT Act 1983) will put an end to unfair competition with UK businesses and will prevent a loss of revenue which, it is estimated, would have amounted to

some £5 million by 1988-89. Full details of the imported services affected are in Schedule 3 of the VAT Act 1983.

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**BUDGET 1987: VALUE ADDED TAX**

**REGISTRATION AND DEREGISTRATION: CHANGES IN THE LIMITS FOR REGISTRATION AND CANCELLATION OF REGISTRATION**

In his Budget Statement today, the Chancellor of the Exchequer announced changes in the limits for VAT registration and cancellation of registration. Details are as follows:

(a) **Registration**

- (i) The annual registration limit is being increased from £20,500 to £21,300 as from midnight tonight.
- (ii) The single quarterly registration limit is also being increased from £7,000 to £7,250 from the same time.

(b) **Cancellation of registration**

- (i) The limit will be increased from £19,500 pa to £20,300 pa (inclusive of VAT) from 1 June 1987 for persons considering cancellation of their registration on the basis of their expected future turnover.
- (ii) Persons will also be able to apply for cancellation of their registration after 1 June 1987 if they have been registered for two years and their turnover (inclusive of VAT) in each of those years has not exceeded £21,300, and provided they do not expect their turnover to go above £21,300 in the year then beginning.



(iii) It is estimated that a further 14,000 persons will be eligible to request cancellation of their registration as a consequence of these changes.

**PUBLIC NOTICE:** Details of the changes in the registration and cancellation limits are contained in Customs and Excise Notice BN 1/87 copies of which will be available at all local VAT offices.

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**BUDGET 1987: VALUE ADDED TAX**

**EXTENSION OF CERTAIN VAT RELIEFS FOR CHARITIES AND ELIGIBLE BODIES**

In his Budget today, the Chancellor of the Exchequer announced a package of VAT reliefs giving additional assistance to charities and certain eligible bodies. From 1 April 1987 VAT relief will be extended to:

- (i) the installation or adaptation of any bathroom, washroom or lavatory facilities for the handicapped in charity residential homes;
- (ii) drugs and chemicals directly used by a charity in medical research;
- (iii) certain vehicles for use by hospices for transporting the terminally ill; and
- (iv) specialised location and identification equipment for use by charitable rescue and first aid services.

The new reliefs are contained in the Value Added Tax (Charities) Order 1987 laid before Parliament today.

The relief for bathroom, washroom or lavatory facilities encompasses an existing extra-statutory concession for individual facilities in a charity residential home for the handicapped. The Order also gives statutory effect to an existing extra-statutory concession for the donation for export of goods to a charity established for the relief of distress.

## **BACKGROUND NOTES**

The effect of this package of measures is to extend the VAT reliefs at present available to charities and eligible bodies at a cost of about £5 million in 1987-88. The amendments are to Groups 14 and 16 of Schedule 5 of the Value Added Tax Act 1983.

In Group 14 zero-rating will for the first time be available for the installation or adaptation (including the supply of related goods) of all bathroom, washroom or lavatory facilities for the handicapped in residential homes run by charities. This will parallel the existing reliefs for the same facilities for the handicapped in private residences.

In Group 16 the new zero-rating for drugs and chemicals directly used in medical research extends last year's relief for medicinal products to charities engaged in medical research. The extension of relief to welfare vehicles (with 6-50 seats) for transporting the terminally ill is a further addition to the relief given last year for vehicles for the deaf, blind or mentally handicapped; the eligible bodies entitled to relief include health authorities and non-profit making hospitals as well as charities. Lastly, the zero-rating of specialised location and identification equipment for charitable rescue and first aid services covers some of the most expensive items in these charities' expenditure and should be of particular benefit in mountain rescue work.

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**TELEPHONE:** 01-382 5468/5469/5470/5471

**BUDGET 1987: VAT MARGIN SCHEME FOR TOUR OPERATORS**

It was announced in the Budget today that provision is to be made in the 1987 Finance Bill for a special VAT margin scheme for tour operators. UK based tour operators who buy in services for their customers will have to pay VAT on the margin between their buying and selling prices if the services are to be used anywhere in the European Community, including the United Kingdom. Additionally, tour operators will not be able to recover any VAT which may be charged by their suppliers for such services.

The services affected are those bought and sold for the benefit of travellers, including accommodation, transport and holiday services (but it is expected that transport will be zero rated). Services which tour operators supply from their own resources will not be covered by the scheme and will continue to be taxed according to normal VAT rules.

Consultations have been taking place between Customs and Excise and the Association of British Travel Agents. Detailed guidance about the operation of the scheme will be published later this year. The scheme is expected to start from 1 April 1988. It will yield an estimated £20 million in 1988-89.

**BACKGROUND NOTE**

The scheme is a requirement under Article 26 of the EC Sixth Directive. Forewarning of the Chancellor's intention to introduce it was given on Budget day last year. At present tour operators' services in respect of overseas package tours are not subject to UK VAT.

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HOUSE, MARK LANE, LONDON EC3R 7HE

**TELEPHONE:** 01-382 5468/5469/5470/5471

**BUDGET 1987: HYDROCARBON OIL**

**REDUCTION IN RATE OF EXCISE DUTY ON UNLEADED PETROL**

In his Budget today, the Chancellor of the Exchequer announced a reduction in the duty on unleaded petrol of 5p a gallon (1.1p a litre), including VAT. It previously bore excise duty at the same rate as leaded petrol.

The reduction applies to all unleaded petrol cleared at import or from bonded warehouse from 1800 hours today.

"Unleaded petrol" is defined as petrol containing not more than 0.02 grams of lead per litre (0.13 grams per litre from 1 April 1990).

**OTHER HYDROCARBON OILS**

The duty rates on leaded petrol, derv and other hydrocarbon oils remain unchanged.

**REVENUE EFFECT**

The revenue effect in 1987/88 of the reduction will be negligible.

Details of the changes are given in Customs and Excise Notice BN 2/87.

## BACKGROUND NOTE

Under European Community law (Directive 85/210/EEC), as a result of a United Kingdom initiative, unleaded petrol is to be generally available throughout the Community by 1 October 1989. Member States are to take appropriate steps to ensure its balanced distribution and to encourage its use. In his Budget Statement last year the Chancellor announced his intention of assisting the introduction of unleaded petrol by creating a duty differential in its favour to offset its higher production costs. Since then unleaded petrol has gone on sale at about 200 garages in the UK. The reduction announced this year should cover those higher costs and ensure that unleaded petrol sells for no more than 4\* leaded petrol at any garage.

**Duty rates** are as follows:

		<b>Pence</b>
<b>Light oils (except unleaded petrol and AVGAS)</b>	per litre :	19.38
	per gallon:	88.10
<b>Unleaded petrol</b>	per litre :	18.42
	per gallon:	83.74
<b>Derv</b>	per litre :	16.39
	per gallon:	74.51
<b>Gas oil</b>	per litre :	1.10
	per gallon:	5.00
<b>AVGAS and road fuel gas</b>	per litre :	9.69
	per gallon:	44.05

The rates per litre are the legal rates; approximate equivalents per gallon are quoted for information only.

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**TELEPHONE:** 01-382 5468/5469/5470/5471

**BUDGET 1987: BETTING AND GAMING DUTIES**

In his Budget Statement today, the Chancellor of the Exchequer announced changes to the betting and gaming duties.

**GENERAL BETTING DUTY:** The duty on on-course betting (now 4 per cent) will be **abolished** with effect from 29 March 1987. (The duty on off-course betting remains unchanged at 8 per cent.)

**GAMING MACHINE LICENCE DUTY:** Rates will be **increased** with effect from 1 June 1987.

(a) Amusement-with-prizes machines in public houses, arcades, etc

5p machines (now £120) will be £150 pa

10p machines (now £300) will be £375 pa

(b) Jackpot machines in clubs etc

5p machines (now £300) will be £375 pa

10p machines (now £750) will be £960 pa

**GAMING MACHINE LICENCE DUTY COLLECTION ARRANGEMENTS:** Changes in the arrangements for the collection and repayment of gaming machine licence duty will operate from 1 October 1987. All licences will be available from the first day of any month and quarter year special licences will be available for the first time. Refund terms on surrender of licences will be improved.



**REVENUE EFFECT:** The overall revenue effect will be neutral, the estimated £20 million annual loss from the abolition of on-course betting duty being recouped from the increase in gaming machine licence duty revenue.

**PUBLIC NOTICES:** Full particulars of the changes are given in Customs and Excise Notices BN 8/87 (On-course Betting) and BN 9/87 (Gaming Machine Licence Duty).

#### **BACKGROUND NOTES**

The on-course rate of general betting duty has been 4 per cent since 1972. Customs and Excise will continue to exercise controls at race tracks and will require certain records to be kept to protect the revenue from off-course betting. The racing and betting industries will be expected to take a part in ensuring that the duty-free status of on-course betting is not abused.

Gaming machine licence duty rates were last increased in the 1982 Budget, and the effect of this year's changes is broadly to restore them to their 1982 value.

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**TELEPHONE:** 01-382 5468/5469/5470/5471

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L Alex  
2C.

CHANCELLOR ✓

*Thank.  
I look forward  
to promises with*

FROM: F CASSELL

DATE: 19 JUNE 1987

cc: Sir P Middleton  
Mrs Lomax  
Mr Scholar

Mr Painter - IR

**SOVEREIGN DEBT PROVISIONING**

We touched on this briefly at your Markets Meeting last Tuesday, and you asked for a note on how the discussions with the Inland Revenue were going.

2. As I mentioned, I am running a little group with the Revenue and the Bank to make sure that we are all in touch with one another's thinking. The Bank have had several discussions with the banks on a possible matrix of country risk factors, and the banks themselves have now talked to the Revenue. These talks all seem to have gone quite well. They have, of course, been helped by the NatWest announcement - well ahead of the half-year results and making it plain that the additional provisioning was for commercial reasons (i.e. not tax-driven).

3. In the course of our own discussions, however, we have encountered some difficulty over the statistical base from which the different parties are working. Most of our figures in the past have been taken from consolidated accounts; but as the NatWest case shows the cost to the UK Exchequer will be strongly affected by whether the banks are holding part of the debts on the books of their US subsidiaries.

4. At my group's meeting last evening we thought it better to delay for a few days putting a report to you, in the hope that we could clarify some of the underlying statistics. We will let you have next week a note by the Revenue on their discussions with the banks and their estimate (necessarily broad at this stage) of the likely cost of the tax relief and its timing, together with a note by ourselves on some other implications of recent developments.



F CASSELL

CASSELL  
TO  
CH/EX  
19/6

FROM: D R H BOARD

DATE: 31 July 1987

*Ch/ See also Mr McGivern's paper below.*

- 1. MR CASSELL
- 2. CHANCELLOR

- cc Chief Secretary
- Financial Secretary
- Paymaster General
- Economic Secretary
- Sir P Middleton
- Sir G Littler
- Mr Lavelle
- Mr H Evans
- Mrs Lomax o/r
- Mr Mountfield
- Mr Scholar
- Mr Culpin
- Miss Noble
- Mr Carpenter
- Mr Cropper

*These various discussions have gone quite well. But there will certainly be some hard bargaining on the 5-7 point discount that Revenue are applying to the matrix figures in determining what is allowable for tax relief. The banks are likely to contest this strongly.*

*Thanks. X does not appear to discuss - of this aspect @ a recent meeting - PRR letter with Mr Cass on that.*

- Mr Battishill )
- Mr Painter ) IR
- Mr McGivern )
- PS/IR

*3. Where stand on Y? Bank v: IR*

INTERNATIONAL DEBT: BANKS PROVISIONING

Officials here, at the Revenue and at the Bank, have now completed their rounds of discussions on this.

2. Mr McGivern's submission of 31 July reports on the substance of the discussions which the Revenue have had with the Bank. It is good that the discussions have been able to produce substantial technical progress, without compromising the distinctive statutory responsibilities of the Revenue and of the Bank. For their part the Bank feel that the talks have been a well worthwhile exercise. They are content with the technical use which the Revenue propose to make of the matrix, although discounting the results by 5-7 percentage points in calculating the amount eligible for tax relief is of course something for the Revenue, not the Bank, to judge. The Revenue have made clear to the banks that prudential provisions might not be allowable in full for tax, but we do not yet know whether the banks have still pitched their expectations from the Revenue/Bank discussions too high. At all events there will be, quite rightly, hard bargaining to come.

3. The estimated Exchequer costs in the Revenue's submission are somewhat lower than their first guess. But they are still

BOARD TO CX 31 JUL

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subject to many uncertainties, and most of these uncertainties point upwards. The point about sovereign versus commercial debt, discussed particularly in paras 15, 19 and 20 of the Revenue submission, is important. The figures being publicised by the clearers for provisions are total figures, ie including existing provisions, provisions against exposures outside the UK tax net, and covering commercial as well as sovereign debt. Standard Chartered will announce its interim results in the next couple of weeks but the figures announced so far by the clearers are annexed. The assumptions which the clearers have also announced about likely tax relief have of course been made entirely on their own responsibility, and that has been made clear. Those assumptions are not a matter for us or the Revenue to comment upon.

4. Having developed this matrix the Bank now need to get on with applying it, with some urgency. Mr Barnes' letter of 29 July, below, attaches the final version of what the Bank propose to issue to relevant UK financial institutions (some of whom have already seen it in draft). The Bank's timetable is to issue the matrix next Wednesday, 5 August, with advance copies to the BBA and to the Association of Consortium Banks the day before. Copies will also be issued, as is routine, to fellow supervisors in the Cooke committee, the European Community and to two or three others.

5. The Bank will only issue a blank matrix, containing neither countries nor scores. Given the necessarily wide circulation of the blank matrix, its existence will come to the attention of the press. Consistent with a low key technical approach, the Bank will not refuse to let journalists have the blank matrix if they specifically ask for it. Of course commentators may quickly come up with their own scored versions of the matrix and will get reasonably close answers. But the Bank will not comment on questions about countries or scores. In handling the press, the Bank will be stressing that the matrix represents one tool in the supervisory methodology, and that many European supervisors have been giving country provisioning guidance for some years.

6. Our Press Office will pass questions about the matrix and its significance on to the Bank. If pressed, our Press Office could also draw on the following:

- (a) this is an entirely proper supervisory activity of the Bank. It would be odd if the Bank were not addressing these important and difficult questions;
- (b) the Revenue and the Bank have different statutory responsibilities which there is no danger of either forgetting. But where the problems which they have to address overlap, it is quite right that they should talk to one another;
- (c) the Treasury has kept in touch with these discussions but has not been involved in shaping the matrix.

7. Our Press Office will also refer tax questions to the Revenue. If asked by the Press the Revenue propose to say that:

- (a) the legal position - set out in the 1983 Statement of Practice - is that tax relief is due to the extent that debt can be shown to be irrecoverable; and
- (b) in dealing with claims for tax deductions on sovereign debt provisions the Revenue will take account of the evidence produced by banks' use of the matrix, to the extent that it is relevant for tax purposes.

*Send this to you*

8. In view of the potential sensitivity (as noted in my submission of 26 June), the Bank are also briefing the FCO, emphasising that the matrix is a supervisory tool only; it is not a Treasury or a Government matrix.

9. The Bank has also kept ECGD informed of these developments. Although the two problems are not identical, ECGD has recently made big changes in its own provisions, carrying the percentage from under 10% to 18% of all sovereign debt (ie debt which has already been rescheduled or refinanced, plus ECGD's other

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X contingent liabilities in those countries). These changes are due to be confirmed by ECGD's Board today and will be published in late August or September. They are not subject to Treasury approval; we believe they are reasonable for this year but will be pressing for a further increase next year. ECGD know that they will have to defend the difference from the Bank's recommendations, both to the press on publication, and to the PAC in due course. They will clear their line with us in good time.

10. This submission is copied to Mr Galpin and Mr Barnes at the Bank of England.

*Douglas Board*

D R H BOARD

*Ref X, 1 (A)  
Wopt so, too.  
It's not the usual  
to use ECGD to  
provision it  
to M...  
an on way  
points in  
is some  
play at  
shops.*

FROM: P MOUNTFIELD  
DATE: 4 August 1987

- 1. SIR G LITTLE
- 2. CHANCELLOR

copies attached:

Chief Secretary  
Financial Secretary  
Paymaster General  
Economic Secretary  
Sir P Middleton

- cc Mr Cassell
- Mr Lavelle
- Mr H Evans
- Mrs Lomax
- Mr Scholar
- Mr Culpin
- Miss Noble
- Mr Carpinter
- Mr Board
- Mr Cropper

*Mr. P... (usual)  
both liaison &  
future (A-XX)*

*See earlier  
papers in separate  
bundle below. This  
decy is at odds  
with your views @  
meeting. It may have  
been ECGD's decision  
but AEF should have kept  
you in the picture*

*Passed on to  
Mr Battishill - IR there  
Mr Painter - IR  
Mr McGivern - IR*

**INTERNATIONAL DEBT: BANKS PROVISIONING**

Mr Taylor records, in his minute of 3 August, that the Chancellor thought our reference to ECGD, in Mr Board's minute of 31 July, did not accord with the discussion at the meeting of 3 July (at which I was not present). *(because he couldn't come, not because he wasn't invited)*

2. In fact, the decision is not strictly one for the Treasury at all. ECGD maintain firmly that the decision is one for them to take, and that our powers are limited to prescribing the form of accounts. To illustrate: in the previous two years, they made much smaller provisions than we told them we thought justified, and the C&AG's report on the trading accounts was heavily qualified as a result. Last year, he made no such qualification. But ECGD themselves, in the light of the Citicorp decision and informal discussions with the Bank of England, decided to increase their general provision this year to just under 18%. Taken together with certain specific provisions, their total cover for political risk is now about 22% - within sight of what the banks have done. ECGD's current policy is to finance this general provision from reserves. In fact they cannot finance it by a transfer from the income-and-expenditure account, because the surplus this year, while positive, is much

*XX*

MOUNTFIELD  
TO  
CX  
4 AUG

too small. They are therefore treating it 'below the line', rather as Midland did. This will however be the last year on which they could do so; changes in the accounts which we have recently agreed will rule out this course in future. And in doing so, they have virtually exhausted their reserves anyway, and have only just avoided showing 'negative reserves' (ie, negative net worth). This provisioning policy follows naturally from the fact that ECGD is required to produce Trading Accounts in line with best commercial practice (unlike many other credit insurers, who are directly financed by their governments on a pay-as-you-go basis).

3. ECGD will find it hard to defend this particular allocation, which is neither one thing nor the other. Logically (as the Chancellor said) the choice is between making no provision at all, and relying on the unspoken support of the Exchequer, or doing the job properly - which probably means provisioning on the level indicated by the Bank of England matrix. Depending on the level of profits next year and the evolution of the debt problem meanwhile, we may well wish to urge ECGD to make an even bigger allocation next year. But in view of the Chancellor's reservations, we would of course consult him before doing so.

R1

P MOUNTFIELD



MR J M G TAYLOR

Ch/ I think the  
assurance in para. 3. commits  
off this correspondence.

X  
10/8

From: Sir G. Littler  
Date: 6 August 1987

c.c. Sir P. Middleton  
Mr Cassell  
Mr Lavelle  
Mr Mountfield

**INTERNATIONAL DEBT: BANKS PROVISIONING**

Your minute of 6 August.

2. There is certainly an element of "playing at shops" in ECGD provisioning. But we have set ECGD up as a kind of shop, with instructions to behave as far as possible as if it were operating commercially. It was on this basis that ECGD embarked on the process of provisioning, and that I and colleagues here pressed (at a time when we were pressing banks to increase provisions) that ECGD should also provision more realistically.

3. We have no legacy of commitment to any particular view for next year. We shall certainly consult the Chancellor before taking up a Treasury position - let alone reaching agreement - on next year's ECGD provisioning. I am asking AEF to review the rationale of ECGD provisioning in good time before then.



(Geoffrey Littler)

*Handwritten red notes:*  
Wass.  
1 note X.