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PART B

1984 BUDGET FINANCE BILL
17 MARCH -

DDs 25years NAzig 25/08/94

PO -CH /NL/~~0015~~ 0819
PART B

COPY 1 OF 21

BUDGET - SECRET

B(84) 751

NB many firms here!
CLA will applaud IIS
Mr [illegible] (who [illegible] : must be stock options
or file) will applaud
Govt & maybe
FT, Sunday [illegible] like Budget
Economist will [illegible] D. Telegraph.)
(so may [illegible]

FROM : M D X PORTILLO
DATE : 2 MARCH 1984

PS/CHANCELLOR

cc PS/Chief Secretary
PS/Financial Secretary
PS/Minister of State
PS/Economic Secretary
Sir P Middleton
Sir L Airey
Mr Fraser
Sir T Burns
Mr Littler
Mr Bailey
Mr Cassell
Mr Monck
Mr Battishill
Mr Evans
Mr Monger
Mr Odling-Smee
Mr Ridley
Mr Hall
Mr Lord

BUDGET PRESENTATION : BODIES AND PERSONS TO BE CONTACTED

At yesterday's Budget Overview meeting I was asked to compile a list of those who should be seen or contacted very soon after the Budget, by Ministers or by officials. The list will need to include those with particular influence or vested interests, with the emphasis on people who can be stirred into welcoming the Budget proposals.

2. I should be grateful for contributions to the list by close on Tuesday 6 March and in the interests of thoroughness I will welcome suggestions however obvious they may seem. Telephone numbers of individuals or companies will be very welcome too.

3. Here is a skeleton to provoke thought (attached).

MP

BUDGET - SECRET

BUDGET - SECRET

Company Tax Reform (including NIS)

CBI - President's Council

Institute of Directors

Institute of Chartered Accountants

Association of British Chambers of Commerce

The Retail Consortium

Leading businessmen who favour reform - Lord Weinstock
Sir Clive Sinclair
Others?

MPs who favour reform

Newspapers/journals which favour reform

Anyone on record on VAT on imports?

Small business groups to welcome 30%?

Oil Tax changes

UKOOA

Brindex - who?

UKOITC - who?

Personal taxation (including LAPR and IIS)

Any group who will speak up to welcome thresholds?

Groups pleased with IIS - National Federation of Self-Employed

Other small businessmens' groups?

MPs, newspapers, who favour end of distortions like LAPR?

What attitude will building societies take on LAPR?

Stock Options

Businessmen prepared to say that change will keep management talent in Britain ie good for jobs eg Dr Herman Hauser of Acorn Computers

BUDGET - SECRET

Composite rate

Any chance the building societies will welcome it publicly?

MPs, journalists who favour even handed treatment

Indirect taxes

Will Scotch Whisky (and gin and vodka) associations cheer in the name of jobs saved?

Pipe tobacco - who will cheer?

Will AA/RAC welcome vintage car exclusion from VED?

Any chance of a nice word from pensioners groups on paraffin?

Wine trade associations

MPs who must be seen

Mr Terence Higgins

Sir William Clark

Mr Peter Hordern?

Mr Edward du Cann?

Mr Anthony Beaumont-Dark?

BUDGET SECRET

(pmf)

CH/EX REF. NO. B(84)468

FROM: MISS J C SIMPSON

DATE: 6 March 1984

cc PS/Chief Secretary
PS/Financial Secretary
PS/Minister of State
PS/Economic Secretary
Sir P Middleton
Sir L Airey
Mr Fraser
Sir T Burns
Mr Littler
Mr Bailey
Mr Cassell
Mr Monck
Mr Battishill
Mr Evans
Mr Monger
Mr Odling-Smee
Mr Ridley
Mr Hall
Mr Lord

MR PORTILLO

BUDGET PRESENTATION: BODIES AND PERSONS TO BE CONTACTED

The Chancellor has seen your minute of 2 March, and has commented that he does not see many friends among the list that you have provided.

2. He has suggested that the Country Landowners Association will applaud the abolition of IIS, and that it must be possible to identify many people and companies who have made representations during the last few months who will applaud the stock options proposals. He has also suggested that the Financial Times, the Sunday Times and maybe the Economist will like the overall shape of the Budget, and that even the Daily Telegraph may also come out in its favour.

B

MISS J C SIMPSON

BUDGET - SECRET

B(84) 750

COPY NO 1.. OF 22

FROM : M D X PORTILLO
DATE : 7 MARCH 1984

CHANCELLOR

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir L Airey
Mr Fraser
Sir T Burns
Mr Littler
Mr Bailey
Mr Cassell
Mr Monck
Mr Battishill
Mr Evans
Mr Monger
Mr Odling-Smee
Mr Ridley
Mr Hall
Mr Lord
Mr Crawley

BUDGET PRESENTATION : BODIES AND PERSONS TO BE CONTACTED

I am grateful for responses to my minute of 2 March. I now attach a draft list of the major bodies and "important" persons to be contacted after the Budget.

2. My preliminary conclusions are:

a) There is no difficulty in finding supporters on NIS, IIS, stock options, VAT on imports, stamp duty etc. The big question is who, apart from Lord Weinstock and Sir Clive Sinclair, will support company tax reform? We have very little idea. In a couple of cases (eg IOD, ABCC) we may need to ring our friends there after the Budget and find out who our likely friends are. But a list of big CT payers from the Revenue might help now (it may already have been commissioned).

b) We need to divide these names in several ways. There are those who must be approached by Ministers or Sir Peter Middleton; and those who can be contacted by officials (including IDT) and advisers. There are those who could go on the media that evening to put in a good word, and others, whether supporters or not, who must be seen at some time soon after, but not immediately.

c) A good impression can be made by contacting people before, during or after the Budget to tell them that a Minister will want to speak to them. That may forestall a number from being too outspokenly critical. The technique is applicable to MPs too.

3. Peter Makeham is now doing some work on who sees whom when, with this list in mind.

4. It would be helpful if IDT could find out who on current plans is going to be on television and radio on Budget Day. On the day, IDT may find this list helpful in recommending to BBC and ITV whom to invite to appear.

5. Preparing this list has made me think again about the problem of how to present the oil tax changes: whether to brief on the benefit to oil from the CT package. If we do not brief even off the record to UKOOA, there is a danger that the initial reaction will be hostile. That might not cause any lasting damage, but it would be better to avoid it. I think we may need to give an unattributable nod and a wink.

MP

M D X PORTILLO

BUDGET - SECRET

BUDGET PRESENTATION : BODIES AND PERSONS TO BE CONTACTED

Body/Person	Attitude
CBI	
Sir Campbell Fraser Sir Terence Beckett Sir James Cleminson President's Committee Committee Chairmen (see lists Annex 1 & 2)	Reform : will vary NIS : welcome VAT on imps:"rushed decision" Stamp duty: welcome Thresholds: "too much" VAT base: uncertain Share options : welcome IIS : welcome
Institute of Directors	
Walter Goldsmith Barry Bracewell-Milnes Bruce Sutherland Graham Mather (for advice on supporters)	Reform : will vary NIS : abolition unnecessary VAT on imps: unknown Stamp duty : welcome? CTT : welcome Thresholds : welcome (why not rates too?) Share options:welcome IIS : welcome?
Association of British Chambers	
Sir David Nicholson John Risk John Ackers Bruce Sutherland (see IOD) Tony Newsome Mr David Nicholson (for advice on supporters)	Reform: uncertain VAT base: unwelcome? Thresholds: welcome Share options:welcome IIS : welcome CTT : welcome

BUDGET - SECRET

Association of Independent Businesses

J B M Donnellan

Reform : uncertain
Thresholds: welcome(why not rates too?)
Share options: welcome
Stamp duty : welcome?
NIS : welcome
LAPR : welcome
VAT base : unwelcome?

National Federation of Self-Employed

Bernard Juby

Stock relief : unwelcome
VAT base : unwelcome
IIS : welcome
NIS : welcome

Union of Independent Companies

Bill Poeton

Consultative Committee of Accountancy Bodies

Reform : welcome

Institute of Chartered Accountants:

Reform : welcome

Eddie Ray - Spicer & Pegler

Reform : welcome

Lord Weinstock - GEC

Reform : welcome

Sir Clive Sinclair - Sinclair

Reform : welcome
Stock Options : welcome

BUDGET - SECRET

George Copeman - Wider Share Ownership Council	Stock Options : welcome IIS : welcome
Dr Herman Hauser - Acorn Computers (spoke at PM's technology conf)	Stock Options : welcome
Building Societies Association - Herbert Walden	Composite rate : welcome LAPR : welcome
Life Offices Association	LAPR : unwelcome
Industrial Life Offices Association	LAPR : unwelcome
Friendly Societies	
Stock Exchange - Sir Nicholas Goodison	Stamp duty : welcome IIS : welcome
Law Society	Stamp duty : welcome
Law Society (Scotland)	Stamp duty : welcome
The Big four banks	Reform : unwelcome (leasing)
NFBTE	Stamp duty : welcome VAT base : unwelcome

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Age Concern	Unsatisfied
Child Poverty Action Group	Unsatisfied
UKOOA: George Band	Welcome (when understood)
BRINDEX: Dr Colin Phipps	Welcome (when understood)
UKOITC : A E Willingale	Welcome (when understood)
Sir John Hoskyns	
Sir John Sparrow	
Sir Hector Laing	
Mr Bond - GEC	
Lord Hanson	
Institute for Fiscal Studies - John Kay	
Institute of Economic Affairs - Lord Harris	

BUDGET - SECRET

Country Landowners Association	IIS : welcome
Clive Thornton - Mirror Group	Composite rate : welcome Reform : welcome? Stamp duty : welcome? VAT base : unwelcome
Financial Times	General welcome Reform :welcome
Economist	General welcome (but wrong reform?)
Sunday Times Andrew Neil Roger Eglin Lionel Barber John Huxley	 General welcome? Cable :welcome
Standard Neil Collins	 General welcome
Daily Telegraph Bill Deedes	 General welcome
Financial Weekly	Unknown
Accountancy	Unknown
Accountancy Age	Unknown
Investors Chronicle	Unknown

BUDGET - SECRET

MPs	Special Interest	Attitude
Sir William Clark	Backbench Committee	Mixed?
Terence Higgins	Select Committee	Mixed?
Anthony Beaumont-Dark	Select/Backbench Committees	Mixed
Peter Hordern		Mixed?
David Howell	PSBR etc	Mixed?
Cecil Parkinson	Business in general Stock Options	Generally in favour?
Tim Eggar	Oil, LTPE, Tax reform	Generally in favour?
Peter Lilley	Oil, PSBR	Generally in favour?
Michael Grylls	Small business Institute of Directors Backbench Industry Committee	Generally in favour?
John Hannam	Backbench Energy Committee Oil	Mixed
Nick Budgen	LTPE Select Committee	Mixed
Nigel Forman	Backbench Committee, Tax reform	Generally in favour
John Selwyn-Gummer	Conservative Party Chairman	-
William Powell (Corby)	Publicity in Liverpool on pipe tobacco duty?	-

BUDGET - SECRET

ANNEX 1

CBI PRESIDENT'S COMMITTEE

Sir Campbell Fraser	President
Sir Terry Becket	Secretary-General
Sir Austin Bide	Glaxo/BL
Sir Richard Butler	National Farmers Union
Sir James Cleminson	Reckitt & Colman (Pres.designate)
Sir Ken Corfield	STC
Ron Dearing	PO
Ken Durham	Unilever
Sir Michael Edwards	ICL
H C Franklin	Chairman - Regional Council
Anthony Fraser	SMMT
J G Gaddes	BEAMA
John Gough	Chairman - Regional Council
Sir John Greenborough	(Shortly Ch. Fin.Cmttee)
Sir Arnold Hall	Hawker-Siddeley
John Harvey-Jones	ICI
Sir Alex Jarratt	Reed International
C F Jeanes	Chairman - Regional Council
Sir Emmanuel Kaye	Lansing Bagnall
Derek Kingsbury	Fairey Holdings
Sir Ian Morrow	Hambros
Norman Payne	BAA
Sir Austin Pearce	BAe
I H Philips	Chairman - Regional Council
John Raisman	Shell UK Ltd
Sir John Read	TSB
Dr Malcom Skillicorn	GKN
Alan Stote	Smaller Firms Council
Charles Tidbury	Whitbread
Sir Peter Walters	BP

BUDGET - SECRET

CBI : CHAIRMEN OF COMMITTEES

Rt Hon The Viscount Colville - British Electric Traction Company
K Durham - Unilever
Sir James Cleminson MC DL - Rickitt & Colman
V G Paige CBE - National Freight Consortium
Sir Alex Jarratt - Reed International
M H Vogel - Air Products Ltd
R I Lindsell - ICI
J M Raisman CBE - Shell UK
Sir John Read - TSB
Sir Austin Pearce CBE - British Aerospace
W J Bartlett - British Paper and Board Industry Federation
D J Flunder MC VRD - No known company connection
R Halstead CBE - Beecham
H P Parry - Amey Roadstone
D J Kingsbury - Fairey Holdings
J M Peake - Baker Perkins Holdings
Sir Campbell Fraser
I D Gardiner - The Electronic Engineering Association
J Charman - ICI
Sir Austin Bide - Glaxo
R J Roots - Fords
A E C Stote - BTS Group
A E Willingale - BP
L S Payne - Sainsbury's

CONFIDENTIAL

PMP

FROM : M D X PORTILLO
DATE : 12 MARCH 1984

C.

PS/CHANCELLOR

See also individual media notes, below

* I do not wish anyone for the Chancellor after the 8pm. [illegible]

cc PS/CST
PS/FST
PS/MST
PS/EST
Sir P Middleton
Mr Battishill
Mr Makeham
Mr Ridley
Mr Lord

BUDGET PRESENTATION : CONTACTS AFTER BUDGET

This morning's Prayers discussed Mr Makeham's minute of 9 March. It was agreed, although some details will change as Ministers make changes between themselves.

2. The Chancellor was anxious that we should now move rapidly to a firm programme of contacts for each Minister. As you will have seen from the Prayers minutes, each private office will be responsible for drawing up such a programme for its Minister. I think that the Chancellor would wish these programmes to be very detailed, showing for example not only when each meeting could be fitted in, but when and by whom contact would be made to arrange it. Early contact from immediately after the moment that the Chancellor sits down, can often forestall unfavourable comment even if the meeting has to be some way ahead.

3. In the case of MPs I would remind private secretaries of the technique of putting a note "on the board" for the Member to find on Budget Day by the time Mr Kinnock sits down. It can say something like: "I know that you will be concerned about subject x, but I know too that you will want to think about the Budget as a whole before reaching a firm view on it. I should be very happy to meet you to discuss your views on it". These notes for key MPs only, would need, of course to be ready before the Budget. Mr David Hunt MP should be informed of those MPs who will be treated in this way. He can locate them in the Chamber and alert them to expect a note.

4. Special advisers will of course help private offices in any way that they can.

5. Private offices will have seen tonight's deadline for the programmes.

J Smith

pp M D X PORTILLO

CONFIDENTIAL

FMP

ECONOMIC SECRETARY TO THE TREASURY

FROM: A M ELLIS
DATE: 12 March 1984

PS/CHANCELLOR

cc PS/Chief Secretary
PS/Financial Secretary
PS/Minister of State
Sir P Middleton
Mr Battishill
Mr Makeham
Mr Ridley
Mr Portillo
Mr Lord

BUDGET PRESENTATION: CONTACT AFTER BUDGET

The Economic Secretary's programme does not include any contacts to be made immediately after the Budget. The plans for contact after Budget Day are as follows:

i) London Clearing Bank: private office to contact on Budget Day with view to meeting on Friday with Kenneth Lucas, Secretary General (283 8866);

ii) Friendly Societies Liaison Committee: letter from Economic Secretary to be delivered after Budget speech to Mr Madders, Chairman of Friendly Society Liaison Committee;

iii) Building Societies Association: private office to contact Herbert Walden on Budget Day with a view to a meeting on Monday 19 March. (The Economic Secretary suggested it may be in impolitic to meet the BSA before their meeting on mortgage rates on Friday.) (629 7233);

iv) Equipment Leasing Association: private office to contact on Budget Day with a view to a meeting on Friday;

v) Sir John Sparrow: Economic Secretary to speak on phone on Wednesday (588 4545);

vi) MPs: Economic Secretary to telephone on Wednesday Michael Grylls; Nigel Forman; John Hannam. N.B. If possible, Michael Grylls to be contacted tomorrow.

A M ELLIS

CONFIDENTIAL

FINANCIAL SECRETARY TO THE TREASURY

PM

FROM: A P HUDSON
DATE: 12 March 1984

PS/CHANCELLOR

cc Chief Secretary
Minister of State
Economic Secretary
Sir P Middleton
Mr Battishill
Mr Makeham
Mr Ridley
Mr Lord
Mr Portillo

BUDGET PRESENTATION: CONTACTS AFTER BUDGET

I attach the programme for the Financial Secretary and this office.

APH

A P HUDSON

FST: BUDGET PRESENTATION

CONTACTS IMMEDIATELY AFTER THE BUDGET

1. Telephone
   Sir Clive Sinclair 0223 353204
   George Copeman (Wider Share Ownership Council) 248 9155

2. Influential Groups to see
   Bruce Sutherland (IOD)
   (Private Office to contact with a view to an early meeting)

CONTACTS AFTER BUDGET DAY

1. Meetings with other representative groups
   Consultative Committee of Accountancy Bodies
   Union of Independent Companies
   Association of Independent Businesses
   (Private Office to contact on Budget Day)

2. Telephone contacts with individuals
   Dr Herman Hauser - Acorn Computers

3. MPs to be contacted personally
   Tim Eggar
   Peter Lilley

4. North Sea Oil Industry
   Send letter to UKOOA
   Copy of letter to UKOOA to be sent to Brindex and UKIOTC

7-16

HOUSE OF COMMONS DEBATES
BUDGET DEBATE

Vol 56, No 118
Tuesday 13 March 1984
(First day)

Summary of Economic and Public Expenditure Points

Col 307	Mr Neil Kinnock (Lab)	Criticised record of past five years - rise in unemployment - fall in share of world trade - use of North Sea revenues
Col 308		Criticised neutral stance of policy Argued for higher public expenditure to stimulate growth and employment
Col 309		Argued that lower inflation not due to Government policy
Col 310		Criticised rise in overseas investment
Col 311		Doubted durability of recovery based on higher personal consumption and borrowing
Col 311	Sir Kenneth Lewis (C)	Commented only on detail of tax proposals
Col 314	Mr Ian Wrigglesworth (SDP)	3 key tests for Budget (a) buttressing growth (b) improving competitiveness (c) helping least well-off On first: Argued that recovery is weak based on consumption, increased personal borrowing and a reduction in the savings ratio Argued that recovery should be sustained by higher capital spending paid for from receipts from asset sales On second: Argued that tax changes would improve competitiveness
Col 316		On third - tax points Criticised stance of fiscal policy - no increase in demand.
Col 317	Mr Robert Banks (C)	Requested further explanation on monetary targets
Col 318		Called for higher limits on part-time earnings for unemployed aged over 55
Col 319		Called for higher capital spending to improve infrastructure possibly using some private finance If public expenditure increased on capital prepared to see higher PSBR Called for more support for textile industry

Col 322	Mr Donald Stewart (SNP)	Argued that balance of trade favourable only because of "Scottish oil" and revenues wasted
		Business confidence in Scotland lower than in rest of UK
		Budget provides little hope of reducing unemployment
Col 323	Mr David Knox (C)	Neutrality not enough. Budget should have raised demand to bring unused capacity - both labour and capital - into use
		Projected growth rates unlikely to reduce unemployment.
Col 324		Higher private and public spending desirable could be achieved by a mixture of reduced taxes and increased capital spending
		PSBR currently too low given position in business cycle
Col 325		Priority should now be to reduce unemployment: inflation substantially beaten.
Col 325	Mr Roy Hughes (Lab)	Neutral budget will do nothing to reduce unemployment
		North Sea revenues "squandered" on unemployment benefit
		Lower inflation does not produce jobs. Called for reduction in unemployment by raising pensioners incomes and spending on capital particularly in nationalised industries
Col 326		Called for controls on overseas investment
		Foreign investment in UK undermines our technical capacity
Col 327	Mr Peter Bottomley (C)	Called for improvements in supply side to meet demand. Tax reform a necessary part of this. Will reduce distortions
Col 329		Called for child benefit to be treated as a tax allowance
Col 330	Mr Austin Mitchell (Lab)	MTFS reduces flexibility. Focus on PSBR to exclusion of other important variables especially in real economy
		Uncompetitive position due to high pound caused high interest rates and contractionary fiscal stance
		Need to lower unemployment by raising PSBR
		Recovery seen in consumption and imports, not output

Debate Adjourned

HOUSE OF COMMONS DEBATES
BUDGET DEBATE

Vol 56 No 118
Tuesday 13 March 1984
(First Day)

Summary of Revenue points

Col 306	Mr Neil Kinnock (Lab)	Budget does more for the City than the country.
Col 307		Welcomed: - rise in income tax thresholds - abolition of National Insurance Surcharge - new procedure for VAT collection. Criticised: - income tax charges as helping those already well off
Col 308		- VAT on takeaway food and home extensions - latter hits construction industry - Extension of composite rate to banks - hurts small saver - abolition of investment income surcharge - helps the well-off - reductions in CTT and CGT - contribute nothing to society - reduction of capital and other allowances - discourages investment
Col 309		Neutrality is not enough.
Col 310		Only those earning over £20,000 have benefitted from this Government's tax reductions. Others have paid more tax. Too much capital going abroad, too much import penetration.
Col 311	Sir Kenneth Lewis (C)	Criticised: - increase in tobacco tax Welcomed: - cut in stamp duty

Col 312		- abolition of NIS
		- corporation tax cuts. Many small businesses can't take advantage of capital allowances
		- reduction of CTT rate - helps small businesses which have to be sold
		- abolition of IIS - investment income provides a pension for many.
Col 313		- VAT on takeaways - exemption was an anomaly
		- charge in rules for VAT on imports
		- switch of tax emphasis to take low-paid out of tax.
Col 314	Mr Ian Wrigglesworth (SDP)	Welcomed: - abolition of NIS
		- reduction of tax burden on businesses
Col 315		Criticised: - reduction in CGT and abolition of IIS - don't help the poor.
		Increases in income tax thresholds welcome but money should have been directed to the very poor. Would prefer a system of amalgamating taxes and benefits.
		Hoped for substantial child benefit increase after May.
Col 316		Critised VAT on takeaways and building alterations - latter hits construction industry.
		Accepted other excise duties.
		Welcomed small size of beer duty increase.

Col 317	Mr Robert Banks (C)	Welcomed: - stamp duty reduction - help for small investors and first-time house buyers. - abolition of IIS - encourages saving. - phasing down of capital allowances - lets businesses make own decisions. Criticised withdrawal of tax concessions for foreign nationals - their expertise needed. Welcomed: - abolition of NIS
Col 318		- VAT changes on tobacco, drink and petrol. Criticised: VAT on building alterations - removes an anomaly but would prefer to have VAT taken off all building works. Welcomed: - change in rules for VAT on imports - raising of tax threshold - helps unemployment.
Col 319		Private capital has major part to play in enterprise zones.
Col 320		More should be done for textile industry. Hotel building allowance shuld go up to 75 per cent enjoyed by industries.
Col 320	Mr Donald Stewart (SNP)	Welcomed: - abolition of NIS
Col 321		- 10p on cigarette tobacco - abolition of duty on kerosene. Criticised: - increase in tax on spirits, though not as large as had been feared

		- VAT on building alterations - hits construction industry
		- VAT on takeaways - hits the poor
		Welcomed improvement in tax allowances.
Col 322		Should have removed VAT on charities and surcharge on electricity.
		North Sea oil being wasted.
		Not enough for unemployed.
Col 322	Mr David Knox (C)	Welcomed: - increase in income tax thresholds
		- modest VAT increases
		- abolition of NIS
Col 323		- changes and reductions in corporation tax - encourage efficiency
		- improve incentives for share schemes
		Critised: - life assurance proposals - perhaps not politically wise
		- lack of encouragement to employ unused buildings, capital equipment and people.
Col 324		- VAT change affecting construction
		Budget should have increased demand by tax cuts and investment in public sector.
Col 325	Mr Roy Hughes (La)	More should be done for unemployed and pensioners.
Col 326		Criticised VAT on home extensions - hits construction industry.
		Should encourage investment in Britain and discourage imports.

Col 327	Mr Peter Bottomley (C)	Welcomed removal of distortions in tax system.
		Hoped for reform of mortgage interest relief system - not mentioned in Green Paper.
Col 328		Welcomed Life assurance measures - tackling "flotsam and jetsam" of tax reliefs. But process of introduction of measures will need debate.
		Tax base should be as broad and rates as low as possible - therefore also welcomed VAT on takeaways and building alterations.
		Right to help the prosperous in order to create employment and revenue.
Col 329		Chancellor right to deal with distortions in taxes on saving.
		Right to remove earned/investment income distinction.
		High rates of tax lead to distorted decisions.
		Child benefit should be regarded as a tax allowance.
Col 329	Mr Austin Mitchell (La)	Budget "moving deckchairs on the Titanic".
		Criticised: - VAT on takeaways - on attack on working people - cut in capital allowances - damages investment. - VAT on building improvements - especially when improvement grants cut. - help to well-off by abolition of IIS, stamp duty reduction, CGT and CTT changes. - lack of anything to tackle unemployment.

Debate adjourned.

Col 478

Welcomed abolition of NIS - should have been done before. But won't foster growth; nor will corporation tax reduction - phasing out means companies will try to defer profits. Will hit manufacturing industry. Financial services and City will benefit.

Mr Barney Hayhoe (MST)

Holiday lettings - caravans which meet conditions will qualify for relief.

Col 479

No VAT on meals on wheels.

Local authority building works and extensions will be taxed, but authorities can reclaim tax. Many improvement grants relate to repairs, which have always been taxable.

Col 480

In progressive income tax system, higher-paid always profit most from reductions. No real increase in higher-rate thresholds. In percentage terms, low-paid gain more. A step in right direction.

Elderly fully protected - 60 per cent of elderly households will pay no tax in 1984/85, others will gain 75 pence (single) or £1.15 (married).

Budget encourages wider share ownership.

Col 482

Corporation tax points to be covered by FST.

Debate adjourned.

"Extension of VAT to imports for one year only" merely brings forward revenue. How will tax cuts financed by this be sustained later?

Col 474

Income tax changes benefit rich most (gave a series of figures) - don't reward enterprise.

Welcomed abolition of tax on cars for disabled.

IIS abolition only favours those with £70,000 capital.

Wanted at least 80 pence increase in child benefit to reflect 12.5 per cent change in allowances.

Col 475

Few people really benefit from stamp duty reduction. Doesn't improve mobility of labour.

Col 476

Abolition of life assurance relief hits poorer savers.

Extension of composite rate to banks brings 3 million people into tax, and taxes some who are on supplementary benefit. Helps rich, who also benefit from stamp duty and IIS measures.

CTT reduction doesn't help enterprise; "a reduction in taxes paid by people who are dead".

Col 477

Composite rate and life assurance measures may lead to less investment in enterprise and more in deposit accounts by rich people.

Phased withdrawal of capital allowances will simply bring forward investment. Capital stock needs bringing up-to-date; allowances are given on new assets.

More profitable investment needed, but growth in economy necessary for this.

Col 466		Indirect taxation increases mean low-paid will pay 91 pence a week more.
Col 466	Mr Nicholas Budgen (C)	Welcomed NIS abolition and reduction in subsidies for capital.
Col 468	Mr Tim Eggar (C)	Welcomed: - stamp duty reduction
Col 469		- change in treatment of stock options. Ministers should encourage employees to take advantage of this. Criticised abolition of IIS at a time when housing benefit reduced.
Col 470		Welcomed corporation tax changes - will decrease avoidance. Right to remove life assurance relief. Should tackle relief on pension investments and mortgage interest, thereby applying principle of corporate tax reform to personal taxation.
Col 470	Mr Michael Hirst (C)	Welcomed corporation tax reform - encourages decision-making without reference to tax regime.
Col 471		Welcomed commitment to simplification of tax system. Should have abolished development land tax.
Col 472	Mr Terry Davis (La)	Drew comparison between this Budget and last Conservative post-election budget - VAT and personal allowance increases. Effect of 1979 has been increased taxation.
Col 473		Tax on takeaways discourages enterprise; tax on building alterations and removal of capital allowances hits construction industry. Not offset by stamp duty reduction.

Would have liked:
- abolition of stamp duty

- more expansion and simplicity in Business Expansion Scheme. Approval of farmers being kept out. Should allow for (1) roll-up of research and development (2) those in entrepreneurial business to take part.

Col 455	Dr Jeremy Bray (La)	Chancellor paying for Corporation tax reductions, which exceed capital allowance reductions, by once-for-all tax on importers. Imprudent in long-term.
Col 458		Given present depressed levels of investment, capital allowances have little distorting effect. Should have been replaced by eg inclusion of research and development in business expansion scheme, or tax allowances on R & D expenditure generally (referred to Select Committee on Science and Technology).
Col 461	Mr Steven Dorrell (C)	Welcomed: - change in VAT collection on imports - corporation tax changes - removal of relief on life-assurance - broadens tax base - increase in income tax thresholds - right on equitable and economic grounds.
Col 463		Must balance tax cuts with right level of public expenditure.
Col 465	Mr David Winnick (La)	Welcomed increased income tax thresholds, but more than three-quarters of families receiving FIS will still pay tax. Only those earning under £18,000 pay less than in 1978/79.

		Should be more encouragement for capital investment.
Col 446	Mr Norman Atkinson (La)	Budget adjustments may have "marginal and indirectly beneficial effect on industry". Profits do not necessarily create jobs.
Col 449	Mr Richard Ryder (C)	Abolition of stamp duty right, though IR document warned of £1 billion cost. A discriminatory tax - discourages achievers and labour mobility.
Col 451	Mr Dafydd Wigley (PL.C)	Welcomed: - NIS abolition - increase in personal allowances, but room for more for single person. Helps well-off most - change in VAT on imported goods; but will once-for-all saving mean £1.2 billion bill if policy later reversed? - relief on vehicles for disabled. Should look at VAT on charities. Criticised VAT on house alterations - what about those waiting for improvement grants?
Col 453 Col 454	Mr John Browne (C)	Special treatment for vehicles for disabled and rise in personal allowances lift people out of the poverty trap. Removal of City's privileges will encourage investment in new enterprise by private individuals. Investment decision-making will be improved by corporation tax, stamp duty, CTT and NIS measures. Capital allowances encourage distortions.

Col [illegible]38 Mr Esmond Bulmer (C)

Congratulated Chancellor on radical programme for industry.

Abolition of NIS will increase efficiency.

Col 438 Mr Bruce Millan (La)

Personal allowance changes expensive but trivial incentive for individual. Together with IIS abolition, they benefit the rich.

Welcomed abolition of NIS, but effect exaggerated.

Col 439

Corporation tax and capital allowances measures look sensible - but will they lead to a surge in uneconomic capital investment in next few years? Will hit manufacturing

Col 440

industry compared with service. Will discourage investment eventually rather than improving its quality.

Stamp duty reduction won't help construction industry, especially after VAT changes and abolition of industrial buildings allowance.

Col 442 Mr David Howell (C)

Welcomed:

- stamp duty reduction

- IIS abolition

- intention of future CGT reforms

- start to uplifting income tax burden

- improved treatment of stock option schemes. Approval of these should be conditional on firms widening employee share ownership schemes. Should be more encouragement of latter.

Col 443

- emphasis on tax-cutting in Red Book. Dynamic effect will offset any drop in revenue - may be no real drop at all.

		Small switch to tax on spending rather than income. Excise duties broadly in line with inflation.
		Extension of VAT base on grounds of consistency.
Col 423	Mr Dale Campbell-Savours (La)	What about construction industry?
	Mr Rees (CST)	It will benefit from NIS, stamp duty, income and corporation tax measures.
		Meals on wheels not affected.
Col 424		New building to remain. zero-rated.
Col 425		Praised abolition of NIS and life assurance premium relief. Latter not retrospective.
Col 426		Stamp duty measures encourage saving without distortion and help City compete.
		Removal of relief for foreign nationals - relief introduced by Labour when tax rates very high. Costly to administer.
		Corporation tax changes bring system into line with present-day needs.
Col 427		A Budget for jobs.
Col 429		Criticised Labour's plan for a wealth tax.
		IIS abolition will improve investment, according to CBI.
Col 432	Mr Roy Jenkins (SDP)	Tax changes for industry won't reduce unemployment. Problem is low profits, not high taxation.
Col 433		Rise in tax thresholds desirable but child benefit increase would be more cost-effective.

pmp

HOUSE OF COMMONS DEBATES
BUDGET DEBATE

Vol 56 No 119
WEDNESDAY 14 MARCH 1984
(Second Day)

Summary of Revenue points

Col 414	<u>Mr Roy Hattersley</u> (La)	Welcomed abolition of <u>NIS</u>.
		On <u>corporation tax</u> measures - if companies retain more profits they won't necessarily
Col 415		invest them. Removal of <u>capital allowances</u> penalises high-growth companies.
		Increase in <u>income tax thresholds</u> helps rich most - should have increased <u>child benefit</u> instead.
		Welcomed removal of duty on <u>paraffin</u>.
		Criticised abolition of <u>IIS</u>, cut in duty on <u>share transactions</u> and <u>CTT reduction</u> - money could be better used elsewhere.
Col 416		Need for <u>VAT on takeaways</u>?
Col 417		Poorer families still poorer under Conservatives - gave various figures.
Col 418		Red Book reveals expected <u>increase in tax take</u>; increase of £21 billion over past 5 years (table 5.6 p39).
Col 419	<u>Mr Peter Rees</u> (CST)	<u>Holiday lettings</u> reliefs to be backdated to April 1982.
Col 420		<u>Cable television</u> ducting to qualify for capital allowances.
Col 422		<u>Income tax</u> - long-term objective to take low-paid out of tax. Third successive increase in <u>personal allowances</u> 12.5 per cent this year. 850,000 fewer taxpayers next year: cost £1,715 million. These increases account for 80 per cent of Budget tax cuts.

UNCLASSIFIED

FINANCIAL SECRETARY TO THE TREASURY

FROM: A P HUDSON
DATE: 14 March 1984

PS/CHANCELLOR

cc Chief Secretary
Minister of State
Economic Secretary
Sir P Middleton
Mr Monck
Mr Battishill
Mr Lovell
Mr Ridley
Mr Lord
Mr Portillo
Mr Makeham
PS/IR

PRESENTATION OF BUDGET MEASURES: POST-BUDGET CONTACTS

1. The Financial Secretary has spoken to three of the people on his list to contact.

2. Sir Clive Sinclair was very pleased with the Budget measures, particularly the company tax package and the new reliefs for share options.

3. George Copeman, of the Wider Share Ownership Council, was pleased at the extension of SAYE limits, and the new share option relief. He asked whether the latter was to be made available only to companies who operated an all-employee scheme, as they had advocated, but seemed to understand the reasons why the Government had come down against this.

4. Tim Eggar MP was very pleased with the whole Budget. He saw no problems with the ACT repayment proposal in the North Sea package.

APH

A P HUDSON

17-16

HOUSE OF COMMONS DEBATES
BUDGET DEBATE

Vol 56 No 119
Wednesday 14 March 1984
(Second day)

Summary of Economic and Public Expenditure Points

Col 414 Mr Hattersley (Lab)	Budget will not reduce unemployment or poverty
	CT reforms will not mean more investment. Higher retained profits likely to be distributed as dividends; invested abroad or saved. Stimulus to investment and growth and increase in demand, which HMG would initiate.
Col 415	Higher child benefit best way to alleviate poverty
Col 416	Calls for higher capital spending + PSBR
Col 417	Budget deflationary - 1984-85 tax receipts forecast up see table 5.6 of FSBR
	Green Paper projections show destruction of education service (? extremely odd)
Col 418	Unemployment and output levels unsatisfactory despite North Sea revenues
Chief Secretary	
Col 430 Mr Roy Jenkins (SDP)	Welcomed decision to target more than one monetary aggregate
	Despite ultimate objective of stable prices, projections published do not show this in foreseeable future
	Rate of recovery not remarkable considering depth of recession and not enough
	Budget mildly restrictive through effect of privatisation (?) and VAT on imports
Col 432	Further reduction in inflation will not generate a spontaneous growth in employment
	Better for industry if Chancellor had raised demand than tax reforms
	Prospect is that current boom shortly over and unemployment could rise further
Col 433	Called for higher public capital spending of £1bn, has a lower import content than spending allowed by raising income tax thresholds

Col 434		Exchange rate mismanaged. When oil runs out there will be pressure on sterling, so we should join EMS to improve stability
Col 435		Not PSBR but total accumulated debt in relation to GDP main impact on interest rates and now less than two thirds of 1964 level
		Need to spend oil revenues on infrastructure and skill training
Col 435	Edmond Bulmer (C)	Raising demand can only provide a small contribution to raising employment. North Sea oil gives opportunity to cushion structural changes eg pay for re-training
		Welcome fall in interest rates
		Can now expect sterling to rise facilitating both inward and outward investment
		Welcome attempts to improve public sector efficiency
Col 437		Hope to see further reductions in LA spending
		Called for higher public capital spending
Col 438	Mr Bruce Millan (Lab)	Judge Budget by effect on unemployment
		Concerned at HMG's attitude to manufacturing. Decline in manufacturing and loss of oil revenues imply future problems on balance of payments
		Need higher investment in manufacturing
Col 441		Called for North Sea oil revenues used to raise demand. PSBR should be raised to level of other industrialised countries and spending on capital raised. Rate of growth projected not enough to reduce unemployment
Col 441	Mr David Howell (C)	Tax cuts preferable to further reductions in PSBR over MTFS period, but requires no change in public spending
		Argued that higher taxes would raise PSBR; private borrowing and money supply
		Argued (a Mr Gilmour) that 1984-85 PSBR is £9¼ billion (£7¼bn + £2bn asset sales)
		Called for higher capital spending on infrastructure (even if PSBR had to rise). Given lagged effect of investment on economy this would sustain growth once recovery in US starts to flag

Col 443	Mr Norman Atkinson (Lab)	Budget won't reduce unemployment. Called for higher wages - a boost to demand Increase in production more important than increase in productivity. Produtivity and profit rises due to cuts in labour force
Col 448		MTFS is "witchcraft" Doubts significance of velocity of money: higher in Germany and Switzerland than in UK, but inflation there still lower
Col 449	Mr Richard Ryder (C)	Tax detail only
Col 450	Mr Dafydd Wigley (PC)	Criticised "lack" of strategy for reducing unemployment
		Unemployment so high throughout UK that measures to raise labour mobility
		Called for higher PSBR and higher capital spending
Col 452		Cuts in public spending hit Wales particularly hard given the significance of agriculture and the nationalised industries in Wales
		Concerned at prospect of lower public expenditure as a percentage of GDP spelt out in Green Paper
Col 456	Bray – Mr J~~ohn Browne~~e (C)	Broad money targets have been broken in past so no longer credible
		Monetary framework does not provide guidance on tightness of policy. PSBR real target
Col 457		Need to pay more attention to exchange rate possibly a fixed exchange rate
Col 458		Should consider balance sheet of public sector assets and liabilities, more important than PSBR
Col 459		Prospects for growth in Green Paper gloomy
Col 461	Mr Steven Dorrell (C)	Growth projections disappointing Accepted that over-optimism dangerous in LTPE context
Col 463		Monetary aggregates unreliable indicator of monetary conditions. Hope ranges in MTFS will not become targets in later years. Tightening projected could constrain output more than inflation
	Should not say this!!	Whole of fiscal adjustment in future years should be used to reduce taxes not to raise expenditure
Col 464		But should raise spending in some areas: training export promotion; education and NHS

Col 464	Mr David Winnick (Lab)	Budget will not reduce unemployment Called for boost to demand and manufacturing
Col 466	Mr Nick Budgen (Con)	Welcomed Green Paper publication, but criticised lack of detail on particular programmes and called for a clearer statement of priorities
Col 467		Called for increased scrutiny of EC budget contributions in Parliament
Col 468	Mr Tim Eggar (C)	Hoped that discussion of MO in Budget Speech does not make an elevation of monetary targets Need to consider all aggregates and exchange rate PSBR of £7.25 billion for 1984-85 not too tight given increase in asset sales and impact of VAT on imports. Real PSBR nearer £8.5-9 billion
Col 469		Welcomed constant cash PSBR for subsequent years of MTFS. If PSBR is not reduced further, reasonable to hold public spending constant and take fiscal adjustment in tax cuts
Col 470	Mr Michael Hirst (C)	Tax detail
Col 471	Mr Terry Davis (Lab)	Called for a real terms rise in child benefit Remainder on tax detail
Col 478	Minister of State	

Debate Adjourned

pmp

HOUSE OF COMMONS DEBATES
BUDGET DEBATE

Vol 56 No 120
Thursday 15 March 1984
(Third Day)

Summary of Revenue points

Col 525	Mr Tom King (SS Emp)	Welcomed: - abolition of NIS gives industry £1,350m per annum, £865m for private sector - corporation tax changes - acceleration of investment due to phased reduction of capital allowances - measures to help small businesses - rise in tax thresholds - change in VAT requirements for importers
Col 526		
Col 529	Mr John Smith (La)	NIS abolition welcome but doubted impact on unemployment - earlier reduction did little. Corporation tax changes tilted against manufacturing. Abolition of capital allowances will help supply industries by bringing forward capital purchases - but effect short-lived.
Col 530		Extension of VAT to building alterations hits construction industry. Measure criticised by Building Employers' Federation.
Col 531		Criticised abolition of IIS if child benefit not to rise by more than inflation. Only those with capital over £70,000 will benefit.
Col 532		Economic problems will be accentuated by dwindling oil revenue.
Col 535	Sir Ian Gilmour (C)	Grateful for NIS abolition - but why not earlier?

Col 537		This is best year for oil - will deteriorate.
Col 538		Budget "strong on tactics and weak on strategy".
Col 538	Mr Brynmor John (La)	Families with children - Child Poverty Action Group's "tax break-even point" shows shift against them in last 4 years. Threshold increases don't help those already below threshold. Child benefit increase needed. To provide money:- Should abolish upper earnings limit on NI contributions.
Col 540		Or should raise thresholds by inflation rate only (5.3%). Should introduce tax for invalidity, maternity and sickness benefit instead of 5% abatement - one in five to ten would then not be liable.
Col 541		Criticised VAT on building alterations - many houses unfit to live in.
Col 542	Sir Brandon Rhys Williams (C)	Welcomed: - NIS abolition - IIS abolition: investors won't just go for capital gains. - corporation tax reduction and removal of distorting effect of stamp duty and capital allowances - CTT reduction - removes uncertainty of providing for it. Criticised: - income tax cuts - funds released will go into consumption not investment - abolition of life assurance relief - will reduce funds in capital market by c. £700m per annum.

Col 543		Upper limit on relief for payments to pension funds should be 100%.
		Should treat indexed debentures in same way as bank debts for tax.
		Should be greater latitude in rules for joint public/private sector investment.
Col 545		Ineffiency in public sector - COP being introduced in wrong way.
		Should have tax credit system.
		Would prefer child benefit increase to rise in allowances.
Col 547	Mr Archy Kirkwood (Lib)	Poverty trap - Budget doesn't change unsatisfactory system.
		Welcomed rise in personal allowances - but not enough.
		Stamp duty cut won't help first-time house buyers.
		IIS abolition won't help poor pensioners.
Col 548		Lower thresholds should have gone up by up to 5%, or VAT released. Plans don't redress indirect/direct taxation balance - poor pay more of both. Cited Low Pay Unit figures. Alliance would increase child benefit in line with tax allowances and redress tax burden for poor Tax level now below poverty line.
Col 549		Abolition of kerosene duty is Budget's only help to pensioners.
		Woodlands: Alliance will consider ways of stopping loophole.
		Tax credit scheme needed.

Col 549	Mr Terrence Higgins (C)	Welcomed abolition of NIS and IIS, and rise in tax thresholds.
Col 550		VAT on takeaways and building alterations - line will be difficult to draw.
		Holiday lettings - back-dating welcome.
		Welcomed assurance that abolition of life assurance relief won't affect pensions.
		Change in tax on people working overseas harsh.
Col 551		"Medium-term tax strategy" will simplify taxation. Should abolish earnings rule.
		Hard to appraise effects of measures on stamp duty, composite rate, capital allowances (effect on leasing?), building societies, VAT on imports.
		Glad Chancellor didn't agree to proposals to tax banks.
Col 554	Mr Bryan Gould (La)	Oil has contributed £9bn to tax revenues - but will fall.
Col 558	Mr Alan Howarth (C)	Welcomed personal income tax cuts and reform of financial markets and business taxation.
		Hoped phasing out of capital allowances and removal of bias against employment wouldn't damage productive investment.
		Welcomed NIS and stamp duty measures.
Col 559		Green Paper disappointing. Tax policy can do much to hold down public spending eg in housing field.
Col 560	Mr Charles Kennedy (SDP)	VAT on imports good news, VAT on building alterations bad for construction industry.

Col [illegible]2		Child benefit should match increase in tax allowances.
Col 564		Alliance approve of IIS abolition, but only in context of overhaul of tax and benefit system.
Col 564	Mr Charles Morrison (C)	Welcomed - NIS abolition - corporation tax/capital allowances changes - will improve quality of investment. Should reduce betting duty.
Col 565		Throughbred studs should be assured of CTT agricultural relief. Welcomed CTT reductions and income tax allowance increases.
Col 567	Mr Roger Freeman (C)	Glad Chancellor kept relief on contributions to pension schemes and tax exemption for pension funds. Pensioners will welcome threshold increases, abolition of duty on kerosene and parafin, IIS abolition.
Col 568	Dr Oonagh McDonald (La)	Only c.180,000 pensioners have at least £70,000 capital and so benefit from IIS abolition.
Col 568	Mr Freeman (C)	Many of these have no other soruce of income. Abuse of life assurance relief could have been stopped: Chancellor has thrown out attractive baby with dirty bath water. Should remove rules that abate 2/3 maximum on pensions. Rise to 100% would be too much.

		Should be more flexibility in rules for additional voluntary contributions to pension schemes.
Col 569	Mr Nicholas Winterton (C)	Welcomed NIS abolition.
		Criticised abolition of life assurance relief - will deprive City of funds.
Col 571		Criticised capital allowances measure - most companies have used allowances wisely. Corporation tax plans welcome - but many companies don't make enough profits to invest on hoped-for scale.
Col 572		Supported rise in thresholds for basic rate and indexation of higher bands - but more will be needed for poor eg child benefit.
		Regretted VAT on building alterations - will increase black economy.
Col 573		Capital allowances removal will hit dairy industry hard.
Col 574	Mr D N Campbell-Savours (La)	VAT on building alterations will encourage total demolition as opposed to renovation and so damage heritage.
Col 575		Criticised VAT on takeaways, CGT and CTT measures - hurt poor, help rich.
Col 576	Mr Nicholas Lyell (C)	Welcomed simplification of tax system and concentration on thresholds. Hoped for reform of tax and benefit system.
		Welcomed share option scheme, IIS abolition.

Col 577	Mr Robert McCrindle (C)	Criticised abolition of life assurance relief - blow to insurance industry and poorly-off. Need only have stopped abuse. To achieve "fiscal neutrality" should rather extend relief to other savings.
Col 579		Intention to remove mortgage interest relief? Or pension contributions? Self-employed retirement annuities?
Col 580	Mr Dave Nellist (La)	Budget for rich. Help for poor offset by VAT rises.
Col 583	Mr Timothy Yeo (C)	Welcomed: - stamp duty reduction
Col 584		- exemption from CGT on corporate fixed interest stock. Hoped for solution next year to problem of CGT on inflation gains; also new incentives for equity investment (of loi de Monory). - NIS abolition - corporation tax measures
Col 585		Criticised: - VAT on building alterations - hits construction industry. - no commitment to increase child benefit in line with tax allowances. no VAT relief for charities - also hit by charge on building alterations.
Col 585	Dr Oonagh McDonald (La)	Tax burden on low paid still higher than in 1978-79. Indexation of personal allowances would have taken 500,000 out of tax anyway. Tax threshold below poverty line. 160,000 recipients of FIS paying tax.

		IIS abolition benefits few.
Col 587		CTT and stamp duty measures too expensive.
		Poor hit by VAT increases and indexation.
Col 588		NIS originally imposed after generous stock relief introduced. Earlier reduction had little effect; abolition will have less.
		Capital allowances change will damage investment.
Col 590	Mr John Moore (FST)	Corporation tax measures - Opposition have advocated this kind of measure.
Col 591		Distortions of present system produce emphasis on tax efficiency not investment efficiency. Changes will give better return on investment; and allow free decision-making.
Col 593		Changes to be phased in to allow for adjustment.
		Announcement of 4 years in advance gives certainty.
		New tax rates will compare favourably with other countries.
Col 594		Will increase profits and hence employment; also remove bias in favour of capital assets.
		Abolition of life assurance relief must be seen in context of total personal savings.
Col 595		Mortgage interest relief - commitment by PM already.
		Alliance confused on IIS policy (see cols 547 and 564).

Col 396

Stud farms: IR discussing with Horse and Pony Taxation Committee.

VAT on construction industry to tackle anomaly and evasion. Industry will benefit from lower tax rates.

Debate adjourned.

CHIEF SECRETARY TO THE TREASURY

FROM: PAUL PEGLER
DATE: 15 March 1984

PS/CHANCELLOR

cc PS/Financial Secretary
PS/Minister of State
PS/Economic Secretary

POST-BUDGET CONTACT

The Chief Secretary today met Mr Streeter and Mr Newman from the American Embassy.

2. The discussion concentrated largely on the impact of the Budget. The Americans had clearly found the Budget astonishing both in its positive impact on the business world and the degree of confidence it had brought to the City. They considered the tax and other changes relating in particular to investment as a very healthy development which would stimulate confidence for the future. It was clear that they saw the Budget as a step in the right direction for stimulation of long term industrial development and they were impressed by the size of that step.

3. On one point of detail, they had received many calls from Americans working in the UK about the impact of the changes on foreign earnings and emoluments.

4. I have minuted the Revenue separately about this.

Paul Pegler

A PS/CHIEF SECRETARY

FROM: M E Corcoran
DATE: 15 March 1984

PS/CHANCELLOR OF THE EXCHEQUER

cc PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
Sir Peter Middleton
Mr Battishill
Mr Makeham — Mr Hall
Mr Ridley
Mr Lord
Mr Portillo
PS/Customs & Excise
Mr Jefferson Smith - C&E

BUDGET PRESENTATION: CONTACTS AFTER THE BUDGET

The Minister of State has now met the Building Employers Confederation (formerly the National Federation of Building Trades Employers).

Most of the discussion was taken up with the extension of the VAT base and the effects of this on the construction industry. They expressed anger and amazement at the extension to alterations and considerable concern about the effect on the industry. They made two specific points as possible ways of mitigating the effects and the Minister said he would pass these on to the Chancellor. They were:

i. to introduce a lower VAT rate covering the whole area of repairs, maintenance and alterations;

ii. to postpone the 1 June start since 10 or 11 weeks would not be long enough to allow many existing schemes to be completed or adjusted while a longer period would allow the phasing of work so as to keep it flowing.

While recognising the industry's concern, the Minister made it clear that the Chancellor's judgement was that a 15 per cent rate and a 1 June start were right.

Mr Hall may care to note that the BEC intend issuing a press notice putting their views. They will refer to the fact that they have made representations to the Minister and that he undertook to report to the Chancellor what they had said.

M E CORCORAN
Private Secretary

HOUSE OF COMMONS DEBATES — Vol 56 No 120

BUDGET DEBATE — Thursday 15 March 1984

(Third Day)

SUMMARY OF ECONOMIC AND PUBLIC EXPENDITURE POINTS

Col 522	Secretary of State for Employment	
Col 527	Mr John Smith (Lab)	Budget will not reduce unemployment. No projections of unemployment given, suggests no strategy for reducing unemployment.
Col 529		Corporate tax reductions may be used to raise wages and profits not employment.
		Called for more support for manufacturing, necessary to recovery.
Col 530		Budget maintains deflationary stance of policy.
		Called for higher public capital spending on housing and infrastructure.
		Called for long-term sup.ben rates to be extended to long-term unemployed with families.
		Called for real rise in Child Benefit.
		North Sea oil revenues wasted, sterling and interest rates too high.
		Recession in past result of domestic policies not difficulties in world economy.
Col 536	Sir Ian Gilmour (Con)	Called for long-term sup.ben to be paid to unemployed.
	Not necessarily! (But we'll have to show this!)	Budget will not create jobs. Until employment rises, recovery is not underway.
Col 537		Concerned that continuation of policy means higher unemployment, lower investment and output and, with falling North Sea revenues, balance of payments problems.

Col 537 (continued)		Monetary aggregates and PSBR - irrelevant intermediate targets. Called for longer time span in IAF. Growth over next few years unlikely to reduce unemployment. Balance of trade deteriorating. Inflation still a potential problem.
Col 538	Mr Brynmor John (Lab)	Should discuss social security in Budget Debates. Called for long-term sup.ben to be paid to unemployed. Restoration of 5 per cent abatement on invalidity, maternity and sickness benefits.
Col 541	Sir Brandon Williams (Con)	Tax detail.
Col 548	Mr Kirkwood (Lib)	Called for increase in Child Benefit in line with basic income tax thresholds. - Restoration of housing benefit cuts - Improvement of pensioners' living standards.
Col 549	Mr Terence Higgins (Con)	Welcomed extension of MTFS. Regretted separation of public expenditure and budget debates. Just as decisions on two subjects need to be brought together. Suspected that public spending still determined taxation and not vice versa.
Col 552		Criticised treatment of asset sales in PSBR. TCSC will return to this. Welcomed lower PSBR and prospects for interest rate cuts.
Col 553		Green Paper only framework for study of long term.
Col 553	Mr Bryan Gould (Lab)	Criticised record on unemployment, output, balance of trade, competitiveness.

Col 553	Continued	
	Mr Bryan Gould (Lab)	Without North Sea oil revenues, Government would have been in serious difficulties over past 5 years.
		Rate of recovery not remarkable given depth of recession. Even if recovery continues significant loss of resources which cannot be made up.
		Rate of growth and productivity unlikely to be maintained.
Col 555		Criticised the evidence showing relationship between £M3 and prices. Wide range of targets introduced to raise probability of any being met.
		Government resorting to fiscal deflation.
		Called for increase in demand.
Col 556	Mr Alan Howarth (Con)	Priority should remain control of inflation. Sorry that stable prices beyond time horizon of MTFS. Statements in Green Paper studiously vague and imprecise.
		Welcome increase in number of aggregates targetted.
Col 557		Called for a balanced budget as concomitant to stable prices.
		Prospects for growth in 1985 and subsequently not as good as FSBR suggests.
Col 558		Green Paper a disappointing document. Should have examined more precisely the pressures on expenditure and set out priorities. Called for more privatisation of services.
Col 560	Mr Charles Kennedy (SDP)	Budget will not reduce unemployment. Neutrality not enough.
		Called for higher social security spending, especially on unemployment and Child Benefit.

Col 564	Mr Charles Morrison (Con)	Called for long-term sup.ben to be paid to unemployed.
		Budget will do little to reduce unemployment. Major political problem.
		Called for improvements to training and competitiveness.
Col 566		Only way to reduce unemployment. Construction needs a boost by higher public spending on capital. Higher PSBR could accommodate this. Given external forces probably can't get interest rates down by reducing PSBR.
Col 567	Mr Roger Freeman (Con)	Tax points only.
Col 569	Mr Nicholas Winterton (Con)	Concerned that Government does not recognise important contribution made by manufacturing. So UK will not be able to take advantage of upturn "when it comes".
		Called for extension of small engineering firms investment scheme to textiles and clothing.
Col 571		Criticised rises in energy prices.
		Welcomed progress on inflation and interest rates.
		Called for increased spending on public sector capital.
		Called for higher war widows pensions.
Col 573	Mr Campbell-Savours (Lab)	Budget will not reduce unemployment. Should have reflated demand.
Col 576	Mr Nicholas Lyell (Con)	Called for a simplification of social security system.
		Called for higher spending on ITS and CP.
Col 577		Budget good for unemployment in long-term but need to alleviate position in short-term. Need to use resources of youth, possibly to provide social services, where limited resources identified by Green Paper.

Col 577	Mr Robert McCrindle (Con)	Spoke entirely on LAPR.
Col 580	Mr Dave Nellist (Lab)	Doubted-that higher profits would feed through into higher employment; - that recovery on the way. Quoted Mr McMahon (Bank) on "negative investment in manufacturing in past 2 years". Argued that increased demand met by imports not higher output. - deficit on manufacturing trade hidden by North Sea output.
Col 582		Called for exchange controls.
Col 583	Mr Timothy Yeo (Con)	PSBR too low (though VAT on imports should be discounted). Called for higher capital spending Budget will raise employment.
Col 584		Welcomed reduction in inflation - and control over wage costs.
Col 585		Called for extension of long-term sup.ben to unemployed.
Col 585	Dr Donagh McDonald (Lab)	Budget will not help low paid or reduce unemployment.
Col 588		Criticised unemployment assumptions in MTFS.
Col 589		Government relying too heavily on North Sea revenues. Argued that services will not provide sufficient employment opportunities. Overall employment prospects in services improving slightly for men but not for women. Argued that fiscal stance too tight. Aims of MTFS unclear,- little decline in inflation shown in FSBR; - restrictive monetary policy futile if stable prices not achieved. Called for higher PSBR and capital spending to sustain recovery. Argued that recovery based on higher personal consumption and borrowing likely to be shortlived.

UNCLASSIFIED

FROM: A M ELLIS
DATE: 16 March 1984
(amid 19/3)

PS/CHANCELLOR — 2

c/x OK?
MOM
19/3

Good. I agree with X, but re BST might Cmnd stay re BBA instead. N.

cc PS/Chief Secretary
PS/Financial Secretary
PS/Minister of State
Sir P Middleton
Mr Battishill
Mr Hall
Mr Makeham
Mr Ridley
Mr Lord
Mr Portillo
PS/IR
Mr Cassell
Mr Lankester
Mr Pirie
Mr Saunders
Mr Ilett

BUDGET PRESENTATION: POST-BUDGET CONTACTS (see also pps below)

The Economic Secretary met Mr Mitchener and Mr McDonald of the (Equipment Leasing Assoc) this morning and Mr Walden, Mr Weir and Mr Bolleat of the BSA this afternoon. Mr Stubbington is minuting separately in detail on these meetings but in short the BSA were pleased with the Budget and the ELA were philosophical.

(see below for both BSA v. [illegible])

Sir Timothy Bevan of the CLCB will be 'abroad' today and unavailable on Monday and the Deputy Chairman is also abroad. The Economic Secretary's preference is therefore to drop the idea of Ministerial contact with the CLCB in this exercise.

X

Mr Pirie has suggested that it might be useful for the Economic Secretary to see a representative of the Finance Houses Association and I will try and arrange this for Monday. The Economic Secretary also spoke to Michael Grylls in the House on Budget Day and he responded favourably. Specifically, he felt that the concerns of the Grylls Group on the lack of measures to revitalise private investment had largely been met and that therefore the resurrection of contacts between the Treasury and the Grylls Group which he had suggested to the Economic Secretary before the Budget would no longer be necessary.

Hooray!

AE

A M ELLIS

cc PPS
Sir P Middleton
Sir T Burns
Mr Cassell
Mr Monck
Mr Monger
Mr Lankester
Mr Evans
Mr Odling-Smee
Mr Lovell
Mr Scholar.
Mr Battishill
Mrs Goodman

COMMITTEE OFFICE
HOUSE OF COMMONS
LONDON SW1A 0AA
01-219 5766 (Direct Line)
01-219 3000 (Switchboard)

TREASURY AND CIVIL SERVICE COMMITTEE

PRESS NOTICE

The 1984 Budget

The Treasury and Civil Service Committee will be taking oral evidence on the Chancellor's Budget at two meetings this week.

Wednesday 21 March in Room 15
at 4.30 - Mr Robin Leigh-Pemberton, Governor of the Bank of England.

Thursday 22 March (room to be announced)
at 10.30 - CBI witnesses (led by Sir James Clementson)

at 11.30 - TUC witnesses (led by Mr Len Murray).

Both meetings are open to the press and public.

19th March 1984 S. Priestley

pd

SAP H3

HM TREASURY

OFFICE NOTICE

ON(LONDON)(84)1
18 January 1984

BUDGET SECURITY

I attach a note detailing this year's Budget Security instructions. These paragraphs should be inserted in the copy of "HM Treasury Security Instructions" in your possession.

2. The special arrangements for Budget security are designed to give additional protection to information about Budget decisions. Heads of Divisions should ensure that staff likely to handle Budget papers are familiar with the security instructions and understand them. It is, however, the personal responsibility of each member of staff to ensure that Budget security procedures are strictly followed.

3. This year's instructions are little changed from the previous edition. But there are a number of points to which I would draw particular attention.

(i) Budget classified information should be communicated to staff in the Chancellor's Departments and the Office of the Parliamentary Counsel <u>only</u> if they need to know about it for the efficient performance of their duties and <u>must not</u> be communicated to <u>anyone</u> outside these Departments without prior authority (paragraph 145).

(ii) All papers recording Ministerial decisions on the Budget judgement and the PSBR, taxation matters and any social security changes to be announced in the Budget <u>must</u> include the BUDGET prefix in their security classification (paragraphs 140-143).

(iii) The instructions stress (paragraph 144) that Budget classified documents should be seen by the <u>absolute minimum</u> of staff consistent with operational needs. It is the responsibility of the authors of Budget classified documents to ensure that this is done. Recipients should see only that part of a document which is strictly necessary for the proper performance of their duties.

(iv) Papers carrying the BUDGET:SECRET classification must not be taken out of the office unless this is absolutely unavoidable (paragraph 151).

(v) The rules for the control of Budget classified papers - and particularly those for the transmission of papers outside the building (paragraphs 146-149) - must be strictly adhered to throughout the Budget period. Heads of Divisions and Private Offices should ensure that support staff carrying out such tasks are correctly applying the required procedures.

(vi) The system of special spot checks on Budget classified documents (paragraph 147) will continue. The checks are carried out on my authority and I would ask that all members of staff should co-operate in them, so that they can be carried out with the minimum of disturbance to all.

4. The Treasury has a good record in protecting the physical security of Budget documents and I do not want the Department to be responsible for any premature disclosure of Budget information. The incidents during 1983 of the unauthorised disclosure of confidential information and the particular pressure under which the Department works during the Budget period both underline the need for the greatest possible care in handling Budget material and for strict adherence to security procedures.

PETER MIDDLETON

XII. BUDGET SECURITY

139. Special security arrangements apply to certain information connected with the Budget. The arrangements apply in addition to the normal departmental security procedures and are intended to provide additional protection for information about budget decisions.

Budget classification and its use

140. The Budget security arrangements apply to information concerning Ministerial decisions on:

(a) the Budget judgement and in particular the PSBR;

(b) taxation matters;

(c) any social security changes announced in the Budget.

The Budget classification must, therefore, be used for papers on which such decisions are recorded or referred to and on papers from which such decisions could be inferred.

141. A Budget classification is not, in general, required for papers containing:

(a) Ministerial decisions relating to economic forecasts, monetary policy, exchange rate policy and other items not directly related to tax or social security decisions, even where these are in the context of a Budget;

(b) arguments for and against a particular course of action, or recommendations from officials to Ministers;

(c) lists of options in which no decision on any of the matters in paragraph 140 is recorded.

142. In addition to the rules set out above, the Budget classification may be applied to papers which are regarded as particularly sensitive despite the fact that no decisions are recorded - where, for example, the very fact that a matter is being discussed is sensitive, or where the total contents of a document might reveal the approach to the Budget likely to be adopted by Ministers. Care and common-sense are needed in applying the classification in such cases. In <u>any</u> cases of doubt over the use of the Budget classification the Treasury Budget Security Officer (see paragraph 155) should be consulted.

143. The classification requires that the ordinary security classification of documents be prefixed by the word BUDGET. BUDGET: TOP SECRET should only be used where the material would fall clearly within the definition of TOP SECRET even if it were not to be included in the Budget. BUDGET: SECRET is the correct classification for papers on the main Budgetary items (ie the main tax rates and social security benefits and major changes in tax legislation). BUDGET: CONFIDENTIAL should be used for the remainder, including all decisions on other tax items.

Communication of Budget classified information

144. The circulation of Budget classified documents should be restricted to the <u>absolute minimum</u> consistent with operational requirements. All authors of Budget classified material should, therefore, ask themselves:

(a) is the document necessary, and need it be circulated?

(b) is a Budget classification necessary?

(c) do all recipients need a copy? Would part of the document suffice for some?

<u>The practice of circulating only parts of documents to selected recipients should be adopted whenever possible.</u>

145. BUDGET classified information should be communicated to staff in the Chancellor's Departments (and the Office of the Parliamentary Counsel) only if they need to know about it for the efficient performance of their duties. Budget classified information must not be communicated to anyone outside the Chancellor's Departments and the office of the Parliamentary Counsel without prior authority having been obtained from the Budget Security Officer. There are only two general exceptions to this rule. First, FP group have authority to communicate to specified Department of Transport officials Budget decisions on VED and the duties on hydrocarbon oils. Similarly, the head of FP has authority to communicate to specified officials in the Department of Health and Social Security certain information about Budget changes in personal taxation. Second, as is appropriate for public expenditure matters, ST group will discuss any social security changes to be announced in the Budget with DHSS officials. In all these instances the Divisions concerned must ensure that these Departments are aware of the need for particular care in handling the information.

Handling of Budget classified documents

146. The recipient of a Budget classified document is, at all times, personally responsible for its security. This applies even if custody of the document is entrusted to another member of his or her staff.

147. To ensure that the required procedures are being adhered to, Budget classified documents will be subject to a series of spot checks. There will be random checks, carried out by FP1 division, of individual copies of classified documents sent to named individuals. There will also be more systematic searches, carried out by EOG, of complete circulation lists of particularly sensitive Budget classified papers.

148. The normal rules for the control and transmission of classified documents (paragraphs 40-99 of HM Treasury Security Instructions) should be applied to all which carry the prefix BUDGET. BUDGET: TOP SECRET documents must always be transmitted in double envelopes and be accompanied by a document receipt. If sent outside the building, the inner envelope should be wax sealed and bear the special TOP SECRET address label. Double envelopes must also be used for BUDGET: SECRET

and BUDGET: CONFIDENTIAL documents sent outside the building. Single envelopes may be used when they are sent, via the messengers within the Treasury. BUDGET: SECRET documents sent outside the building must also be accompanied by receipts. If two or more papers are put in the same envelope the inner envelope should be marked "two (or more) enclosures".

149. BUDGET: TOP SECRET and BUDGET: SECRET documents should normally be sent by messenger to other departments. If no messenger is available, they should be sent by special signature service of the IDS, a receipt being obtained from the post room. BUDGET: CONFIDENTIAL documents should be sent either by messenger or the IDS. Budget classified documents should not, <u>in any circumstances</u>, be sent by post or transmitted on facsimile equipment.

150. Paragraph 52 sets out the rules for photocopying BUDGET: TOP SECRET and BUDGET: SECRET documents. A similar record should be kept of copies of BUDGET: CONFIDENTIAL papers. Recipients should as far as possible avoid making copies of <u>any</u> Budget classified document.

151. Paragraphs 66-73 specify the arrangements for taking classified papers out of the office. BUDGET: SECRET papers are subject to the overriding restriction that they must <u>not</u> be taken out of the office unless <u>absolutely unavoidable</u>. In such an event, they should be carried in a locked briefcase, box or pouch and kept securely at all times.

<u>General points</u>

152. BUDGET: SECRET documents need not be numbered if less than 21 copies are produced. If 21 or more copies are produced they should be numbered in the same way as ordinary SECRET documents, in accordance with the normal security instructions.

153. Budget classified papers must <u>not</u> be typed in typing pools. Particular care should be taken about the custody of carbons, photocopies, dictating machine tapes, word-processing discs, shorthand notes etc containing classified information.

154. All BUDGET: SECRET or TOP SECRET waste should be destroyed by shredding; arrangements for this may be made with the Executive Officer in charge of Committee Section (extension 4917). Recipients of Budget classified documents must keep a proper record of any they destroy. If a document has been destroyed, the production of such a record is necessary to meet the requirements of the spot checks described in paragraph 147.

155. Budget classified papers must not be sent to sector registries before Budget day. "Allocated clerks" may file Budget classified material, but files must show the appropriate classification until after the Budget.

Queries

156. Any questions about the Budget Security instructions should be addressed to the Budget Security Officer, who is the Principal in FP1 Division (extension 6047) concerned with Budget matters.

FROM: R H AARONSON
DATE: 19 MARCH 1984

Minute overleaf
RA 19/3

1. MR ALLEN
2. CHANCELLOR

PWP

cc: Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Mr Byatt
Mr Cassell
Mr Battishill
Mr Monger
Mr Folger
Mr G P Smith
Ms Seammen
Mr Martin
Mr Lord
Mr Portillo
Mr Isaac)
Mr Blythe) I.R.
Mr Painter)
Mr Calder)

BUDGET DEBATE: IFS ARTICLE

Mr Allen's minute of 16 March warned that the Institute for Fiscal Studies (IFS) would be analysing the distributional effects of the Budget in the weekend press. As expected, their research appeared in the Sunday Times and is also referred to by Michael Meacher in this morning's Guardian (copies attached).

2. Since the Opposition usually draw on the IFS analysis in the debate, some briefing is attached, although the article contains fewer points which might be quoted against the Government than in previous years. For example, most people are shown as gaining from the Budget.

R.H. Aaronson

R H AARONSON

58/3

This is a useful analysis of the IFS article which, fortunately, stops short of some of the more tricky questions concerning the tax/benefit interaction.

2. You asked whether it is true that more families will benefit from the increase in personal allowances than they would from an (equal cost) increase in child benefit. The short answer is "yes". For the Debate this evening, I would suggest you say something on the following lines:

> "Some have argued that raising child benefit is a better way of helping the poor or of alleviating the poverty and unemployment traps than raising tax allowances. Of course one can do sums showing that a family with children does better out of an increase in child benefit than an equal-cost increase in tax allowances. But the other side of the coin is that whereas only some 6 million families would gain from an increase in child benefit, about 20 million families or single people will gain from the proposed increase in allowances, more than three times as many".

Another - but perhaps less effective - way of making the same point is that only some 40 per cent of working-age households have children and so would benefit from an increase in CB. The other 60 per cent would not gain at all,nor would their incentives to work be improved.

3. I also attach some (manuscript) amendments which the Revenue have suggested on the speaking material I sent you on 16 March.

RA

R I G ALLEN

FACTUAL

1. As in previous years, the IFS have analysed the effects of the Budget on typical families, and compared their position next year with their pre-1979 position. The method involves selecting families from the Family Expenditure Survey and attributing pay and price rises thought appropriate for that type of family. The results are thus rather dependent on the assumptions made and the "typical" families do not necessarily reflect the average of the whole population.

2. The IFS's main conclusions are:

Changes since 1978-9

(a) Most families are better off.
(b) The rich have done best.
(c) The family whose head is unemployed is 15% worse off.

Effects of the Budget

(d) Most families gain (in real terms).
(e) Among the working population, there is no clear distributional pattern. Although there is some tendency for those on low incomes to gain less, the biggest percentage gain is at £7,000 a year.

(The second biggest is at nearly £50,000.)

(f) The only losers are the pensioner couple, mainly because of tobacco duty.
(g) There is not much improvement in the poverty and unemployment traps.

POSITIVE

(i) IFS show most families gaining from Budget.

(ii) Most also better off since 1978-79.

DEFENSIVE

(i) Rich have done best? Main factor in comparison with 1978-79 is cuts in top marginal rates of income tax in 1979. Necessary to restore incentives.

(ii) Rich do best out of Budget? Not what IFS say. Family on £50,000 a year see real income rise by 1.3% as a result of Budget. Man on £7,000 gains 1.7%. Even unemployed man gains 1.2%.

(iii) Income in unemployment 15% lower than in 1978-79? IFS figures cover only those with sufficient resources not to need supplementary benefit (SB). Affected by taxation of unemployment benefit and abolition of earnings-related supplement. Necessary to improve incentive to work. For those dependent on SB, value of "safety net" maintained in real terms.

(iv) Pensioners lose from Budget? Real value of pension will be maintained. IFS figures reflect fact that they have picked a couple who smoke cigarettes. Do not reflect average position.

(v) Budget has not done much for traps? Did not claim big impact. Raised thresholds as part of long-term process of easing traps and getting thresholds back to sensible levels. No overnight solutions.

(vi) Better to raise child benefit? If I may say so, effect of IFS prescription does not sound dramatic either. Only 75,000 families would see ratio of out-of-work to in-work income fall below 90%. No effect at all on childless people.

Winners and losers – how you have fared

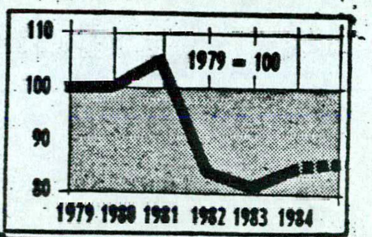
JOBLESS MAN WITH FAMILY

Former local authority manual worker, unemployed now for three months. Wife does not work; one child. Council house rent and rates £20.50 per week. Spending exceeds net income (currently £76.15) by £10 a week. Savings running out fast.

Dramatic fall in real spending power of short-term unemployed results from abolition in 1982 of earnings related supplements and taxing of unemployment benefit. Gains from increased allowances in the budget, but cigarettes cost him extra 60p.

GAIN UNDER THIS BUDGET: 88p (1.2%) LOSS UNDER TORIES: £13.44 (15%)

Weekly amounts

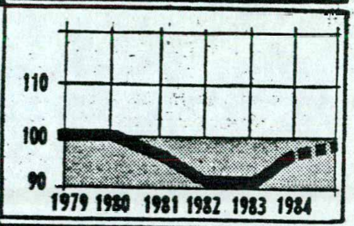


SEMI-SKILLED WORKER

He earns £138 a week. Wife does not work; one young child. Council house rent and rates £20 a week. A large part of their spending is on food and fuel. They drink and smoke moderately. They have no car but bus fares to work are high.

A rewarding year for this family, because wages have risen faster than inflation. They gain a little from the budget – the increase in real income tax allowances outweighing real rises in the cost of beer and cigarettes. Still a little worse off than in 1979.

GAIN UNDER THIS BUDGET: 78p (0.7%) LOSS UNDER TORIES £2.14 (2.0%)

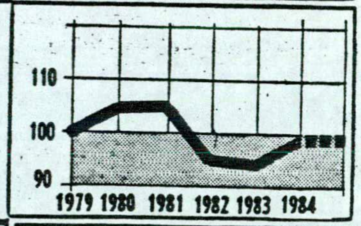


COUNCIL MANUAL WORKER

Unskilled, earning £94 a week, plus £10 in "black economy". Two children; non-working wife. Rent and rates £14.50 a week. Drink and smoke heavily. No car. Could claim family income supplement, rent and rate rebates, but do not.

The Clegg awards of 1980 raised their income but the squeeze on public sector wages, combined with rises in rents and high national insurance hit them hard. Gained from higher tax allowances in last two budgets. Nearly back to 1979.

GAIN UNDER THIS BUDGET: 49p (0.5%) LOSS UNDER TORIES: 97p (1.0%)

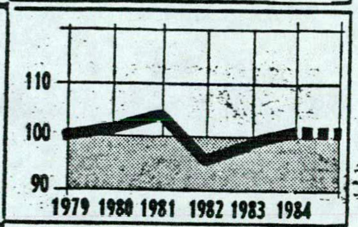


COUPLE ON A PENSION

They live in a council house and depend mainly on the state pension of £54.50 a week. Their main expenditure (apart from rent of £9 and rates of £4.75) is on food and fuel, although they both smoke and drink.

Kept up with inflation for two years under Howe but rent rises and a real cut in pension in 1981 took their real net income to below 1979 level. Change in uprating formula, and big increases in cigarette tax means loss this year.

LOSS UNDER THIS BUDGET: 25p (0.4%) GAIN UNDER TORIES: 39p (0.6%)

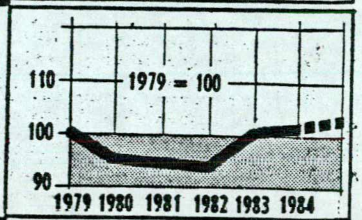


SKILLED MANUAL WORKER

He earns £198 a week. Two children and nonworking wife. Buying house. Mortgage repayments £34 a week. Rates £7.50, repairs etc. £9.50 Housing accounts for one-third of spending; food and fuel 22%. Have car. Drink, smoke moderately.

Now rather better off than in 1979. Hit by 1981 budget and national insurance increases but wage rises above inflation since then, and higher real tax allowances, have helped to restore his position. Will gain further when mortgage interest cut.

GAIN UNDER THIS BUDGET: £1.09 (0.7%) GAIN UNDER TORIES: £4.76 (3.1%)

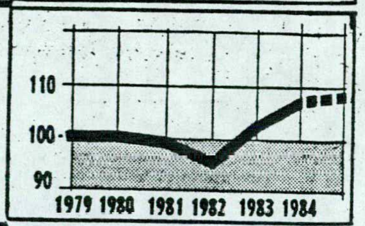


MIDDLE MANAGER

Cushioned from high mortgage rates at first by generous pay rises but 1981 budget pushed them into higher tax bands. Have done well this year as a result of a higher-than-inflation wage rise. Now out of higher rate tax.

He earns £16,900 a year. She earns £48 per week. Two teenage children. Mortgage (£28 a week) well on way to being repaid. They have two cars (one provided by the company). Both drink and smoke moderately.

GAIN UNDER THIS BUDGET: £2.94 (1.1%) GAIN UNDER TORIES: £20.73 (7.5%)

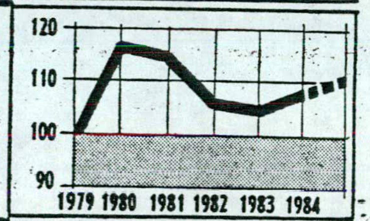


YOUNG CIVIL SERVANT

He is a clerical officer working in London. His current salary, including London weighting is £6,950 a year. Lives in privately rented accommodation. Drinks but does not smoke. Runs a car. Food, fuel and housing are 47% of his spending

In the early Howe years very high pay rises (results of comparability studies) kept his real spending power up. Later low wage rises made hime worse off. Helped this time by allowance and cut in duty on wine.

GAIN UNDER THIS BUDGET: £1.60 (1.7%) GAIN UNDER TORIES: £8.54 (10%)

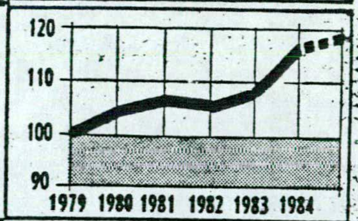


SENIOR MANAGER

He earns £23,300 a year; wife earns £78.27 a week. One car (provided by company). Both their children have left home. They drink and smoke moderately. They have paid off their mortgage and now save £31 per week.

Pay rises well above inflation for first two years under Howe, plus cuts in higher rate income tax in 1979, kept their real spending power rising. Only bad year was 1981 because of non-indexation of tax allowances and thresholds.

GAIN UNDER THIS BUDGET: £3.35 (1.1%) GAIN UNDER TORIES £56.55 (19.0%)

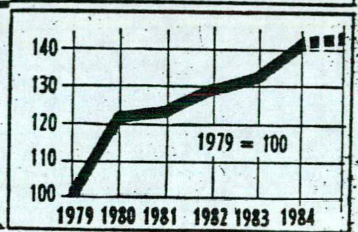


COMPANY DIRECTOR

He earns £48,600 a year, supplemented by investment income of around £1,200 a year. Salary rose 9% this year. They own their house outright; drink but do not smoke; run two cars (one of which is provided by his company):

The 1979 budget, which cut higher rates of tax, reduced his tax bill enormously, from 49% of gross income in March 1979 to 41% in March 1980. Since then, his income has risen slightly faster than their cost of living. Gains from non-indexation of wine and spirits.

GAIN UNDER THIS BUDGET: £6.84 (1.3%) GAIN UNDER TORIES: £158.32 (43%)



• Figures show what typical families gain compared with what they would have gained if taxes and duties had simply increased in line with inflation. Information prepared for the Sunday Times by the Institute for Fiscal Studies

Better-off do better

NEARLY everyone is better-off following Nigel Lawson's first budget, but some are more better-off than others.

The highest-paid company director on around £50,000 a year has an extra £6.84 a week purchasing power as a result of the budget; the jobless family man just 88p. Since the Conservatives took office in 1979, the gap is wider still – £158.32 a week more for the top director but £13.44 less for the jobless.

This finding emerges from the 1984 version of the annual budget study of household income, commissioned from the Institute for Fiscal Studies by The Sunday Times. For these studies the institute uses its computer model of the exact pattern of household earning spending and taxes to chart how typical British households are faring.

The unique virtue of the model is that it enables the IFS to calculate the impact of the budget on typical families, and to set this against the background changes of their purchasing power over several years. It is much more sophisticated than the conventional tax tables, published in the newspapers after the budget, because it takes account of the impact on different types of family, of changes in direct taxes in indirect taxes, such as beer duty; of the effect of such factors as different wage and salary increases, and of changes of rents and mortgages. The figures must not be pushed too far, however: every individuals family's circumstances are different, so no actual family's gains and losses will be identical to those in our table.

The highlight of this year's study, prepared by the institute's Andrew Dilnot, are:

- Nearly everyone is now at least as well-off as when the Conservatives took office in 1979. The unemployed are the exception. They have lost heavily, mainly as a result of the 1982 decision to tax unemployment benefits.
- For those in work tax cuts in Sir Geoffrey Howe's final 1983 budget, and wage increases running ahead of inflation have provided the main boost to incomes. Lawson's budget has given most people a more modest leg-up.
- The government is determinedly testing its theory that better rewards for the relatively well-off will improve economic performance. All the better off families studied by the IFS have done better than the average – the richest of all spectacularly so.
- Pensioners have more or less held their ground since 1979, after a big improvement in their relative living standards between 1974 and 1979.

Friday's cut in mortgage rates will further raise living standards for those groups buying their own homes. A family with a £15,000 mortgage, – like the skilled manual worker in our table – benefits by £3.00 a week for 1% off the rate.

Our typical families do not include the fortunate few on very large investment incomes who benefit from the abolition of the investment income surcharge. A family with an investment income of £20,000 a year would gain £37.21 a week from the change.

Lawson's budget put raising tax allowances first because, he said, "low tax thresholds worsen the poverty and unemployment traps, so that there is little if any financial incentive to find a better job, or even none at all." But separate IFS calculations show that the raising of the thresholds will have little impact.

They measure the incentive effect by calculating the marginal rate of tax – that is to say, what proportion of each extra pound earned goes to the taxman. The impact of the budget turns out to be small: the average person's marginal tax rate will fall by only 0.3 percentage points, from 39.3% to 39.0%.

What of the "unemployment trap", the incentive not to work at all? Before the budget, 2.9% of the working population were hardly better off for working. These people – 580,000 in all – have an income while on the dole equal to 90% or more of what they would earn in work. The budget changes hardly alter their number.

Could Lawson have done better? Yes, says the IFS, by raising the child benefit. Child benefit is payable to all who qualify – workers and the jobless. It is tax-free, so it does not blunt the work incentive. If Lawson had put his £940m into raising the benefit by £1.50, 75,000 fewer families would get as much as 90% of their work income when on the dole. In other words one in seven of those at present in this unemployment trap would have been freed.

David Lipsey

GUARDIAN 19.3.84 Page 9.

As the rich get richer, the numbers living in poverty soar

Michael Meacher

THE number of people in poverty in Britain in 1983 passed the 7½ million mark. On March 16, 1984 the FT industrial ordinary index hit an all-time high of 894.7. The two events were not unrelated. A similar conjunction occurred, though at a lower level, in the property and fringe banking boom of 1973.

Two years ago, on January 5, 1982, the FT industrial ordinary index stood at 518.1, thus implying an average 73 per cent rise in the wealth of equity holders during the past two years. At the other end of the spectrum there were 1.8 million pensioners, and about 5.4 million below pension age, including dependants, living on meanstested supplementary benefit (the semi-official State poverty line), over seven months ago. The total figure now is almost certainly over 7½ million. In May 1979, the equivalent figure was 4.4 million. The increase in less than five years in the numbers living in poverty has therefore been no less than 72 per cent, a figure unprecedental since 1929.

Another factor pushes this total even higher. For 7½ million excludes those living *below* the supplementary benefit level but not claiming benefit — either out of pride, ignorance of their entitlement, or for whatever other reason. In 1981, the last occasion when an attempt was made officially to estimate the number of these, it was found that there were about 810,000 pensioners in this category, plus 100,000 sick and disabled people, 400,000 unemployed and 50,000 one-parent families — 1.39 million in all. Thus the best estimate that can be made of the total number of people living in poverty in Britain today is about 8½-9 million — one in six of the whole population.

Apart from these extremes of wealth and poverty, what have been the changes in the living standards of the nation as a whole?? Here movements in the index of real personal disposable income are acknowledged to be the best indicator. What this reveals is a fall from a level of 116.9 (where the 1975 real personal disposable income level equals 100) in the fourth quarter of 1979 to 111.5 in the third quarter of 1983, a fall of 4.7 per cent.

There is, however, a good deal of variation round this average. First, whilst overall the standard of living of the 86 per cent of the workforce still in work has risen slightly on average, the standard of living of the unemployed has dropped much more dramatically (and this does not refer to the obvious loss of income from being made redundant, but to the level of benefit available to the unemployed today as opposed to four years ago).

As a result of the cut in the real value of unemployment benefit in 1981, and the total abolition in 1982 of the earnings-related supplement to unemployment benefit, a married man unemployed now receives, not a third of national average earnings as he used to, but less than a quarter.

Secondly, amongst those who are still in work, there has been a sharp polarisation since 1979. The poorest families at half average earnings (which were about £167 a week gross in April 1982), despite big wage increases in 1979-80, are slightly worse off because of low wage settlements combined with large council rent rises and large national insurance contribution increases. The family on average earnings did slightly better, despite the steep rise in mortgage interest, because wage increases in the last two years held up better. On the other hand, the family at one and a half average earnings (£230 gross a week) has ended slightly worse off because recent pay increases at this level have not been so high.

At the higher income levels, however, the changes have been dramatic. At three times average earnings (nearly £25,000 a year) managers and professionals have not only had bigger than average pay rises (on the evidence of a retail survey of big UK companies) but also very generous tax concessions. They are left, therefore, 11 per cent better off in real terms than in 1979.

At the top income level (chairman, chief executive, higher professional) of five times average earnings, or £40,000 a year, the same factors writ even larger—bigger annual pay increases plus enormous tax handouts in the 1979 budget (worth an extra £4,000 a year at top executive levels)—have combined to produce a huge gain in living standards. They are now some 22 per cent better off in real terms than in 1979 (according to the Institute of Fiscal Studies' calculations).

Another way of illustrating the changes in spending power as between different sections of the population is to examine not short-term adjustments of the tax burden, but long-run shifts in income distribution since before the last war. These are set out in the table. The trend revealed is a very significant one. It shows that the richest 10 per cent had a 3½ times bigger income share of the nation's resources in 1938-9, but this had declined over the next 40 years to slightly over twice. However in Mrs Thatchers first year this trend was reversed and the richest 10 per cent *increased* their share, back to the proportion they took 20 years ago. Conversely, the middle 60 per cent of the population steadily increased their income share throughout this 40 year period, but this trend was reversed for the first time in 1979-80. The poorest 30 per cent of the population, who have never had more than about half the income share that their numbers might have suggested, have suffered a steady gradual decline over the last 30 years, but it accelerated markedly in the single year 1979-80.

It would, of course, be helpful to extend this analysis further to the next three years. But a political decision has recently been taken to discontinue all work on estimates of the distribution of wealth (for a saving of only £14,000 a year) and to carry out estimates of distribution of income only every three years instead of every year as previously. As a result the next analysis, for 1981-2, is still not ready for publication.

A third relevant factor concerns the changes in the distribution of wealth. Inland Revenue data shows that in 1980 (the latest evidence) the richest 1 per cent of the adult UK population owned 23 per cent of total marketable wealth, which amounted to £566,000 million. The richest 10 per cent owned 58 per cent of all marketable wealth, whilst the poorest 50 per cent owned only 6 per cent. This means that the average person among the richest 1 per cent in the country held about £315,000 in private wealth (an average figure which conceals enormous variations ranging up to more than £100 million in some individual cases) whilst the poorest half of the population held on average only about £1,600 each.

It is difficult to assess with any certainty how wealth-holdings have changes over time. According to Inland Revenue data, in 1974 the richest 1 per cent held exactly the same share of total wealth as in 1980, and the poorest half of the population held marginally more in 1974 than in 1980, so if anything there has been a slight recent *increase* in inequalities.

The present Stock Exchange boom is sharply expanding the wealth of some of the richest people in the country. But it is a roller-coaster form of wealth generator. Over the last 20 years as a whole the FT-Actuaries 500 share index has actually fallen 28 per cent in real value. Yet over this period the rich have substantially reduced their holdings in equities and transferred their wealth more and more into property.

Wealth-holders have been very generously treated by the Exchequer. Whilst income tax, which increasingly bears heavily on the lowest paid, has steadily increased its take as a proportion of all Government revenue, capital taxes — capital gains tax, estate duty and capital transfer tax—have been considerably reduced, from 6 per cent of all Government taxes in 1070-1 to only 2 per cent now (compared to a colossal 72 per cent from income tax). The process of under-taxing wealth relative to income was taken even further in the 1982 budget which reduced the take from CGT and CTT by an amount the Inland Revenue estimates at £195 million in a year, equal to a fifth of the total take of all capital taxation.

The conclusion is not just that poverty is now on the increase, but that the former long-term trend towards greater equality has now been set in reverse.

Michael Meacher is Labour MP for Oldham West and Shadow spokesman for Health and Social Security.

BUDGET DEBATE, 19 MARCH

<u>Personal Tax: A Budget for the Rich</u>?

I would like now to deal with the charge - raised by several of the Opposition benches and others - that this is a Budget for the rich. This charge, or charges, for it is aimed at several different aspects of the Budget, is wholly misconceived where it is not ill-informed.

2. First, it ignores the substantial reductions in income tax being proposed. Available resources are being concentrated - for the third year running - on raising the real value of the basic allowances for single people and married men. These will be over 7 per cent high in real terns than last year, and ~~25~~ 16 per cent higher than in ~~1981-82.~~ 1978-79. 80 per cent of the total cost of income tax reductions ~~- some £1¾ billion in 1984-85 -~~ in a full year goes on raising personal allowances. Raising allowances gives maximum help to the low-paid. In this respect it is much preferable to reducing the basic rate, where the benefits are spread across taxpayers in proportion to their taxable income. Because the basic personal allowances are to be increased by 12½ per cent, but the higher rate thresholds by only 5-6 per cent, ~~they will add 2.3 per cent to the net income of a married man at half average earnings but only 1.2 per cent - only half as much - at twice average earnings.~~

, but will reduce the income tax bill of a married man at half average earnings by 2.3 per cent of his total income; but the reduction at twice average earnings will be 1.2 per cent - only half as much.

3. Mr Hattersley claimed inthe House (14 March) that the increase in the thresholds provides much less help [£10~~6~~8 in 1984-85] to a couple who earn £5,000 a year than to one earning £50,000 a year [£600]. He had clearly

read as far as Table 2 in the Treasury press release on "Income Tax". It is a pity he did not read further. Table 9A shows that - after allowing for a 6½ per cent increase in earnings - the percentage of income paid in income tax and NIC for a couple on £~~3~~4,000 a year falls by 1~~½~~¼ percentage points in 1984-85 but that for a couple on £50,000 a year it falls by only one-tenth of 1 percentage point.

4. The increase in the basic allowances are a significant contribution to our long-term goal of restoring thresholds to sensible levels. Twenty years ago the married man's allowance stood at 45 per cent of average earnings. By the time we took office it was down to 31 per cent. The changes I propose in this Budget, together with those in my rt hon Friend the Foreign Secretary's last Budget, make a start on reversing the downward trend. A twenty-year decline cannot be reversed overnight. Next year the married man's allowance will still only be 33 per cent of average earnings. But we have made a start. Further increases in allowances will be a priority as resources permit.

5. It is true that the age allowances are to be increased by less than the basic personal allowances. But their real value is being maintained, as is that of the retirement pension. It was right to concentrate the bulk of the resources available on raising the basic thresholds. All agree that the latter are too low. Some people on very low incomes pay tax. And the tax threshold is lower for people of working age. It must be remembered that the age allowances are still substantially higher than the main allowances - £800 in the case of a married couple and £485 for a single person.

6. There have been suggestions that a better way of easing the poverty and unemployment traps would have been to devote the resources used on raising tax allowances to increasing child benefit. Let us be clear of what the proponents of this course are suggesting. The problem of the poverty trap is that those caught in it face very high marginal rates, sometimes in excess of 100 per cent. If their gross income increases they pay more tax and national insurance and have their-means tested benefits reduced, so that they can actually end up worse off in net terms.

7. One way to tackle this problem is to replace means-tested benefits by universal benefits, such as child benefit. This would reduce marginal rates. But against that it would leave the net income of the poorest families unchanged. They would gain from higher child benefit but lose from reduced means-tested benefits. This is the only way that higher child benefit can help the poverty trap. By contrast, raising tax allowances - as we are proposing - both reduces marginal rates and increases net income for the poorest families in the trap. 10,000 fewer families will receive FIS while at the same time paying income tax - a 6 per cent drop in the number so affected. Moreover, increasing allowances by more than indexation will take 400,000 people of working age out of tax. Their marginal rate drops by 30 per centage points. And net income in-work is expected to rise faster than income out-of-work for most people. So the incentive to take a job - the unemployment trap - is improved.

8. There is another underlying assumption of the child benefit route that I would challenge. This is that we are only concerned with the incentives - whether it be the poverty trap or the unemployment trap - of those with children. In fact I am at least as concerned to give young single people an incentive to take jobs at reasonable wages, or to improve their skills to get better jobs, as I am concerned about married men with children. Here again tax allowances have the edge. They are good for the incentives of the childless as well as those with children.

9. Now let me turn briefly to indirect taxes. Increases were needed here to contribute to the financing of the income tax reductions. But - with the exception of tobacco where there are strong health reasons for a real increase - excise duties on average have merely been raised in line with inflation. The extension of the VAT base is, of course, a real increase. But it is not expected to hit particularly hard at low-income groups. For example, the biggest item is the extension to building alterations which will affect only owner-occupiers.

10. Taking account of indirect tax increases, the Budget is estimated to give a net gain in real terms to a family on average earnings. On the Government Actuary's assumption about earnings growth, and the FSBR forecast for prices, I expect real take-home pay to be significantly higher in 1984-85 compared with 1983-84. [The largest percentage gains will be for the low-paid, assuming their earnings rise in line with the average.]

[Defensive point if pressed: Over 70% of IIS payers are either over 65 or otherwise pay tax at only the basic rate, or both.]

11. Next, I might mention the number of ways in which the otherwise "better-off" lose directly from this Budget. One is the measures we are proposing to withdraw the tax reliefs on the foreign earnings of UK residents working or trading abroad. This relief was introduced in 1974 at a time of absurdly high marginal rates. It is no longer justified. UK top and average tax rates are no longer out of line with our competitors. The reliefs are also excessively complex and much abused - at the expense of employers, tax revenue and the balance of payments. Secondly, we are taking a further, considered step towards

taxing car benefits on a realistic basic - a 10 per cent increase is proposed for 1985-86. Thirdly, there is the withdrawal of LAPR on new policies, a change which will remove an important distortion to savings decisions and which, over a period of years, will yield substantial revenue savings for use elsewhere.

12. Finally, in case my inadvertent references to "married men" instead of "married couples" leaves me open to the charge of sexism, I would like to make a new announcement. The House will recall that in 1980 we published a Green Paper on the taxation of husband and wife. This was designed to encourage and inform public debate on whether, and if so how, the present tax system should be adapted to reflect the social and economic changes over recent years. Many people and organisations gave their views and these were very valuable. But the questions raised in the paper were so complex and wide-ranging that, not surprisingly, no clear concensus emerged about the direction of any change. However,the debate cannot stop there. I hope to publish later this year a further paper which will set out the Government's present thinking and help forward public discussion and understanding of the issues involved.

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Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

19 March 1984

The Editor
Hansard
House of Commons
London SW1

Dear Sir,

... I attach a copy of the Official Report No 118 Volume 56 with some corrections indicated on the text as printed of the Budget Speech. You will find these in columns 286, 287, 289, 290, 291, 294, 295, 297, 302, 303 and 304.

Of those that are not simply corrections of typographical errors, the one that is absolutely essential is the insertion of the new heading "Business Taxation" in column 295, although the Chancellor does, of course, attach importance to all of them.

Yours faithfully,
Judith Simpson

Miss J C Simpson
Private Secretary

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[Mr. Speaker]

1. Consolidated Fund Act 1984.
2. Restrictive Trade Practices (Stock Exchange) Act 1984.
3. Occupiers' Liability Act 1984.
4. Tourism (Overseas Promotion) (Scotland) Act 1984.
5. Merchant Shipping Act 1984.
6. Education (Amendment) (Scotland) Act 1984.
7. Pensions Commutation Act 1984.
8. Orkney Islands Council Order Confirmation Act 1984.
9. Western Isles Islands Council (Kallin Pier, Harbour Jurisdiction) Order Confirmation Act 1984.
10. Ullapool Harbour Order Confirmation Act 1984.

WAYS AND MEANS

Budget Statement

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

3.40 pm

INTRODUCTION

The Chancellor of the Exchequer (Mr. Nigel Lawson): This Budget will set the Government's course for this Parliament.

There will be no letting up in our determination to defeat inflation. We shall continue the policies that we have followed consistently since 1979. These policies provide the only way to achieve our ultimate objective of stable prices. To abandon them would be to risk renewed inflation, and much higher unemployment. As a result of our determined efforts, inflation is at its lowest level since the 1960s. Economic recovery is well under way and employment is growing.

These achievements are a tribute to the courage and foresight of the five Budgets presented by my distinguished predecessor, whose duties unfortunately keep him in Brussels today.

I shall do nothing today to compromise those successes. But there is much that I can do to build upon them.

My Budget today has two themes—first, the further reduction~~s~~ of inflation; and, second, a series of tax reforms designed to enable the economy to work better, reforms to stimulate enterprise and set British business on the road to profitable expansion, reforms that will help to bring new jobs.

I shall begin by reviewing the economic background to the Budget. I shall then deal with the medium term financial strategy; with monetary policy and the monetary targets for next year; and with public borrowing and the appropriate PSBR for the coming year. I shall then turn to public expenditure, including the prospects for the longer term. Finally, I shall deal with taxation, and the changes in the structure of taxation which will pave the way for cuts in taxes in subsequent years. For this will be a tax reform Budget.

As usual, a number of press releases, filling out the details of my tax proposals, will be available from the Vote Office as soon as I have sat down.

THE ECONOMIC BACKGROUND

I start with the economic background.

Since 1980, inflation has fallen steadily from a peak of over 20 per cent. For last year as a whole it was down to about 4½ per cent., the lowest figure since the 1960s. And with lower inflation have come lower interest rates.

This in turn has led to an economic recovery whose underlying strength is now beyond dispute. Whereas in some previous cycles recovery has come from a self-defeating stimulus to monetary demand, this time it has sprung from sound finance and honest money. Lower inflation and lower interest rates benefit industry, business, and consumer confidence alike. 1/C

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Across the economy, total money incomes grew in 1983 by about 8 per cent., of which 3 per cent. represented real growth in output. Although there is still room for improvement, this is a very much healthier division between inflation and real growth than the nation experienced in the 1970s. Output in the second half of 1983 is now reckoned to have exceeded the previous peak, before the world recession set in, and is still rising strongly.

Productivity, too, has continued to improve rapidly. Just as over the past year many have wrongly predicted an end to the recovery, so some have tried to dismiss the sharp rise in productivity as a flash in the pan. Yet in 1983 manufacturing productivity grew by 6 per cent. for the second year in succession. Unit labour costs across the whole economy are likely to show the smallest annual increase since the 1960s. This has allowed a welcome and necessary recovery in real levels of profitability.

Higher profits lead to more jobs. The number of people in work increased by about 80,000 between March and September last year. The loss of jobs in manufacturing has slowed down sharply, while jobs in services increased by getting on for 200,000 in the first nine months of last year.

But further progress is needed. Although our unit wage costs in manufacturing rose by under 3 per cent. last year, our three biggest competitors, the United States, Japan and Germany, did better. The employment prospect would be significantly improved if a bigger contribution to improved cost performance were to come from lower pay rises.

Demand, output, profits and employment all rose last year. Home demand has played the major part in the recovery so far. Lower inflation reduced people's need to save, and real incomes rose. Personal consumption increased by over 3½ per cent. compared with 1982. Fixed investment rose rather faster than consumption, with investment in housing and services particularly strong.

Our rate of economic growth last year was the highest in the European Community. For much of 1983 our export performance was affected by weak demand in many of our overseas markets, while imports rose slightly faster than home demand. But by the end of last year world trade was clearly moving ahead again, and in the three months to January manufacturing exports increased very substantially. The balance of payments on current account last year is estimated to have been in surplus by about £2 billion.

Our critics have been confounded by this combination of economic recovery and low inflation. Even the pessimists have been forced to acknowledge the durability of the recovery. It is set to continue throughout this year at an annual rate of 3 per cent. Inflation is expected to remain low, edging back down to 4½ per cent. by the end of this year. With rising incomes and low inflation, consumption will continue to grow. And, encouraged by improved profitability and better long-term growth prospects, investment is expected to rise by a good 6 per cent. this year.

Looking abroad, too, economic prospects are more favourable than they have been for some time. Output in the United States should continue to grow strongly this year, and recovery is spreading to the rest of the world.

1/c Of Course, there are inevitable risks and uncertainties. The size and continued growth of the United States budget deficit is a cause of widespread concern and keeps interest rates high, exacerbating the problems of the debtor countries. And the need to finance the United States deficit by inflows of foreign capital has kept the dollar artificially high and led to a massive and growing trade deficit, greatly increasing the pressures for protectionism within the United States.

A second potential risk is disruption in the oil market. The United Kingdom, and indeed the whole world economy, inevitably remain vulnerable to any major disturbances in this market.

But despite these risks there is a growing sense throughout the industrialised world that the recovery this time is one which can be sustained. The essential requirement is the continued pursuit of prudent monetary and fiscal policies.

THE MEDIUM-TERM FINANCIAL STRATEGY

For the United Kingdom, the medium-term financial strategy has been the cornerstone of such policies. It will continue to play that role—to provide a framework and discipline for Government and to set out clearly, to industry and the financial markets, the guidelines of policy. Too often in the past Governments have abandoned financial discipline whenever the going got rough, and staggered from one short-term policy expedient to another. The temptation to accommodate inflationary pressure proved irresistible, and the nation's longer-term economic performance was progressively undermined.

The medium-term financial strategy was designed to remedy this, by imposing a disciplined financial framework which would also ensure consistency between monetary and fiscal policies, and a proper balance in the economy. It is so designed to ensure that the more inflation and inflationary expectations come down, the more room is available for output and employment to grow.

People now know that the Government intend to stick to their medium-term objectives. They understand that the faster inflation comes down, the faster output and employment are likely to recover. The increasing degree of realism and flexibility in the economy owes much to the pursuit of firm and consistent policies within the MTFS framework.

Originally the MTFS covered four years. In this first Budget of a new Parliament it is appropriate to carry it forward for five years. So the MTFS published today in the Financial Statement and Budget Report — the Red Book — shows a continuing downward path for the monetary target ranges over the next five years, and a path for public borrowing consistent with that reduction. It takes full account of important influences such as the pattern of North sea oil revenues, and the level of asset sales arising from the privatisation programme.

For the two final years of the new MTFS, which lie beyond the period covered in last year's public expenditure survey and last month's White Paper, the Government have not yet made firm plans for public spending. But the MTFS assumption—and at present it is no more than an assumption — is that the level of public spending in 1987-88 and 1988-89 will be the same in real terms as that currently planned for 1986-87.

The precise figures set out in the MTFS are not of course a rigid framework, lacking all flexibility. As in the past, there may need to be adjustments to take account of changing circumstances. But no changes will be made that might jeopardise the consistent pursuit of the Government's objectives.

MONETARY POLICY

Monetary policy will continue to play a central role. Further reductions in monetary growth are needed to achieve still lower inflation.

Over the 12 months to mid-February the growth of sterling M3 as been well within the 7 to 11 per cent. target range, with M1 at the top of the range and PSL2 a little above it. While in the early months of the target period most measures of money showed signs of accelerating, since the summer growth in all the target aggregates has been comfortably within the range. And nominal interest rates have continued to decline in line with falling inflation.

has

Other evidence confirms that monetary conditions are satisfactory. The effective exchange rate has remained fairly stable, despite the international uncertainties which I have described.

If monetary policy is to stay on track, its practical implementation must adapt to changes in the financial system and in the significance of different measures of money. There is of course nothing new in this. Over the years we have more than once altered the target ranges and aggregates to take account of such changes. But the thrust of the strategy has been maintained.

One important development has been the decision to give a more explicit role to the narrow measures of money. Sterling M3 and the other broad aggregates give a good indication of the growth of liquidity. But a large proportion of this money is in reality a form of savings, invested for the interest it can earn. In defining policy it is therefore helpful also to make specific reference to measures of money which relate more narrowly to balances held for current spending.

It was for this reason that M1 was introduced as a target aggregate, but it has not proved entirely satisfactory for that purpose. With the rapid growth of interest-bearing sight deposits, M1 has become an increasingly poor measure of money held to finance current spending. The signs are that this will continue.

Other measures of narrow money have not been distorted to the same extent. In particular, MO, which consists mainly of currency, is likely to be a better indicator of financial conditions than M1. There is also the new aggregate M2, which was specifically devised to provide a comprehensive measure of transactions balances. This may also be a useful guide but, being new, still needs to be interpreted with particular care.

In the past two years, it has been possible to set a single target range for both broad and narrow measures of money. But this will not normally be the case; for narrow monetary aggregates tend in the long run to grow more slowly than broader measures. Thus, this year's Red Book sets out two separate—though overlapping—ranges.

The target range for broad money will continue to apply to sterling M3, and for the coming year will be set at 6 to 10 per cent., as indicated in last year's MTFS. The target range for narrow money will apply to MO and for next year will be set at 4 to 8 per cent. *[Interruption.]* Opposition Members ought to sit quiet. They have a lot to learn.

To avoid any possible misunderstanding, let me stress that the use of MO as a target aggregate will not involve any change in methods of monetary control.

The two target aggregates will have equal importance in the conduct of policy. And the authorities will continue to take into account other measures of money, especially M2 and PSL2, which include building society liabilities, as well as wider evidence of financial conditions, including the exchange rate. As in the past, monetary conditions will be kept under control by an appropriate combination of funding and operations in the money market.

So far as funding is concerned, the public sector's borrowing requirement, as I shall shortly explain, will be significantly lower in the coming year. In financing it, the role of national savings will remain important. This year's national savings target of £3 billion is likely to be 1/2 achieved: the target for the coming year will again be £3 1/2 billion.

Precise monetary targets for the later years will be decided nearer the time. But to give a broad indication of the objectives of monetary policy, the new MTFS, like previous versions, shows monetary ranges for a number of years ahead. These ranges are consistent with a continuing downward trend in inflation: they demonstrate the Government's intention to make further progress towards stable prices.

PUBLIC SECTOR BORROWING

I turn now to public borrowing. Just as the classical formula for financial discipline—the gold standard and the balanced budget—had both a monetary and a fiscal component, so too does the medium-term financial strategy.

The MTFS has always envisaged that the public sector borrowing requirement would fall as a percentage of gross domestic product over the medium term. By 1981-82 we had brought it down to 3·5 per cent. of GDP.

Since then, however, there has been little further fall. The latest estimate of the PSBR for the current year, 1983-84, remains what it was in November; around £10 billion, equivalent to 3·25 per cent. of GDP. This is significantly above what was intended at the time of last year's Budget, and would have been higher still had it not been for the July measures.

We now need a further substantial reduction in borrowing in order to help bring interest rates down further as monetary growth slows down. Sterling interest rates are, of course, also influenced by dollar interest rates; but that makes it all the more important to curb domestic pressures. In contrast to virtually the whole of the post-war period, United Kingdom three-month and long-term rates are now lower than American rates. As long as American rates remain near their current level, it is highly desirable that this advantage be maintained.

The higher level of asset sales we are planning as the privatisation programme gathers pace is a further reason for reducing the PSBR significantly in the coming year. Asset sales reduce the Government's need to borrow. But their effect on interest rates may be less than the effect of most other reductions in Government spending programmes. 2½

Last year's MTFS showed an illustrative PSBR for 1984-85 of 2·5 per cent. of GDP, equivalent to around £8 billion. But I believe that it is possible, and indeed prudent, to aim for a somewhat lower figure, I am therefore providing for a PSBR next year of 2·25 per cent. of GDP, or £7·25 billion. £7¼ 2¼

The House will recall that in November I warned that on conventional assumptions, including the 1983 Red Book's PSBR figure of £8 billion for next year, I might have to increase taxes slightly in the Budget. I am glad to report that the latest, and more buoyant, forecasts of tax revenue in the coming year have improved the picture. A PSBR of £7·25 billion will require no overall net increase in taxation. £7¼

Moreover, while the measures I shall shortly announce will, after indexation, be broadly neutral in their effects on revenue in 1984-85, they will reduce taxation in 1985-86 by well over £1·75 billion. And the MTFS published today shows that there should be room for further tax cuts not only in 1985-86, but throughout the remainder of this Parliament, provided that we stick firmly to our published plans for public expenditure to 1986-87, and maintain an equally firm control of public spending thereafter. £1¾

PUBLIC EXPENDITURE

The public expenditure White Paper setting out our spending plans for the next three years was approved by the House last week. Today I want to consider the important issue of Government spending in a rather wider perspective.

For far too long, public spending has grown faster than the economy as a whole. As a result, the tax burden has steadily increased and income tax has extended steadily lower down the income scale.

We have seen a massive enlargement in the role of the state, at the expense of the individual, and a corresponding increase in the dead weight of taxation holding back our economic progress as a nation.

This process has to stop. But it has arisen because much public spending is directed to eminently desirable ends. This raises difficult issues which deserve the widest possible consideration and debate.

The Government are therefore publishing today, in addition to the customary Budget documents, a Green Paper on the prospects for public spending and taxation over the next 10 years. It examines past trends; discusses the pressures for still higher spending; and examines the rewards for the individual and the benefits for the economy if these pressures can be contained.

The Green paper concludes that, without firm control over public spending, there can be no prospect of bringing the burden of tax back to more reasonable levels. On the assumptions made in the Green Paper, the burden of taxation will be reduced to the levels of the early 1970s only if public expenditure is kept broadly stable in real terms over the next 10 years.

The Government believe that the issues discussed in the Green Paper merit the attention of the House and the country.

In contrast to previous years, I have no package of public expenditure measures to announce in this Budget. The White Paper plans stand.

I can, however, make one announcement, which I think the House will welcome. Within the published plans the Government have been able to provide the National Heritage Memorial Fund with additional resources which will enable it among other things to secure the future of Calke Abbey. My right hon. Friend the Secretary of State for the Environment will be announcing the details later today.

The House will recall that proposals for the new rates of social security benefit to come into force in November are not now made at the time of the Budget. Following last year's legislation to return to the historic method of uprating, price protection is measured by reference to the retail price index for May. My right hon. Friend the Secretary of State for Social Services will be announcing the new rates of social security benefits, including child benefit, when the May RPI is known.

Before leaving Government spending, I should add a word on public sector manpower. At the beginning of the last Parliament, the Government set themselves the target of reducing the size of the Civil Service from 732,000 in April 1979 to 630,000 by April of this year. That target will be achieved. We have now set ourselves the further target of 593,000 by April 1988. I am confident that a smaller Civil Service will continue to improve its efficiency. The tax changes that I shall be announcing today will reduce manpower requirements by at least 1,000 in my own Departments, which will help towards meeting the 1988 target.

TAX REFORM

I indicated at the outset that this will be a radical, tax-reforming Budget. It will also significantly reduce the overall burden of tax over the next two years taken together. And I hope to have scope for further reductions in future Budgets.

My proposals for reform are guided by two basic principles: first, the need to make changes that will improve our economic performance over the longer term; second, the desire to make life a little simpler for the taxpayer.

But I am well aware that the tax reformer's path is a stony one. Any change in the system is bound, at least in the short term, to bring benefits to some and disadvantages to others. And the disapproval of the latter group tends to be rather more audible than the murmurings of satisfaction from the former.

Some commentators have suggested that our entire income-based tax system should be replaced with an expenditure-based system. Even if a root-and-branch change of this kind were desirable, it would, I believe, be wholly impractical and unrealistic.

But I do not believe we can afford to opt for the quiet life and do nothing. So I have chosen the middle way: to introduce reforms, some of them far-reaching, within the framework of our existing income-based system. I shall also be proposing transitional arrangements where I believe it fair and appropriate to do so.

The changes I shall be proposing today fall into three broad categories. These are the taxation of savings and investment, business taxation, and the taxation of personal income and spending.

SAVINGS AND INVESTMENT

First, the taxation of savings and investment. The proposals I am about to make should improve the direction and quality of both. And they will contribute further to the creation of a property-owning and share-owning democracy, in which more decisions are made by individuals rather than by institutions.

I start with stamp duty. This was doubled from its long-standing 1 per cent. by the post-war Labour Government in 1947, reduced by the Conservative Government in 1963, and once again doubled to 2 per cent. by Labour in the first Budget presented by the right hon. Member for Leeds, East (Mr. Healey) in 1974. I am sorry that he is not

[Mr. Nigel Lawson]

in his place today. At its present level it is an impediment to mobility and incompatible with the forces of competition now at work in the City, following the withdrawal of the Stock Exchange case from the Restrictive Practices Court.

I therefore propose to halve the rate of stamp duty to 1 per cent. The new rate will apply straight away to Stock Exchange deals. It will also apply from today to other transactions where documents are stamped on or after 20 March.

For the home buyer, the new flat rate 1 per cent. stamp duty will start at £30,000. Below this level no duty will be payable. As a result of this £5,000 increase in the threshold, 90 per cent. of first-time home buyers will not have to pay stamp duty at all.

Reducing the rate of duty on share transfers will remove an important disincentive to investment in equities and increase the international competitiveness of our stock market. It should also help British companies to raise equity finance.

In addition, I have four proposals to encourage the issue of corporate bonds. I shall go ahead with the new arrangements for deep discount stock and the reliefs for companies issuing Eurobonds, and for convertible loan stock, which were announced but not enacted last year. And I propose to exempt from capital gains tax most corporate fixed interest securities provided they are held for more than a year. As such securities are already exempt from stamp duty, this means that the tax concessions for private sector borrowing in the corporate bond market will now be virtually the same as for Government borrowing in the gilt-edged market.

The reductions in stamp duty will cost £450 million in 1984-85, of which £160 million is the cost of the relief on share transfers, and £290 million the cost of the relief on transfers of houses and other buildings and land.

Next, life assurance. The main effect of life assurance premium relief today is unduly to favour institutional rather than direct investment. It has also spawned a multiplicity of well-advertised tax management schemes, and no fewer than 50 pages of legislation attempting to deal with its abuse. I therefore propose to withdraw the relief on all new contracts made after today. I stress that this change will apply only to new, or newly enhanced, policies, taken out after today. Existing policies will not be affected at all. The change is estimated to yield about £90 million in 1984-85.

I am also proposing to curtail the special — but unfortunately widely abused — privileges for what are known as "tax exempt" friendly societies, and bring them into line with the normal rules for friendly societies doing "mixed" business. However, the limits within which in future all friendly societies will be able to write assurance on a tax exempt basis will be increased from £500 to £750.

I have also reviewed the tax treatment of direct personal investment. The investment income surcharge is an unfair and anomalous tax on savings and on the rewards of successful enterprise. It hits the small business man who reaches retirement without the cushion of a company pension scheme, and impedes the creation of farm tenancies. In the vast majority of cases it is a tax on savings made out of hard-earned and fully-taxed income. More than half of those who pay the investment income surcharge are over 65, and of these half would otherwise by liable to tax at only the basic rate.

I have therefore decided that the investment income surcharge should be abolished. The cost in 1984-85 will by ~~be~~ some £25 million, building up to around £350 million in a full year.

Finally, I propose to draw more closely together the tax treatment of depositors in banks and building societies. These institutions compete in the same market for personal deposits. I believe that they should be able to do so on more equal terms as far as tax is concerned. One source of unequal treatment has already been removed, with the recent change made on legal advice in the tax treatment of building societies' profits from gilt-edged securities. They are now treated in the same way as those of the banks have always been.

But the major source of unequal treatment, against which the banks in particular have frquently complained, is the special arrangement for interest paid by building societies. The societies pay tax at a special rate — the "composite rate" — on the interest paid to the depositor, who receives credit for income tax at the full basic rate.

This system, which has worked well for the past 90 years, has both an advantage and a disadvantage. The disadvantage is that a minority of depositors, who are below the income tax threshold, still pay tax at the composite rate. It has not, however, stopped many of them from using building societies because of the competitive rates these ~~they~~ have offered. The advantage of the scheme is its extreme simplicity, particularly for the taxpayer; most taxpayers are spared the bother of paying tax on interest through PAYE or individual assessment, while the Revenue is spared the need to recruit up to 2,000 extra staff to collect the tax due on interest paid without deduction.

In common with my predecessors of all parties over the past 90 years, I am satisfied that the advantage of the composite rate arrangement outweighs the disadvantage. It follows that equal treatment of building societies and banks should be achieved, not by removing the composite rate from the societies, but by extending it to the banks and other licensed deposit takers.

Non-taxpayers will still continue to be able to receive interest gross, should they wish to do so, by putting their money into appropriate national savings facilities. But the purpose of the move is not, of course, to attract savings into Government hands: as I have already announced, next year's target for national savings will be the same as this year's and last year's; and the total Government appetite for savings, which is measured by the size of the public sector borrowing requirement, is being significantly reduced.

The true purpose of the move is simple: fairer competition and simplicity itself. The great majority of individual bank customers will, when it comes to tax, be able to forget about bank interest altogether, for all the tax due on it will already have been paid. And it will be easier for people to compare the terms offered for their savings by banks and building societies.

The purpose of the change is not to raise additional revenue. The composite rate arrangement is designed to collect no more tax than would be due at the basic rate from all depositors under existing arrangements.

However, the Inland Revenue will be able to make staff savings of up to 1,000 civil servants. Moreover, this figure takes no account of the substantial numbers of additional Inland Revenue staff who would have been required to operate the present system as the trend towards the payment of interest on current accounts develops.

Accordingly, I propose to extend the composite rate arrangements to interest received by United Kingdom resident individuals from banks and other licensed deposit takers with effect from 1985-86. The composite rate will not apply either to non-residents or to the corporate sector. Arrangements will also be made to exclude from the scheme certificates of deposit and time deposits of £50,000 or more.

Taken together, the major proposals I have just announced on stamp duty, life assurance premium relief, the investment income surcharge, and the composite rate, coupled with other minor proposals, will provide a simpler and more straightforward tax system for savings and investment. They will remove biases which have discouraged the individual saver from investing directly in industry. They will reinforce the Government's policy of encouraging competition in the financial sector, as in the economy as a whole. And they are part of a package of measures designed to enable interest rates to fall, and reduce the cost of borrowing.

BUSINESS TAXATION (new heading)

I now turn to business taxation. Here the Government have two responsibilities towards British business and industry. The first is to ensure that they do not have to bear an excessive burden of taxation. The second is to ensure that, given a particular burden, it is structured in the way that does least damage to the nation's economic performance.

The measures that I am announcing today will, taking the next two years together, result in a substantial reduction in the burden of taxation on British business. And, in addition, I shall be proposing a far-reaching reform of company taxation.

Responses to the corporation tax Green Paper in 1982 showed a strong general desire to retain the imputation system. I accept that. But other changes are needed.

The current rates of corporation tax are far too high, penalising profit and success, and blunting the cutting edge of enterprise. They are the product of too many special reliefs, indiscriminately applied and of diminishing relevance to the conditions of today. Some of these reliefs reflect economic priorities or circumstances which have long vanished, and now serve only to distort both investment decisions and ~~distort~~ choices about finance. Others were introduced to meet short-term pressures, notably the upward surge of inflation.

With inflation down to today's low levels, this is clearly the time to take a fresh look. And with unemployment as high as it is today, it is particularly difficult to justify a tax system which encourages low-yielding or even loss-making investment at the expense of jobs.

My purpose, therefore, is to phase out some unnecessary reliefs in order to bring about, over time, a markedly lower rate of tax on company profits.

First, capital allowances. Over virtually the whole of the post-war period there have been incentives for investment in both plant and machinery and industrial, although not commercial, buildings. But there is little evidence that these incentives have strengthened the economy or improve the quality of investment. Indeed, quite the contrary: the evidence suggests that businesses have invested substantially in assets yielding a lower rate of return than the investments made by our principal competitors. Too much of British investment has been made because the tax allowances make it look profitable, rather than because it would be truly productive. We need investment decisions based on future market assessments, not future tax assessments.

I propose to restructure the capital allowances in three annual stages. In the case of plant and machinery, and assets whose allowances are linked with them, the first year allowance will be reduced from 100 per cent. to 75 per cent. for all such expenditure incurred after today, and to 50 per cent. for expenditure incurred after 31 March next year. After 31 March 1986 there will be no first year allowances, and all expenditure on plant and machinery will qualify for annual allowances on a 25 per cent. reducing balance basis.

In addition, from next year annual allowances will be given as soon as the expenditure is incurred, and not, as they are today, when the asset comes into use. This will bring forward the entitlement to annual allowances for those assets, such as ships and oil rigs, for which some payment is normally made well before they are brought into use.

For industrial buildings, I propose that the initial allowance should fall from 75 per cent. to 50 per cent. from tonight, and be further reduced to 25 per cent. from 31 March next year. After 31 March 1986 the initial allowance will be abolished, and expenditure will be written off on an annual 4 per cent. straight line basis.

When these changes have all taken place, tax allowances for both plant and machinery and industrial buildings will still on average be rather more generous than would be provided by a strict system of commercial depreciation.

The changes in the rates of allowances will not apply to payments under binding contracts entered into before midnight tonight, provided that the expenditure is incurred within the next three years.

There will be transitional tax arrangements for certain investment projects in the development areas and special development areas. When a project in those areas has had an offer of Industry Act selective financial assistance and also attracts regional development grants, the existing capital allowances will continue to apply to the expenditure to which the selective assistance is related. These arrangements will cover projects for which offers have already been made between 1 April 1980 and today. Similar arrangements for regional development grants were, of course, announced by my right hon. Friend the Secretary of State for Trade and Industry in his White Paper last December.

Over the same period to 31 March 1986 most other capital allowances will be brought into line with the main changes which I have announced. The Inland Revenue will be issuing a press notice tonight giving full details of these proposals.

Next, stock relief. As the House will recall, this was introduced by the last Labour Government as a form of emergency help to businesses facing the ravages of high inflation. Those days are past; and the relief is no longer necessary. Company liquidity has improved and, above all, inflation has fallen sharply. Accordingly, I propose not to allow stock relief for increases in prices after this month.

The changes that I have just announced, in capital allowances and stock relief, enable me to embark on a major programme of progressive reductions in the main

[Mr. Nigel Lawson]

rate of corporation tax. For profits earned in the year just ending, on which tax is generally payable in 1984-85, the rate will be cut from 52 per cent. to 50 per cent. For profits earned in 1984-85 the rate will be further cut to 45 per cent. Looking further ahead, to profits earned in 1985-86, the rate will go down to 40 per cent.; and for profits earned in 1986-87 the main rate of corporation tax will be 35 per cent.—no fewer than 17 percentage points below the current rate.

All these rates for the years ahead will be included in this year's Finance Bill; and when these changes are complete, our rates of capital allowances in this country for the generality of plant and machinery will be comparable with those in most other countries, while the rate of tax on profits will be significantly lower.

The substantial reduction in the rate of corporation tax will bring a further benefit. Our imputation system allows a company to offset in full all interest paid. But only a partial offset for dividends is allowed. Companies thus have a clear incentive to finance themselves through borrowing and in particular bank borrowing rather than by raising equity capital. The closer the corporation tax rate comes to the basic rate of income tax, the smaller this undesirable distortion becomes.

Of course, the majority of companies are not liable to pay the main rate of corporation tax at all. For them it is the small companies' rate, at present 38 per cent., which applies. I propose to reduce this rate forthwith to 30 per cent. for profits earned in 1983-84 and thereafter. A tax regime for small companies which is already generous by international standards will thus become markedly more generous.

The corporation tax measures I have just announced will ~~be~~ cost £280 million in 1984-85. In 1985-86 the cost will £450 million—made up of £1,100 million by way of reductions in the rates, only partially offset by a £650 million reduction in the value of the reliefs. During the transitional period as a whole, these measures should have a broadly neutral effect on the financial position of companies. But when the changes have fully worked through companies will enjoy very substantial reductions in the tax that they pay.

Business and industry can go ahead confidently on the basis of the corporation tax rates I have announced today, which set the framework of company taxation for the rest of this Parliament.

Over the next two years, these changes will cause some investment to be brought forward, to take advantage of high first year capital allowances—a prospect made all the more alluring for business since the profits earned will be taxed at the new, lower rates. But the more important and lasting effect will be to encourage the search for investment projects with a genuinely worthwhile return, and to discourage uneconomic investment.

It is doubtful whether it has ever been really sensible to subsidise capital investment irrespective of the true rate of return. But certainly, with over 3 million unemployed, it cannot make sense to subsidise capital so heavily at the expense of labour.

These changes hold out an exciting opportunity for British industry as a whole: an opportunity further to improve its profitability, and to expand, building on the recovery that is already well under way. Higher profits after tax will encourage and reward enterprise, stimulate innovation in all its forms, and create more jobs.

I now turn to some more detailed measures affecting business.

The business expansion scheme, introduced last year as a successor to the business start up scheme, has been widely welcomed as a highly imaginative scheme for encouraging individuals to invest in small companies. It is already proving a considerable success. It now needs time to settle down, and I have only one change to propose this year.

The scheme was designed to offer generous incentives for investment in new or expanding companies in high risk areas. The ownership of farmland cannot be said to fall within this category, and I therefore propose that from tomorrow farming should cease to be rated as a qualifying trade under the scheme.

Next, in keeping with what I have said about removing complexity and distortions, I propose to abolish two reliefs in the personal tax field which were introduced at a time when this country suffered from excessively high rates of income tax. As we have reduced those rates, the reliefs are no longer justified.

The first is the 50 per cent. tax relief—falling after nine years to 25 per cent.—applied to the emoluments of foreign-domiciled employees working here for foreign employers. These employees are often paying much less tax here than they would either in their own country or in most other European countries. At present income tax rates, the need for this relief has clearly disappeared. Moreover, it is open to widespread abuses. It is, for example, possible for someone whose parents came here from abroad, and who has himself lived here all his life, to enjoy this relief, if he works for a foreign company. That cannot be right.

I therefore propose to withdraw the relief for all new cases from today. For existing beneficiaries, the 25 per cent. relief will cease on 6 April, and the 50 per cent. relief will be phased out over the next five years.

I also propose to withdraw the foreign earnings relief for United Kingdom residents who work at least 30 days abroad in a tax year. This relief, too, harks back to the days of penally high income tax rates. It, too, has been exploited, in particular by those who prolong their overseas visits purely in order to gain a tax advantage. I propose to withdraw the matching relief for the self-employed who spend 30 days abroad, and for those resident in the United Kingdom who have separate employments or separate trades carried on wholly abroad. The relief will be halved to 12½ per cent. in 1984-85 and removed entirely from 6 April 1985.

However, I am not making any change to the 100 per cent. deduction given for absences abroad of 365 days or more. In addition, I have authorised consultations by the Inland Revenue about a possible relaxation in the rules governing the taxation of expenses reimbursed to employees for travel overseas.

The abolition of these reliefs will eventually yield revenue savings of over £150 million, and represents another useful step in the removal of complexity and distortions in the tax system.

I need to set the car benefit scales for 1985-86 for those provided with the use of a car by their employer. Despite the increases over recent years, the levels still fall short of any realistic measure of the true benefit. I am proposing an increase of 10 per cent. in both the car and car fuel scales with effect from April 1985.

Unnecessarily high rates of tax discourage enterprise and risk taking. This is true of the capital taxes, just as it is of the corporation and income taxes. It is a matter of particular concern to those involved in running unquoted family businesses. The highest rates of capital transfer tax are far too high and badly out of line with comparable rates abroad. I propose therefore, in addition to statutory indexation, to reduce the highest rate of capital transfer tax from 75 per cent. to 60 per cent. For lifetime gifts I propose to simplify the scale so that the rate is always one half of that on death.

For capital gains tax I will, as promised, bring forward in the Finance Bill proposals to double the limit for retirement relief to a figure of £100,000, backdated to April 1983. A consultative document on other possible changes in this relief is being issued next week. I am proposing no other changes this year in capital gains tax beyond the statutory indexation of the exempt amount from £5,300 to £5,600. However, the tax continues to attract criticism—not least for its complexity—and that is a matter to which I hope to return next year.

We have done much to improve the development land tax. Early in the last Parliament, my predecessor increased the threshold from £10,000 to £50,000. I now propose a further increase to £75,000, which will reduce the number of cases liable to the tax by more than one third.

Next, share options. The measures introduced in the last Parliament to improve employee involvement through profit-sharing and savings-related share options schemes have been a notable success. The number of these schemes open to all employees has increased from about 30 in 1979 to over 670 now, benefiting some half a million employees. To maintain and build on this progress I propose to increase the monthly limit on contributions to savings-related share option schemes from £50 to £100. I have also authorised the Inland Revenue to double the tax-free limits under the concession on long service awards, and to include within these limits the gift of shares in the employee's company.

But beyond this, I am convinced that we need to do more to attract top calibre company management and to increase the incentives and motivation of existing executives and key personnel by linking their rewards to performance. I propose therefore that, subject to certain necessary limits and conditions, share options generally be taken out of income tax altogether, leaving any gain to be charged to capital gains tax on ultimate disposal of the shares. The new rules will apply to options meeting the necessary conditions which are granted from 6 April.

I am sure that all these changes will be welcomed as measures to encourage the commitment of employees to the success of their companies and to improve the performance, competitiveness and profitability of British industry.

As the House knows, the Government are deeply concerned at the threat which the spread of unitary taxation in certain United States states has posed to the United States subsidiaries of British firms. With our European partners we are monitoring the situation closely, and await with keen interest the imminent report of United States Treasury Secretary Regan's working group. It is essential that a satisfactory solution is found and speedily implemented.

United States firms operating in this country are not, of course, taxed on a unitary basis.

I now turn to oil taxation. Last year's North sea tax changes were well received, and there has been a substantial increase in the number of development projects coming forward, and a new surge in exploration. Work on no fewer than 128 offshore exploration and appraisal wells started last year—an all-time record.

The Government are already committed to a study of the economics of investment in incremental development in existing fields. This is of increasing importance, and in consultation with my right hon. Friend the Secretary of State for Energy I therefore propose to review this area with the industry, and to legislate as appropriate next year to improve the position. To prevent projects being deferred pending this review, any changes will apply to all projects which receive development consent after today.

Meanwhile, I am taking two measures to prevent an unjustified loss of tax from the North sea. First, in addition to the PRT measures on farmouts which I announced last September, I am limiting the potential corporation tax cost of such deals. Second, I propose to repeal the provision which allows advance corporation tax to be repaid where corporation tax is reduced by PRT. I have also reviewed the case for extending last year's future field concessions to the southern basin, but have concluded that an additional incentive here is not needed.

I have just two further changes affecting business to propose, both of which will come into force on 1 October.

Ever since VAT was introduced in this country, we have treated imports differently from the way our main European Community competitors treat them. While they require VAT on imported goods to be paid in the same way as customs duties, we do not. Under our system an importer does not have to account for VAT on his imports until he makes his normal VAT return, on average some 11 weeks later. During this time the importer enjoys free credit at the taxpayer's expense. But when one British business man buys from another, he gets no such help from the taxpayer: he pays his VAT when he pays his supplier.

The European Commission has for some years now been seeking, with our full support, to get a system like ours adopted throughout the Community. But the plain fact is that in all that time the Commission has made no progress whatever.

I must tell the House that I am not prepared to put British industry at a competitive disadvantage in the home market any longer. Should our European partners at any time undergo a Damascene conversion, and agree that the Commission's proposal should be accepted after all, then of course we would revert to the present system. But in the meantime I propose to move to the system used by our European competitors. We shall provide the same facilities for payment of VAT on imports as apply to Customs duties. That means that most importers will be able to defer payment of VAT by, on average, one month from the date of importation. But that is all.

As I have said, this change will apply from 1 October. By bringing forward VAT receipts, it will bring in an extra £1·2 billion in 1984-85, some of which will be borne by foreign producers and manufacturers. There will of course be no increased revenue in subsequent years.

The second change I propose to make on 1 October concerns the national insurance surcharge. This tax on jobs was introduced by the Labour Government in 1977 at the rate of 2 per cent., and further increased by the right hon.

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[*Mr. Nigel Lawson*]

Member for Leeds, East in 1978 to 3½ per cent. During the last Parliament, this Government reduced it to 1 per cent., and we are pledged to abolish it during the lifetime of this Parliament.

Given the impact that this tax has, not only on industrial costs but also—at a time of high unemployment—on jobs, I have decided to take the opportunity of this my first Budget to fulfil that pledge. Abolition of the national insurance surcharge from October will reduce private sector employers' costs by almost £350 million in 1984-85, and over £850 million in a full year. It will thus be of continuing help to British industry. As before, the benefit will be confined to the private sector.

The house will I am sure agree that a Budget which substantially reduces the Government's demands on financial markets, which abolishes the national insurance surcharge, and which cuts the rates and simplifies the structure of corporation tax is a Budget for jobs and for enterprise. It offers British industry an opportunity which I am confident it will seize.

PERSONAL TAXATION: TAXES ON SPENDING

Having announced major reforms of both the taxation of savings and investment and the taxation of business, I turn now to third and final area in which I propose to make progress on tax reform. This is the taxation of personal income and spending.

The broad principle was clearly set out in the manifesto on which we were first elected in 1979. This emphasised the need for a switch from taxes on earnings to taxes on spending. My predecessor made an important move in this direction in his first Budget, and the time has come to make a further move today. To reduce direct taxation by this means is important in two ways. It improves incentives and makes it more worthwhile to work, and it increases the freedom of choice of the individual.

Having regard to the representations I have received on health grounds, I therefore propose an increase in the tobacco duty which, including VAT, will put 10p on the price of a packet of cigarettes, with corresponding increases for hand-rolling tobacco and cigars. This will do no more than restore the tax on tobacco to its 1965 level in real terms. These changes will take effect from midnight on Thursday. I do not, however, propose any increase in the duty on pipe tobacco.

I propose to raise most of the other excise duties broadly in line with inflation, so as to maintain their real value: not to do so would run counter to the philosophy I outlined a moment ago. But with inflation as low at it now is, the necessary increases are on the whole mercifully modest.

I propose to increase the duties on petrol and derv by amounts which, including VAT, will raise the price at the pumps by 4½p and 3½p a gallon respectively. This does no more than keep pace with inflation. The changes will take effect for oil delivered from refineries and warehouses from 6 o'clock this evening. I do not propose to increase the duty on heavy fuel oil, which is of particular importance to industrial costs.

There is one excise duty which I propose to do away with altogether. Many of those who find it hardest to make ends meet, including in particular many pensioners, use paraffin stoves to heat their homes. It is with them in mind that I propose to abolish the duty on kerosene from 6 o'clock tonight. I am sure that this will be welcomed on all sides of the House.

The various rates of vehicle excise duty will, once again, go up roughly in line with prices. Thus, the duty for cars and light vans will be increased by £5, from £85 to £90 a year. However, in the light of the reassessment by my right hon. Friend the Secretary of State for Transport of the wear and tear that various types of vehicle cause to the roads, there will be reductions in duty for the lightest lorries, offset by higher increases for some heavier lorries. All these changes in vehicle excise duty will take effect from tomorrow.

However, I propose to exempt from vehicle excise duty all recipients of the war pensioners' mobility supplement. In addition, the existing VAT relief for motor vehicles designed or adapted for use by the handicapped will be extended, and matched by a new car tax relief. The effect will be that neither VAT nor car tax will apply to family cars designed for disabled people or substantially adapted for their use.

I now come to the most difficult decision I have had to take in the excise duty field. As the House will be aware, the rules of the European Community, so far as alcoholic drinks are concerned, are designed to prevent a member state from protecting its own domestic product by imposing a significantly higher duty on competing imports. In pursuit of this, the Commission has taken a number of countries to the European Court of Justice.

In our case, the Commission contended that we were protecting beer by under-taxing it in relation to wine. We fought the case, but we lost; and I am now implementing the judgment handed down by the court last year. Accordingly, I propose to increase the duty on beer by the minimum amount needed to comply with the judgment and
4c maintain revenue: 2~~p~~ on a typical pint of beer, including VAT. At the same time, the duty on table wine will be reduced by the equivalent of about 18p a bottle, again including VAT.

We have thus complied with the court's judgment, and I am happy to be able to tell the House that the Italian Government have, after discussions, given us an undertaking that they will comply with earlier court rulings on discrimination against Scotch whisky.

As for the rest of the alcoholic drinks, cider, which increasingly competes with beer but attracts a lower duty, will go up by 3p a pint. The duties on made-wine will be aligned with those on other wine, and I propose to increase the duty on sparkling wine, fortified wine and spirits by about 10p a bottle, including VAT. All these changes will take effect from midnight tonight.

These changes in excise duties will, all told, bring in some £840 million in 1984-85, some £200 million more than is required to keep pace with inflation. The addition is, of course, due to the increase in tobacco duty.

The remainder of the extra revenue I need to enable me to make a substantial switch this year from taxes on earnings to taxes on spending must come from VAT. I propose no change in the rate of VAT. Instead, I intend to broaden the base of the tax by extending the 15 per cent. rate to two areas of expenditure that have hitherto been zero rated.

First, alterations to buildings. At present repairs and maintenance are taxed, but alterations are not. The borderline between these two categories is the most confused in the whole field of VAT. I propose to end this confusion and illogicality by bringing all alterations into tax.

I recognise that this will be unwelcome news for the construction industry, but construction will of course benefit very greatly from the reduction in the rate of stamp duty which I have already announced: £290 million of the cost of that reduction in 1984-85 relates to transfers of land and buildings, and of that £290 million over 90 per cent. relates to buildings and building land. Nevertheless, to allow a reasonable time for existing commitments to be completed or adjusted the VAT change will be deferred until 1 June.

Secondly, food. Most food is zero rated, but food served in restaurants is taxed, together with a miscellaneous range of items including ice cream, confectionery, soft drinks and crisps, which were brought into tax by the right hon. Member for Leeds, East. Take-away food clearly competes with other forms of catering, and I therefore intend to bring into tax hot take-away food and drinks, with effect from 1 May.

The total effect of the extensions of the VAT coverage which I have proposed will be to increase the yield of the tax by £375 million in 1984-85 and by £650 million in a full year.

The total impact effect on the retail price index of the VAT changes and excise duty changes taken together will be less than three quarters of 1 per cent. This has already been taken into account in the forecast which I have given to the House of a decline in inflation to 4·5 per cent. by the end of the year. 4½

The extra revenue raised in this way will enable me, within the overall framework of a neutral Budget, to lighten the burden of income tax.

PERSONAL TAXATION: INCOME TAX

Since we took office in 1979, we have cut the basic rate of income tax from 33 per cent. to 30 per cent. and sharply reduced the confiscatory higher rates inherited from the last Labour Government. We have increased the main tax allowances not simply in line with prices but by around 8 per cent. in real terms. It is a good record, but it is not enough. The burden of income tax is still too heavy.

During the lifetime of this Parliament, I intend to carry forward the progress we have already made. For the most part, this will have to wait for future Budgets, particularly since I have thought it right this year to concentrate on setting a new regime of business taxation for the lifetime of a Parliament—and beyond. But as a result of the changes to taxes on spending which I have just announced, I can take a further step in this Budget.

I propose to make no change this year in the rates of income tax. So far as the allowances and thresholds are concerned, I must clearly increase these by the amounts set out in the statutory indexation formula, based on the 5·3 per cent. increase in the retail price index to December. The question is how much more I can do, and how to direct it.

I have decided that, this year, the right course is to use every penny I have in hand, within the ~~framework of the~~ framework of a revenue neutral Budget, to lift the level of the basic tax thresholds, for the married and single alike. It makes very little sense to be collecting income tax from people who are at the same time receiving means-tested benefits. Moreover, low tax thresholds worsen the poverty and unemployment traps, so that there is little if any financial incentive to find a better job or even any job at all. There is, alas, no quick or cheap solution to these problems. But that is all the more reason to make a further move towards solving them now.

I propose to increase the other thresholds in line with the statutory indexation requirement, but by no more. The first higher rate of 40 per cent. will apply when taxable income reaches £15,400 a year and the top rate of 60 per cent. to taxable income over £38,100. The single age allowance will rise from £2,360 to £2,490 and the married age allowance from £3,755 to £3,955.

For the basic thresholds, statutory indexation would mean putting the single and married allowances up by £100 and £150 respectively. I am glad to say that I can do considerably better than that. I propose to increase the basic thresholds by well over double what is required by indexation. The single persons's allowance will be increased by £220, from £1,785 to £2,005; and the married man's allowance by £360 from £2,795 to £3,155.

This is an increase of around 12·5 per cent., or some 7 per cent. in real terms. It brings the married man's tax allowance for 1984-85 to its highest level in real terms since the war. It means that the great majority of married couples will enjoy an income tax cut of at least £2 a week, and it means that a large number of people, those with the smallest incomes of all, are taken out of income tax altogether. Some 850,000 people — over 100,000 of them widows—who would have paid tax if thresholds had not been increased will pay no tax in 1984-85. That is 400,000 more taken out of tax than if the allowances had merely been indexed.

All these changes will take effect under PAYE on the first pay day after 10 May. Their cost is considerable—some £1·8 billion in 1984-85, of which roughly half represents the cost of indexation.

This is as far as I can go on income tax this year, within a broadly revenue-neutral Budget for 1984-85. But so long as we hold to our published planned levels of public spending, there is an excellent prospect of further cuts in income tax in next year's Budget. These would be on top of the measures I have announced in this Budget which, as I have already told the House, will reduce taxation in 1985-86 by well over ~~£1·75~~ billion, with business taking the lion's share. £1¾

CONCLUSION

I have, Mr. Deputy Speaker, completed the course I charted at the outset this afternoon. I have described the recovery, and how the Government plan to sustain it, and assist the creation of new jobs. I have reaffirmed our commitment to further reductions in inflation, by maintaining sound money and by curbing Government borrowing. I have embarked on a radical programme of tax reform, abolishing outright two major taxes — the investment income surcharge and the national insurance surcharge—and I have been able to propose measures which will significantly reduce the burden of taxation over the next two years. I commend this Budget to the House.

Mr. Deputy Speaker: Under Standing Order No. 114, the first motion, entitled "Provisional Collection of Taxes", must be decided without debate.

CONFIDENTIAL

RMP

FROM: MISS M O'MARA
DATE: 19 March 1984

Mr Martin

cc PS/Chief Secretary
PS/Financial Secretary
PS/Minister of State
PS/Economic Secretary
Sir P Middleton
Mr Cassell
Mr Battishill
Mr Monger
Mr Salveson
Mr Ridley o.r.
Mr Lord
PS/Inland Revenue
PS/Customs & Excise
Mr Graham/Parl Counsel

BACKERS FOR THE FINANCE BILL

The Chancellor has seen your minute of 14 March. He would like to invite the Secretaries of State for Trade and Industry, Energy, Environment, and Transport and the Minister of Agriculture to be backers for the Bill, plus, as a courtesy, the Foreign and Commonwealth Secretary. I should be grateful if Mr Salveson could check with the Parliamentary Clerks in the Departments concerned whether their Ministers are content and if he could let you know the outcome.

MOM

MISS M O'MARA

CONFIDENTIAL

CONFIDENTIAL

FROM: F MARTIN
14 MARCH 1984

1. MR MØNGER 14/3

2. CHANCELLOR

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Sir P Middleton
Mr Cassell
Mr Battishill
Mr Salveson
Mr Ridley
Mr Lord

PS/Inland Revenue
PS/Customs & Excise
Mr Graham - Parliamentary Counsel

C.
I think we should ask all five, and - as a courtesy - the F+C.S.

I agree.

BACKERS FOR THE FINANCE BILL

One minor Finance Bill matter we need to decide is the names for the backers of the Bill. The Financial Secretary traditionally gives these before "walking the floor" and presenting the Bill in dummy (the Bill then being read formally for the first time and ordered to be printed) at the end of the Budget debates and the vote on the Resolutions - this year, on Monday 19 March.

2. It is traditional to include the Chairman of Ways and Means and all the Treasury Ministers in the Commons. A maximum of seven non-Treasury Ministers may also be added, particularly if they have an interest in any of the Bill's clauses. Recent Finance Bills have therefore been backed by, for example, the Secretaries of State for Industry, Trade, Energy, Transport and Environment.

3. This is primarily a matter for your personal choice. Because of the effects of the corporation tax proposals on the various industries their Departments sponsor, it might be presentationally useful to have among the backers, the Secretaries of State for Trade and Industry, Energy, Environment and Transport. The ~~Secretary of State~~ Minister for Agriculture might likewise be considered because of the effects on the agricultural sector. The Secretary of State for Trade and Industry would also "qualify" in the context of the proposals affecting life assurance, and the Secretary of State for Transport on the VED contents of the Bill. And you might also wish to

consider including the Secretary of State for Employment.

4. As a matter of courtesy, it is usual for your Private Office to check that whoever you decide to include as a backer is content with this. If your Private Office could then let me know the names, I will inform Parliamentary Counsel, who in turn lets the House authorities know.

F. Martin

F MARTIN

(pwj)

HOUSE OF COMMONS DEBATE
BUDGET DEBATE

Vol 56 No 122
Monday 19 March
(Fourth Day)

Summary of Revenue points

Col 710	Mr Norman Tebbit (SSTI)	Tax burden for poor eased by rise in thresholds
Col 711	Mr Peter Shore (La)	Swiss interest in investment in UK due to capital allowances - will vanish after 2 years.
Col 711	Mr Tebbit (SSTI)	Swiss have been recommending investment in UK for many months
Col 712		Lower corporation tax rate encourages investment by eating up less profit
		NIS abolition worth £850m per annum to private sector
Col 713		Stamp duty reduction will boost London as financial centre
Col 714		Reform of corporate tax system - incentive to effective investment and free decision-making. Elements balanced.
Col 714	Dr Keith Hampson (C)	VAT on building alterations - will it damage inner-city re-housing development by private sector?
Col 715	Mr Tebbit (SSTI)	Inevitable there will be losers and gainers. Local authorities can reclaim VAT.
Col 716		Corporate tax measures: encourage foreign investment in UK, remove distortions and discrimination against labour, and bring forward investment. Advantage of low tax rates will increase as we move out of recession.
		Changes will save 1,000 tax-gathers and 10,000 tax accountants.

		Share options change will encourage initiative.
		Budget continues help to small firms: reduction of tax rate, rise in VAT threshold, CTT reduction, IIS abolition.
		Reforms encourage research and development (100% FYAs).
Col 720	Mr Peter Shore (La)	Corporation tax measures will cost £450m in 1985-6, £1 3/4bn in 1986-7.
		North Sea oil tax at peak - up to £10bn under this Government. Set to fall to £9bn.
Col 724		Abolition of capital allowances will hit high-technology industries, encourage investment overseas. Allowances don't encourage investment at expense of employment. Both manufacturing and service industries will suffer.
Col 725		VAT on building alterations hits construction. How will local authorities be compensated?
Col 726	Mr Edward Heath (C)	4 - year commitment on corporation tax dangerous.
Col 727		Welcome NIS abolition but doubted would lead to increase in jobs.
		VAT on building alterations hits construction - won't be offset by corporation tax and stamp duty changes.
		VAT at ports misunderstood in Europe.
Col 728		Composite rate for banks moves manpower burden onto banks, discourages payment of wages by cheque.
		VAT on takeaways creates further anomalies.

		IIS abolition welcome but real problem is wealth distribution.
		Criticised removal of 25% reduction for travellers overseas. Little abuse. Will push up seamen's wages.
Col 729		Mr Tebbit implied that capital allowances measure will encourage unproductive investment in next 2 years. Wrong - allowances have been well used, and imitated abroad.
Col 730		Government inconsistent - giving cash incentives but arguing against fiscal interference.
		Personal tax - child allowance increase preferable to single or married person's allowance.
Col 731		Should have tax credit system.
Col 732		Chancellor has counted on oil price rise - may no happen.
Col 736	Mr J Enoch Powell (OUP)	"We tax in order to redistribute income according to a pattern which we in the House decide".
Col 736	Sir William Clark (C)	Welcomed:
		- rise in thresholds above inflation
		- capital allowances change - must foster labour-intensive industry.
		Withdrawal of life assurance relief - should have had earlier notice. Glad pensions, endowments etc not affected.
Col 739		Welcomed:
		- IIS abolition

		- <u>share options</u> change
		- <u>development land tax</u> alleviation. Could have been abolished - a time-waster which should have been incorporated in <u>CGT</u>
		- <u>stamp duty</u> reduction, but more could be done.
		- <u>People working overseas</u> - mustn't make regime too penal.
		Chancellor should consider increasing <u>allowances for service industry</u>.
		<u>NIS</u> abolition welcome.
		<u>Advance announcement of corporation tax measures</u> gives certainty.
Col 740		4th protocol to <u>double taxation convention</u> - should abolish <u>unitary tax</u>. Dividends already paid by UK firms to Americans. <u>Petroleum revenue tax</u> paid here by Amercians can be set against USA tax.
		<u>Taxation of gilt dealing by building societies</u> - element of retrospection - should be rethought.
		<u>Cigarette taxation</u> - diminishing returns in future?
		<u>Composite rate</u> shouldn't cause problems for wage-earners receiving cheques. Will produce another windfall next year but not enough to make up for £1.2bn from <u>VAT on imports</u> - latter a welcome measure but one-off.
Col 741	<u>Mr Richard Wainwright</u> (Lib)	Fewer <u>cigarette</u> sales would be welcome.
Col 742		<u>IIS</u> abolition goes too far.

Col 743		Capital allowances abolition too drastic - doesn't encourage free choice. Phase-out encourages investment for tax reasons. Income tax allowances rise - child benefit must be considered alongside this.
Col 744	Mr Jeff Rooker (La)	Conservatives in opposition promised to take child benefit into account in reducing taxes.
Col 745	Mr Wainwright (Lib)	Income tax change-figures inadequate.
Col 746	Mr Edward du Cann (C)	Welcomed "modest tax increases", NIS abolition. Relief for savers and investors: welcomed IIS, CGT, CTT, shares option, and stamp duty measures. Stamp duty should be abolished.
Col 747		Regretted abolition of life assurance relief - won't encourage direct investment - this a bad principle anyway. Owner-occupied housing, pension funds and savings have also been privileged.
Col 748		Welcomed corporation tax measures and spread of VAT - move towards expenditure-based tax system. Much still to do. Income tax system also too complex. Should amalgamate with benefits system. Welcomed Green Paper "The Next 10 Years".
Col 751	Mr Robert Sheldon (La)	VAT on imports windfall is key to Budget. Other advance payments to be considered? What about duty deferments for spirits and tobacco?

		VAT on takeaways creates anomalies.
		Tax simplification: "the enemy of fairness".
Col 752		Mortgage relief "irrational". With abolition of Schedule A tax and CGT exemption, too much in this area.
		Tax reform must contribute to prosperity. Oil wealth will decline.
		Admitted capital allowances have been used for wrong investment, but labour can't replace capital.
Col 755 Col 756	Dr Keith Hampson (CO	VAT on building alternation hits construction, extends black economy, depreciates quality of housing stock. Repercussions for improvement grants, inner city development, Housing Corporation cash limits.
Col 758	Dr M S Miller (La)	Tax on tobacco so lucrative that Government not serious about discouraging smoking.
Col 759		IIS abolition and corporation tax reduction wrong priority - not neutral.
		VAT on takeaways hits poor.
		Abolition of relief for time abroad hits seamen.
Col 760	Mr Peter Fry (C)	Welcomed change in VAT on imports
		Abolition of life assurance relief runs counter to other Government policy - discourages saving for old age. Abuse could be stopped by restricting relief to basic rates or limit amount of relief (cf mortgage relief).

Col 761	Mr Peter Shore (La)	Implications for mortgage and pension contributions relief?
Col 761	Mr Fry (C)	Should be made clear these won't be touched.
Col 762		VAT on building alterations discourages energy conservation. Cut-off date too sudden - should postpone for 3 months.
Col 763	Mr A E P Duffy (La)	Capital allowances measure does nothing for industrial renewal. 4 - year plan doesn't allow for world trade movements. Business and financial communities profit most from personal and corporate tax cuts.
Col 764	Mr Ralph Howell (C)	Welcomed: - IIS abolition - switch from direct to indirect taxation
Col 765		- personal tax changes - but questioned Chancellor's statement re married man's allowance - not enough. Budget doesn't do enough for "poverty trap".
Col 767	Mr Brian Sedgemoor (La)	Budget gives incentives to rich and dead: Chancellor "using necrophilia as a weapon in our economic salvation".
Col 770	Mr Conal Gregory (C)	Rise in threshold for mortgage relief and stamp duty reduction helps house-buyers. NIS and corporation tax measures will boost employment. Capital allowances - same rates should apply to hotels.

Col 771		VAT on building alterations encourages black economy. Commencement date should be changed.
		Abolition of life assurance relief will discourage savings, though offset by mortgage rate reduction. Not enough consultation.
Col 772	Mr Dick Douglas (La)	Life assurance measure hasty.
Col 774		Corporation tax changes - not properly backed by figures. Attack on investment.
		Government cushioned by oil revenue.
Col 775	Mr Nigel Forman (C)	Welcomed rise in personal allowances, NIS abolition, corporation tax reform, stamp duty reduction, tobacco duty increase.
Col 776		Hoped for real increase in child benefit, further tax reform to remove most or all allowances and move closer to US system.
Col 777		Declining oil revenues will increase British vulnerability.
Col 778	Mr Francis Maude (C)	Welcomed corporation tax and life assurance measures - remove distortions. Should reduce mortgage relief - could then reduce overall tax burden.
Col 779		Should have abolished development land tax, CGT and CTT.
		New growth from service industries.
Col 780		Welcomed NIS abolition.
Col 780	Mr Ivor Stanbrook (C)	Welcomed shift from income to spending.

		VAT on building alterations causes hardship.
Col 781	Mr Jeff Rooker (La)	Tax burden higher under Conservatives. Budget a simplistic adjustment.
		Commitment to keep child benefit in line with tax allowances.
Col 782		IIS abolition unfair.
		Tax-free age allowance for over 65's not up enough.
		Abolition of Life insurance relief not in manifesto - but used to scare voters off Labour.
Col 783		Demanded figures for effect of Budget changes.
		No evidence NIS abolition will boost employment.
Col 784		CBI say Budget "too savage" on manufacturing. Tax burden on industry going up - Red Book shows expected increase in corporation tax revenue.
Col 785		Budget won't end tax avoidance industry.
Col 786		Tax burden will remain higher than under Labour (quoted Green Paper).
		National Insurance contributions are also a tax - they will have to rise.
Col 788		Manifesto promised not to put VAT on necessities Labour will oppose VAT changes.
		More figures needed on corporate taxation.
Col 788	Mr Nigel Lawson (Ch Ex)	Personal allowances highest since war; percentage of income taken lower. In progressive

tax system increase in allowances bound to be of greater benefit higher up scale. Help concentrated on poor this year.

Budget helps all taxpayers, not just those with children. Child benefit already highest ever.

Col 791	If plans adhered to, should be scope for tax cuts bringing overall burden back to early 1970s level.
Col 793	Tax credit system would cost over £10bn.
	Phasing out of capital allowances will be more than offset by cuts in corporation tax rate. Allowances will still be more generous than strict commercial depreciation, and comparable with other countries, especially for small businesses.
Col 794	Tax incentives not needed for investment - cf commercial buildings. No evidence that subsidies beneficial. Measures will improve quality of investment. Principle favoured by Labour's "Programme" of June 1982.
	Budget a strategy for lower and simpler taxation.

Question put and agreed to

Float

EMBASSY OF THE
UNITED STATES OF AMERICA

CH/EXCHEQUER

REC.	20 MAR 1984 20/3
ACTION	MR NORGROVE.
COPIES TO	CST. EST.
	Sir P. Middleton
	Mr Littler.
	Mr Unwin.

Mr Lavelle.
Mr Bottrill.

24 Grosvenor Square
London W1A 1AE
March 20, 1984

PWP

Dear Chancellor:

Don Regan has asked me to convey to you the enclosed congratulatory letter. I shall be receiving the signed original later this week, which I shall forward.

Sincerely yours,

Jerry M. Newman

Jerry M. Newman
U.S. Treasury Representative

Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
H M Treasury
Parliament Street
London SW1P 3AG

Enclosure

THE SECRETARY OF THE TREASURY
WASHINGTON

March 20, 1984

Dear Nigel:

Please accept my sincere congratulations on your new budget. It is clear that you have undertaken a major new effort on tax reform which should have profound effects on the outlook for the U.K. economy.

At budget time, I wish we had a parliamentary system. I am envious of the speed and ease with which you will be able to get Parliament to approve your budget.

I look forward to seeing you during the Interim Committee meetings.

With best wishes.

Sincerely,

Donald T. Regan

Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
H M Treasury
Parliament Street
London SW1P 3AG

P

FROM: MISS M O'MARA
DATE: 20 March 1984

APS/Economic Secretary

cc PS/Chief Secretary
PS/Financial Secretary
PS/Minister of State
Sir P Middleton
Mr Battishill
Mr Lankester
Mr Allen
Mr Pirie
Mr Ilett
Mr Ridley
PS/Inland Revenue
Mr Corlett/IR

BUDGET PRESENTATION: CONTACTS AFTER THE BUDGET

The Chancellor has seen your minute of 19 March and agrees with Mr Mitchener that the Government is likely to get some criticism from the shipping and shipbuilding industries. He has commented that he assumes we have our defences well prepared.

MOM

MISS M O'MARA

19

FROM: MISS M O'MARA
DATE: 20 March 1984

PS/Economic Secretary

PS/Chief Secretary
PS/Financial Secretary
PS/Minister of State
Sir P Middleton
Mr Cassell
Mr Battishill
Mr Lankester
Mr Pirie
Mr Hall
Mr Saunders
Mr Ilett
Mr Makeham
Mr Ridley
Mr Lord
Mr Portillo
PS/IR

BUDGET PRESENTATION: POST-BUDGET CONTACTS

The Chancellor has seen your minute of 16 March. He agrees that the Economic Secretary should no longer attempt to meet the CLCB but wonders whether he might see the BBA instead.

MOM

MISS M O'MARA

ECONOMIC SECRETARY TO THE TREASURY

FROM: T M STUBBINGTON
DATE: 19 March 1984

PS/CHANCELLOR — 2

X is quite right. I ~~think~~ assume we have our defences prepared. N.

cc PS/Chief Secretary
PS/Financial Secretary
PS/Minister of State
Sir P Middleton
Mr Battishill
Mr Lankester
Mr Allen
Mr Pirie
Mr Ilett
Mr Ridley
Mr Corlett - IR

BUDGET PRESENTATION: CONTACTS AFTER THE BUDGET

The Economic Secretary last Friday met Mr Mitchener (Chairman of Equipment Leasing Association and the Director of Lombard North Central) and Mr McDonald, a Deputy Secretary of the ELA.

The discussions were very relaxed. Mr Mitchener admitted the ELA had been surprised by the announcement, but he said he had no intention of making any protest. He agreed that in the short term the changes would make leasing more attractive. He expected a boom in leasing up to the first quarter of 1985 or so and thereafter some easing off - eventually a fall in leasing activity of 25 per cent or more, though it was difficult to project exactly how the various factors would balance out. Mr Mitchener also agreed with the Economic Secretary's suggestion that the period of spectacular expansion in leasing had come to an end well before the Budget. They could only have expected further expansion in line with investment trends generally.

Mr Mitchener confirmed that leasing would continue to play a significant role after the full Budget package had come into effect. Short term leasing would have much less price advantage but would still have non-priced advantages, eg off-balance sheet financing. Longer term leasing would retain a significant price advantage and in any event there were few alternative sources of finance for certain kinds of investment.

X Mr Mitchener thought that the Government would get rather more criticism from the shipping and ship building industries, for whom leasing was especially important, contributing in particular to the relative advantage (or lack of disadvantage) in placing orders with UK yards. Mr Mitchener added that he would like early technical consultations with the Revenue on a few points of difficulty, in particular the definition of "binding contracts" entered into before Budget Day. Mr Corlett agreed to arrange this.

The Economic Secretary asked that he should be kept informed as to how reliefs in trade is going and once the implication of Budget measures had been thought through by the leasing industry he would like to meet the ELA again.

T.M. Stubbington
T M STUBBINGTON

PERSONAL AND CONFIDENTIAL

(P-P)

FROM: J O KERR
DATE: 21 March 1984

Mr Peretz

cc Sir P Middleton
Miss O'Mara

BUDGET PREPARATIONS: PRIVATE OFFICE GUIDELINES

... I attach some notes which you may, I hope, find helpful in the run-up to next year's Budget. I have confirmed with the Chancellor that the views attributed to him at various points are in fact his; and Sir P Middleton too is content with the text.

J O KERR

PERSONAL AND CONFIDENTIAL

FROM: J O KERR

DATE: 15 March 1984

BUDGET PREPARATIONS: PRIVATE OFFICE GUIDELINES

The Guardian leak apart, the Chancellor was well content with the way in which the Budget preparation exercise was handled this year, and has in particular confirmed that he sees value in the two innovations made since his days as Financial Secretary - ie the early weekend "Chevening" conference, and the regular pattern of formal "overview" meetings. Following the leak enquiry, and before next year's preparations start, it will be necessary to establish with him whether for security reasons he wishes to move closer to a system of making the Budget in water-tight compartments, with only a very few individuals having the run of the whole ship. These notes are descriptive of the current practice; and would need to be reviewed in the light of any decision to tighten internal security.

Initial Preparations

2. The first point to note is that it is essential to make an early start. This year the Chancellor had constructed by early September his private list of the main candidate tax reforms; and most items on his list saw the light of day on 13 March. Of course one has at that stage very little feel for how much forecast room for manoeuvre there will be; but it is possible, and highly desirable, to arrive at a rough allocation of priorities. It is not necessary - or I think desirable - for the Chancellor's preliminary thoughts to be disseminated at all; though he will wish to discuss them with the Permanent Secretary at various points in the autumn. Having a rough plan up his sleeve does however help him to guide Treasury Ministers on the areas of reform which they should be pursuing with the Revenue Departments: it is also useful to him in deciding how best to play discussions in No 10, Chequers seminars, and - next year - the involvement of Lord Cockfield on tax reform. Given that October and early November tends to be much taken up with Survey

PERSONAL AND CONFIDENTIAL

and then Autumn Statement issues, it is important to get cracking in September (and therefore not to let the CFM/G5/G10/Interim Committee/Development Committee/IMF/IBRD meetings obtrude too much).

<u>Chevening</u>

3. The FCO are already aware that the Chancellor will wish to hold another Chevening conference next January. Dates should be settled, and a firm booking made, before the summer break. Negotiations should be conducted between Private Offices, after discussion between the Chancellor and the Permanent Secretary; and the outcome should be confirmed in a short letter from the Chancellor to the Foreign Secretary (whose house Chevening notionally is).

4. The three previous such conferences have taken place on the first or second weekend after the Christmas break. With the likelihood of an April Budget next year - and that is a decision which ought if possible to be settled very early on, though the announcement is not made until the first Thursday after Parliament's return from the Christmas recess - it might be possible to consider moving one weekend later. But it would still be important to ensure that the key paper - by Sir T Burns - is available for Christmas reading.

5. The Chevening agenda is drawn up by the Permanent Secretary in consultation with the Chancellor. So too is the invitation list - ~~or at least~~ ie The names of those in addition to Ministers, Permanent Secretaries and Special Advisers, who are to be invited to come for all/part of the weekend. (It is important to let Ministers and Permanent Secretaries know <u>in the summer</u> of the chosen date: if there were to be any absentees, much of the point of the exercise would be lost. A decision on whether wives are, as in the past, to be invited also has to be taken.)

6. The Chancellor and the Permanent Secretary have agreed that for future Chevenings <u>all</u> papers will be circulated to Ministers at least one week in advance.

Overviews

7. Since 1982 we have developed a regular practice of Budget "overview" meetings each Tuesday morning, starting 9 days after the Chevening conference. The discipline these impose on the flow of papers and decision-taking is useful: their other primary purpose is to involve the full Ministerial team. So Private Offices need to be told, at Christmas-time, when the weekly series will start, and to be reminded that "overviews" are to be treated as virtually unbreakable engagements.

8. The agenda for each "overview" should be decided on the preceding Wednesday/Thursday; and all those commissioned to produce papers for it should be reminded - again on the Wednesday/Thursday - that such papers must reach the offices of all "overview" members by the Friday night. A formal agenda notice should go round on the Thursday/Friday. The Monday should be used for small meetings - eg of Ministers, or between the Chancellor and the Permanent Secretary - on particular issues to be taken on the Tuesday. People should be discouraged from raising at the "overview" issues emerging from papers not mentioned on the agenda notice. All "overviews" should be formally recorded, with clear action instructions.

9. The permanent membership of the "overview" team is clearly a matter which will have to be reviewed following the leak.

10. A permanent feature of each "overview" agenda should be a score-card minute from the Central Unit, produced on the previous Friday and incorporating all Budget decisions taken up to then.

Cabinet

11. The November Economic Cabinet does not, and should not, have much Budgetary significance. The February Economic Cabinet is however crucial, not least because it can have substantial impact

on the parameters of the eventual PSBR decision. Its date needs to be fixed with No 10 and the Cabinet Office before Christmas - and a late Budget could mean a move from the early February dates of recent years to a mid-February date. But it is worth bearing in mind that the closer the date gets to Budget day, the greater the risk that the Chancellor will be pressed to show a little of his hand. The scope of the Chancellor's paper needs to be decided quite soon after Chevening: the 1983 and 1984 papers followed a similar pattern, and were well received. The paper must of course be cleared in advance with No 10.

12. The Budget Cabinet - ie on the morning of Budget day - has not caused problems since 1981. No paper is, of course, circulated.

Prime Minister

13. The Chancellor ought if possible to have an opportunity for a long private talk with the Prime Minister in late January/early February about the probable broad outline of the Budget. This was contrived in No 11 in 1984, and worked extremely well. When all the main Budget measures have been settled internally - and this ought to happen at the latest some 2½ weeks before Budget day - the Prime Minister's formal endorsement should be obtained through a series of formal minutes from the Chancellor. There were 6 such minutes in 1984: they deserve very careful drafting. Some attention to timing is also desirable: the Chancellor's weekly "bilateral" talks with the Prime Minister, which for much of the year are movable feasts, and sometimes quite short, need in the key period - ie 2-4 weeks before the Budget, to become very firm entries in both diaries, and must not be rushed. The Chancellor's minutes should be timed to arrive fairly early on the afternoon of the day before the "bilateral" in question, so that the Prime Minister has time to digest them before she sees the Chancellor.

14. Budget secrecy in No 10 is good, and strictly observed. In previous years Sir A Walters was an "overview" member: in 1984 we were not asked to, and did not, extend this facility to Mr Redwood. He - but none of his Political Unit staff - did however see the Chancellor's minutes. The only Private Secretaries who did so were Mr Butler and Mr Turnbull. Mr Ingham was brought in only to be shown a Speech draft on the Thursday before Budget day.

Cabinet colleagues

15. In early February the Private Office must, after consultations, draw up a list of all those Cabinet colleagues who have to be consulted on individual Budget measures. Except when the matter is highly technical, such consultations go best in No 11, in great Budget mystique, and with no officials present. The most obvious exception is oil taxation, where an existing Working Group of Revenue/Treasury/Energy officials has a good tradition of reaching agreements, without leaking.

16. For Budget '85, special arrangements will have to be made for Lord Cockfield. I suspect that the Chancellor will wish him to join all main internal meetings on the Capital Taxes, and some on personal tax, but will not wish him to become a permanent member of the "overview" team. This however needs to be confirmed in the autumn.

Chancellor's diary

17. It is important to ensure that the diary is kept reasonably free from extraneous engagements/meetings in the Budget period. Budget "purdah" provides a good excuse for turning down all social lunches/dinners, all speaking engagements, and press activities from early February. But a free ½ day should be preserved in each week once the "overview" season has started, in order to allow the Chancellor to focus in No 11 on key Budget issues, rather than doing so via the

overnight box, with no officials around for informal discussions. Either 17 or 10 days before the Budget, the Chancellor should be given a 3 day weekend at Stoney Stanton to work on the Speech. (17 days in advance would be best, but 10 days worked perfectly well this year.)

Budget Speech

18. The preparation and circulation of early drafts of the Budget Speech is a Central Unit task. (I think it very likely that the circulation will be much reduced, following this year's leak.) The Private Office take over the Speech as soon as all the main Budget measures have been decided - ie some 2½ weeks before Budget day. Its preparation becomes the principal task in the last week.

19. The Chancellor likes to write - ie re-write - all his own stuff. But it helps if the Private Office produce formulae along lines that may be broadly acceptable to replace obviously unusable chunks of (eg Revenue) gunge. And the Private Office must of course clear, with the key officials concerned, formulae emerging from No 11, whether constructed by the Chancellor or constructed in the Private Office and blessed by him.

20. The text must be completed over the weekend before Budget day. That means that the final draft has to go round on the preceding Thursday, and the provisional final version on the Saturday. No 10 should get their draft by the Wednesday at the latest, and should then see succeeding versions.

Handling the Revenue Departments

21. The Private Office need to be particularly careful during the Budget period to keep in very close touch with the heads of the Revenue and Customs. Both need to be aware of all meetings on their subjects which will involve the Chancellor, and to be given the opportunity to attend. Both need to be consulted each week about the "overview" agendas; and it pays for the PPS to have a separate informal

weekly conversation to enable both to mention any worries not being brought out in the papers. And Customs need to be asked - in early February - to produce a private list of their real deadlines for excise duty and VAT decisions; and need to be made to feel that this remains the top paper in Private Office trays throughout.

Handling other Treasury Ministers

22. Extended "Prayers" meetings, without PPSs, are useful in January - pre- and post-Chevening, and at least once or twice during the final run-up to the Budget. In the last month, the normal form should be for normal "Prayers" meetings to be two-part, with the PPSs being thrown out at half-time to allow for some discussion of Budgetary matters thereafter.

23. The key point is to ensure that all Ministers (a) feel fully involved in the whole Budget process; and (b) are clear as to the precise tasks which have been delegated to them, and when their recommendations will be required. Informal liaison between the Private Office and other Ministerial Private Offices, usually on a nightly basis, is important in the last few weeks.

Budget Day Arrangements

24. The press razamataz needs to be pre-planned, at least a couple of weeks in advance. Timings for the Finance Committee and Lobby engagements need to be watched. And work on the Budget Broadcast should start very early on. (The first step is for the Chancellor to confirm to Mr A Jay in early January that his assistance would again be welcome; in February - or for an April Budget early March - preliminary decisions need to be taken on charts and graphics; a script for the first half (ie not covering the measures) needs to be with Mr Jay at least 2/2½ weeks before the day; and weekly meetings to check on progress should be set up. Mr Folger and Mr Portillo carried the main load this year: with considerable success.)

JOK

J O KERR

cc Mr Folger
Mr Hall
Mr Ridley
Mr Lord
Mr Portillo

Treasury Chambers. Parliament Street. SWIP 3AG
01-233 3000

21 March 1984

Anthony Jay Esq
33 Mount Avenue
Ealing
London W5

Dear Tony

Now that the dust is settling after the Budget, I should like to let you know how very grateful I am for all your help over the television exercise. From your initial tutorial through your work on the script and advice on the graphics to your help and encouragement on Budget Day - it all was invaluable. The product seems to have been generally well received: most of the credit for that is due to you.

I have taken your advice, and got hold of the video; and I very much hope to take up your kind offer of a further tutorial on the basis of it before next year's exercise. I do hope that you will feel able to play your key part again throughout the exercise next year - but the main purpose of this letter is simply to thank you for all you did this time.

I really am most grateful. It would not have been possible without you

Yours
Nigel

NIGEL LAWSON

It is most important that the CST, in his speech, does deal with Fairness [illegible] (para 3).
2. He should also try to focus on those matters in the Fin. Bill which I was not able to include in the Budget speech.
This will maximise press coverage.

C

Mr

Speech outline looks ok to me.
If 2nd reading is on April 11th, you will be flying to Washington.

FROM: JOHN GIEVE
DATE: 28 March 1984

MR F MARTIN

cc PPS
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Cassell
Mr Monger
Mr Battishill
Mr Folger
Mr Norgrove
Mr Hall
Mr Lord
Mr Portillo
PS/Inland Revenue
PS/Customs & Excise

(See also note on paper below)

FINANCE BILL SECOND READING DEBATE

The Chief Secretary discussed with you and others yesterday his Speech in the Second Reading Debate - which may now be on April 11 rather than April 10. You agreed to put together a first draft by 3 April, in consultation with EB and the Revenue departments. This should be about 30 minutes in length. It should include the following elements:

a. Introduction - setting the Budget in the context of a long term strategy of reducing the burden of taxation, Keeping the pressure on inflation, while improving the "supply-side" performance of the British Economy by freeing market forces.

b. A common thread in the Budget measures is removal of distortions and simplification. The overall aim is lower rates of tax, higher thresholds, and less special exemptions.

c. Much of the Bill is left over from last year and, many draft clauses have been subject of consultation and amendment since April 1983 (say how many).

d. The main points in the Bill include VAT on alterations and take away food - naturally unwelcome that present borderlines non-sensible, new bordelines generally comprehensible and sensible, new constructions still exempt, comparisons with rest of europe.

e. Income tax allowances - major increase this year, record since 1979, further step on the road which will eventually help on poverty trap.

- [case against lower rate band]
- child benefit, no decisions until June, highest level ever, [but is probably counted like other benefits as public expenditure and not as a relief from tax]

f. Company Taxation (CT rates, allowances, and NIS) - a brave and imaginative reform, pick up comments from CBI and equipment leasing association etc.

g. Savings and Investment (LAPR, stamp duty, IIS) - fairly brief section.

h. A section picking up the other parts of the Bill eg. CGT, CTT, oil and gas, controlled foreign companies and offshore funds, share options.

i. The Peroration - reforming Budget, a strong theme through the Bill.

2. In the sections on individual measures, he would like to pick up particular criticisms where these can be shown to rest on a misunderstanding of the measures or where we have a clarification/concession to offer. In particular he would like to comment on:

- the impact of the extension of VAT on historic houses etc.
- any concession to help housing associations (see Mr Gow's recent letter)
- any concession to the handicapped on VAT or car tax
- motability.
- lifeboats

He would be grateful for any further suggestions.

3. He thinks, if it can be fitted in, he should also make a brief statement on Furniss and Dawson. That might be put in in relation to the clauses on controlled foreign companies offshore funds.

4. The Chief Secretary has also asked for some defensive briefing to use in case of interventions. Mr Folger agreed to coordinate this. This should take the form of a series of one page notes with a form of words for use at the top and background at the bottom. Particular subjects which he wants covered are the following:

- impact of tabacco tax on jobs
- VAT on imports
- lack of consultation of LAPR and company tax reform (vis previous Green Paper on corporation tax)
- VAT on charities
- industrial life assurance companies and friendly societies
- share options - further complications in the tax system
- effect of company tax changes on films and shipping.
- possibility of further extensions of VAT eg. energy, new building, food, newspapers and magazines
- possibility of further simplification in the savings field - eg. pensions and mortgage interest relief.
- no doubt other subjects will need to be included following the Chancellor's appearance before the TCSC.

JG

JOHN GIEVE

2.39

(pwp)

FROM: MISS J C SIMPSON

DATE: 29 March 1984

cc PS/Financial Secretary
PS/Minister of State
PS/Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Cassell
Mr Monger
Mr Battishill
Mr Folger
Mr Norgrove
Mr Martin
Mr Hall
Mr Lord
Mr Portillo
PS/IR
PS/C&E

PS/CHIEF SECRETARY

FINANCE BILL SECOND READING DEBATE

The Chancellor has seen your minute to Mr Martin of 28 March with the outline for the Chief Secretary's speech in the Second Reading Debate. He has commented that it is most important that the Chief Secretary should deal with Furniss and Dawson (your paragraph 3). He has also suggested that it would be helpful if the Chief Secretary could focus on those matters in the Finance Bill which he himself was not able to include in the Budget speech, as this would maximise the press coverage.

JS

MISS J C SIMPSON

MOB

UNCLASSIFIED

(plip)

FROM: F MARTIN

DATE: 29 March 1984

CHIEF SECRETARY

cc PS/Chancellor
PS/Financial Secretary
PS/Economic Secretary
PS/Minister of State
Mr Monger
Mr Battishill
Mr R I G Allen
Mr Folger
Mr Ridley
Mr Lord

PS/Inland Revenue
PS/Customs and Excise

FINANCE BILL 1984

In discussion with the Opposition and more generally you may find the attached table prepared by Inland Revenue useful. It covers the Revenue clauses in the Bill concerning items dropped from the 1983 Finance Bill, proposed new clauses for that Bill not published before the dissolution and items which the Government announced before the Budget would be in the 1984 Bill. These comprise a total of 59 clauses and 11 schedules, and about 122 pages of the Bill. In addition, there are 6 similar clauses and 1 schedule in the Customs and Excise/Treasury areas, totalling about 8 pages of the Bill. Thus of the Bill's 223 pages (215 excluding the repeals schedule) some 130 deal with "pre-Budget" items of one type or another. About 60 pages are for measures dropped from the 1983 Finance Bill. And of the Bills 123 clauses and 23 schedules, some 44 clauses and 10 schedules (covering about 103 pages) have been subject to consultation, either formally through the publication of draft clauses or informally through discussion with the interested representative bodies.

F Martin

F MARTIN

A. MEASURES DROPPED FROM 1983 FINANCE BILL

Clause No.	Title	Length (Pages)	Consultation (Yes or No)	Formal/ Informal	Draft Clauses Published
25	Self employed persons living in job-related accommodation	2/3	No	-	-
32	Apportionment of income etc of close companies	1/6	No	-	-
38, 39 + Sch 10	Share Options	8 1/4	No	-	-
41	Discounts on bills of exchange drawn by trading companies etc	1	Yes	Informal	-
42	Incidental costs of obtaining loan finance	1	Yes	Informal	-
43	Trustee savings banks	1/2	Yes	Informal	-
46	Group Relief: apportionment	3/4	Yes	Formal	8.11.1983
48	Stock Relief: houses taken in part exchange	1	Yes	Informal	-
52	Double taxation relief to be applied before advance corporation tax	1	Yes	Formal	-
56	Proceedings in magistrates' courts and county courts	1/2	No	-	-
61	Capital gains tax: small gifts, instalments and monetary limits for reliefs etc.	1/2	Yes	Informal	-

(A. Continued)

Clause No.	Title	Length (Pages)	Consultation (Yes or No)	Formal/ Informal	Draft Clauses Published
67	Capital gains tax: foreign currency accounts	1/3	Yes	Informal	-
69	Capital gains tax: non-resident settlements: definition of "settlement" and "settlor"	1/4	Yes	Formal	30.1.1984
80 to 89 + Schedules 16, 17 & 18	Controlled Foreign Companies	35 1/2	Yes	Formal	31.10.1983
99	Capital transfer tax: special discretionary trusts: excluded property	1/2	No	-	-
101	Capital transfer tax: property moving between settlements	1/2	No	-	-
102	Capital transfer tax: adjustment of tax	1/3	No	-	-
103	Capital transfer tax: recovery of tax	1/2	No	-	-
115	Development land tax: deferred liability	1	No	-	-
117	Development land tax: deduction of tax from consideration for disposals by non-residents	2/3	Yes	Informal	-
118	Development land tax: payment by instalments and postponement	1	No	-	-
122 + Sch 22	Special and General Commissioners	4	Yes	Formal	-

B. PROPOSED NEW CLAUSES NOT PUBLISHED BEFORE THE DISSOLUTION OF PARLIAMENT

Clause No.	Title	Length (Pages)	Consultation (Yes or No)	Formal/ Informal	Draft Clauses Published
35	Interest on quoted Eurobonds	1 2/3	Yes	Formal	13.12.1983
36 + Sch 9	Deep discount securities	8	Yes	Formal	22.12.83
44	Pension Funds etc: extension of tax exemption to dealings in financial futures	1/3	Yes	Formal	13.12.83
49 + Sch 11	Furnished holiday lettings	2 2/3	Yes	Formal	31.1.1984
68 + Sch 14	Capital gains tax: postponement of tax due from beneficiaries on gains of non-resident trustees	13 1/2	Yes	Formal	30.1.1984
72	Disqualification of certain life insurance policies	2/3	Yes	Formal	22.8.1983

C. OTHER ITEMS WHICH THE GOVERNMENT ANNOUNCED WOULD BE IN THE 1984 BILL

Clause No.	Title	Length (Pages)	Consultation (Yes or No)	Formal/ Informal	Draft Clauses published
24	Relief for interest: money borrowed for investment in employee-controlled company	1/2	Yes	Informal	-
31	Scholarships	1	Yes	Informal	-
34	Building Societies: interest to be payable gross on certain deposits	1/2	Yes	Formal	30.9.1983
40	Share incentive schemes: shares in authorised unit trusts	2	Yes	Informal	-
54	Grants to assist industry in Northern Ireland	1/2	No	-	-
58	Capital allowances: transfers under Oil and Gas (Enterprise) Act 1982	3/4	No	-	-
59	Capital allowances: first year allowances: recipients of mobility supplement	1/2	Yes	Informal	-
64	Capital gains tax: disposals and acquisitions treated as made at market value: removal of certain exceptions	1	Yes	Informal	-
65	Capital gains tax: parallel pooling amendments	1	Yes	Informal	-

(C. Continued)

Clause No.	Title	Length (Pages)	Consultation (Yes or No)	Formal/ Informal	Draft Clauses Published
74 + Sch 15	Insurance policies issued outside the United Kingdom	5	Yes	Formal	22.2.1984
90-97 + Schedules 19 & 20	Offshore Funds	18 1/2	Yes	Formal	22.2.1984
106	Stamp duty: extension of stamp duty relief on sales at discount	3/4	No	-	-
109	Restriction on PRT reliefs	2	No	-	-
110	Sales of oil: treatment of certain payments	1	No	-	-

FROM: F MARTIN
DATE: 3 APRIL 1984

CHIEF SECRETARY

cc Chancellor ✓
Financial Secretary
Economic Secretary
Minister of State
Mr Cassell
Mr Monck
Mr Monger
Mr Battishill
Mr Folger
Mr R I G Allen
Mr Griffiths
Mr Lord
PS/Inland Revenue
Mr Kucyzs IR
PS/Customs & Excise
Mr Wilmott C&E

c/ Furniss vs Dawson is in § 11-12.

I agree: para 18 should be omitted: if we are attacked for lack of greater details during the debates, FST can say something in the wind-up. Paras 34 and 35 should be emboldened in the speech - eg before paras 29 and 30 - and substantially strengthened along the lines of Mr Monger's paper for the TCSC. N.

FINANCE BILL SECOND READING DEBATE

Attached is a first draft for your speech. It covers most of the ground set out in Mr Gieve's minute of 28 March and is based on contributions by EB and the Revenue Departments, though they and others have not had the opportunity to comment on my "editorial" treatment. Apart from general improvements that might be made to the presentation, two areas mentioned in Mr Gieve's minute have not been covered as yet - the question of a concession to housing associations to help with VAT on alterations and the question of help to Motability to assist with the effects of the capital allowance changes. I understand that both questions are still under consideration.

F Martin

F MARTIN

203/2

FINANCE BILL SECOND READING

CHIEF SECRETARY'S SPEECH DRAFT 3.4.84

The Budget which my right hon Friend the Chancellor of the Exchequer presented to the House a month ago was designed above all to carry forward the firm financial policies that have provided the right framework for lower inflation and lower interest rates. Only by maintaining the pressure against inflation can we have sustainable growth of output and maintain the heartening turnround in employment which we saw in 1983. Under the Government's medium term financial strategy, sustained deceleration of monetary growth and steady reduction of public borrowing should bring a further gradual slowing down in the growth of money national income. Within this, lower inflation will continue to make room for growth of real GDP. My RHF set out a 5 year path for progress on those lines, right through this Parliament. With firm control of public spending there will be room within the strategy for overall reductions in taxation. Reductions in taxation - improving incentives and increasing the return on investment - will in turn assist the continued improvement in economic performance. In short, the strategy is designed to achieve that virtuous circle - the growth in output accompanied by l~~a~~ow and declining rates of inflation, leading to the increased investment and productivity in turn supporting further non-inflationary growth - which is the only sure basis for real improvements in employment and living standards.

2. As the House has no doubt noted, a number of figures published in the month since the Budget have confirmed these positive trends in our economy.

3. The reduction in short term interest rates has continued, following the cut in bank base rates on 14 March. Three month rates are also now [nearly 2 per cent] below those in the US. So the markets are expressing a confidence in the balance of our fiscal and monetary policies. Lower interest rates made possible by restraint of public borrowing are good for business and personal borrower~~s~~. And I need hardly remind the House of the 1 per cent cut in mortgage interest rates announced by the Building Societies on 16 March.

4. The March figure for unemployment, an increase of 11,000, follow~~ing~~ed disappointing figures for January and February. Nevertheless, the labour market picture is brighter than a year ago. The employed labour force is estimated to have risen from March last year. And unfilled vacancies, for example, are much higher than they were a year ago. Short-time working is at the lowest level for four years and overtime working has risen strongly. Economic growth in 1984 should be consistent with continued growth of employment, though the number of new jobs and the rate of growth in total employment will continue to depend crucially on realistic levels of pay.

x 5. Exports in February, at £6033 million, were an all-time record. And, within the total, manufactured exports are doing very well - in the 3 months to February they were up 6 per cent in volume terms, and at their highest for four years. Of course manufactured imports are rising as well. But that is not unexpected given the growth in the economy and in no way diminishes the encouraging performance of our manufacturing industries. The forecast 5 per cent increase in total export volume for this year looks well-founded. Higher exports, and strong growth in investment will make an increasing contribution to broadly based growth, complementing a further, albeit slower, rise in consumers' expenditure.

lc 6. The fourth point on which I should like to comment is the results we had last week from the first CBI monthly trends inquiry since the Budget. These confirmed that the widespread recovery in manufacturing is continuing. Total and particularly export demand have strengthened further. More manufacturers than at any time since 1976 are expecting to increase their output. The CBI now expect increases in manufacturing investment of about 8 per cent in both 1984 and 1985.

7. Of course there have been other statistics - continuing good news on inflation, the figures for investment in the second half of last year and confirmation of a healthy and necessary rise in profits ~~in profits~~ for 1983. But I have said enough I think to show that the non-infationary recovery in output we have seen since 1981 continues steadily. This is the context of the Finance Bill before the House today, a Bill which provides a major reform of the tax system. A central aim of my right hon Friend's Budget is to improve the working of the economy by reducing the burden of tax on profits and earnings and by reducing the tax-induced distortions to decision-taking which have hampered the creation of output, wealth and jobs.

8. Before describing these measures I should draw the attention of the House to the report of the Treasury and Civil Service Committee on the Budget, which was published yesterday. I am grateful to my right hon Friend the Member for Worthing and his colleagues on the committee for producing a report which will no doubt help inform the House's consideration of the Bill.

9. I should also remind the House that this year's Finance Bill contains rather more than the Budget proposals. Because of the intervention of the General Election, the Bill contains a number of clauses originally introduced in the 1983 Bill, together with the clauses which the Government had proposed to introduce into that Bill but which did not come forward because of the dissolution and clauses on tax changes which the Government announced in advance of the 1984 Budget. Of the Bill's total contents,

about 130 pages deal with such pre-Budget items of one type or another. The silver lining is that this has enabled a very substantial amount of prior consultation on the Bill's contents. Of the Bill's 123 clauses and 23 schedules, some 44 clauses and 10 schedules - comprising about 103 pages of the legislation - have been subject to consultation, either formally through the publication of draft clauses or informally through discussion with the representative bodies and groups most directly interested. I am sure that this will greatly facilitate consideration of the Bill.

10. Regarding the clauses which stem from this year's Budget, here are a number which do not have the same weight as the major reforms which the Bill introduces, but which are nevertheless of importance in particular contexts. There are, for example, the improvements in share option schemes in clauses 38 and 39. In successive Budgets, the Government has introduced measures to encourage wider share ownership. These have been notably successful and widely welcomed. This year, we are proposing a new relief for approved share options, replacing the income tax charge by a charge to CGT on disposal of shares. This is designed to help companies attract and motivate key management - on whom so much depends - by linking their rewards with the company's success. Clauses 61 to 69 provide some minor improvements to capital gains tax, including in clause 66 a useful simplification of the CGT code to allow gifts to heritage maintanance funds to be treated like other gifts, as has been urged by the Historic Houses Association. Clauses 75 to 79 improve the corporation tax regime applying to the oil and gas industry while clauses 109 and 110 make minor changes in petroleum revenue tax, following the major changes last year which the House will recall did a great deal to increase exploration and development. Clause 98 provides a reduction in the top rates of capital transfer tax. These were out of line with other direct taxes, and with other countries' estate taxes. The rate schedule for lifetime gifts will be reformed so that it is always half the rate for transfers on death. Clauses 99 to 192 improve the CTT regime with respect to discretionary trusts, while clause 104 and schedule 21 tidy up the CTT legislation in advance of its consideration later this year. Clause 114 will raise the threshold for development land tax from £50,000 to £75,000 and clauses 115 to 118 make other useful improvements which will similarly assist industrial and commercial development. Two lengthy sections of the Bill are devoted to legislation to counter abuse. Clauses 80 to 89, together with Schedules 16 to 18, deal with controlled foreign companies. Clauses 90 to 97, and Schedules 19 and 20, are concerned with offshore funds. Both those major pieces of legislation were subject to full consultation in advance. As a result, the contolled foreign companies provisions have been substantially modified, while we will be bringing forward amendments on offshiore funds at Committee stage.

11. In the context of tax avoidance the House may find it helpful if I say a few words about the recent decision in the case of Furniss V Dawson~~s~~. This confirmed the so-called "new approach" to interpretation of the tax statutes [explain] which had begun to emerge from other decisions, notably in Ramsay. I believe that the principle which is emerging from this line of cases is bringing the interpretation of the tax statutes more closely in line with practice in other major countries abroad, such as the United States, and - dare I say it - in line with the clear intention of the legislature. Over time, I believe that it will help us to make legislation itself simpler, more straightforward and less onerous.

12. When the decision was first published, it was the subject of much speculation - some of it frankly alarmist. For example, there was speculation about the Revenue challenging the tax treatment of covenants, leasing transactions and straightforward transfers of assets between group members. I am glad to find that most commentators are now seeing the decision in a more balanced perspective and glad also to emphasise to the House that the decision will not be used to challenge straightforward transactions entered into for valid commercial reasons. Clear guidance has been issued to Inspectors of Taxes on this point.

13. At the centre of the Finance Bill are the clauses which provide for the reform of business taxation and of the tax treatment of savings and investment, coupled with the clauses which provide for a switch from taxes on personal income to taxes on expenditure and enable a substantial real increase in income tax allowances as a start in raising thresholds to realistic levels.

14. Clause 18 of the Bill provides for the progressions reduction in the main rate of ~~compensation~~ corporation tax to 35 per cent in 1986-87, clause 47 for the abolition of stock relief, clause 57 and schedule 12 for the cutting back of the subsidy element in capital allowances and clause 113 for the final abolition of the National Insurance Surcharge from 1 October 1984. The aim is to encourage employment, enterprise and the efficient allocation of resources. The method is to get the Government off the back of the corporate sector, to a position where the maximum tax on profits is not one-half, but one-third, and to a position where decisions are based not on the tax subsidy which can be gained but the profits which can be produced. The abolition of the tax on jobs plus the elimination of the bias in favour of investment on capital equipment will not only lead to more investment ~~on~~ in people but also to more productive investment overall. Who would say for example, looking at our economic performance since the War, that we had got the balance of our investment exactly right? While the level of UK investment appears to have been well up to that of our main competitors, the indicators are that the returns from it have been significantly lower. Indeed all the evidence suggests that it is

the poor quality of and use of our investment that has lain at the root of many of our problems. After all investment is a sacrifice of current consumption and this is only worthwhile if the return adequately repays this sacrifice. Up to now too much investment has been undertaken only because it has been subsidised by the tax system. In future companies will need to pay more attention to the <u>real</u> profitability of investment - what a project earns pre-tax.

15. This will, I accept, mean that some projects which otherwise would have taken place will not now proceed. But by the same token, other better projects, which would not previously have gone ahead, now will do so. And, what is more, the combination of the lower rates of corporation tax with the capital allowances changes should mean that projects with high rates of return will be more profitable than under the old system.. Thus the overall effect of these reforms will be to encourage winners rather than losers and to reward risk-taking and enterprise instead of tax planning and to lead to more employment instead of lost jobs.

16. In this context I was surprised to see in the week after the Budget a suggestion emanating from a firm of stockbrokers that the Budget in effect concealed a substantial increase in the tax payable on companies in about 1986-87. I should like to say a few words about this, lest even after this healing lapse of time there remains any misunderstanding. My RHF the Chancellor said that his corporation tax proposals would cost the Exchequer £m280 in 1984-85 and £m450 in 1985-86 and that during the transitional period as a whole there would be a broadly neutral effect on the financial position of companies. It does not require mathematical skill of the highest order to see that he was expecting some increase in revenue in the following years. It would be misleading to attempt to give exact figures for the additional yields several years ahead, as this turns on the difference between two very large changes in opposite directions. But the figures quoted in that article are altogether too high. There are a number of offsetting factors which may not have been fully taken into account, including the steps which companies will themselves take to increase their allowances: nor may sufficient allowance have been made for the increase in profits which should flow from the Chancellor's proposals. On any basis, such effect as exists could not last for longer than a year or two and companies will certainly benefit very significantly from the changes as a whole by the end of the 1980s.

17. No doubt that understanding underlies the generally favourable reaction to these proposals. For example the CBI view, as explained in their evidence last month to the Treasury Committee, is that, with rising profitability the new regime for corporation tax will be more favourable than the old. They suggested that the 100 per cent initial and first year allowances had been of doubtful effectiveness in inducing higher investment. Restructured capital allowances, giving a longer average period of write-off, were

realistic when taken together with the major reduction in the rate of tax. Overall, the CBI considers, the tax climate would be more encouraging, a factor which will not, I think, go without notice in multinational organisations considering future investment in this country.

? tactless in view of the Guardian

[18. The generally favourable reception which the corporation tax proposals have received has been particularly pleasing given the fact that in the nature of things it was not possible to consult on these changes in advance. While consultation has come to be the normal practice in relation to more detailed tax changes, we reluctantly had to take the view that such a radical restructuring of the corporation tax rates and allowances, with the other changes and the very large sums involved, was so much at the centre of my Right Hon Friend's Budget strategy as to preclude prior discussion on this occasion. Of course my Right Hon and Learned Friend, the Member for Surrey East, did consult widely about the corporation tax in his Green Paper issued in January 1982. And in his 1983 Budget he announced that we had decided to leave the broad structure of the tax unimpaired - in particular the imputation system - in response to the generally expressed plea for stability which came over very firmly from industry and commerce. My Right Hon and Learned Friend did not say, nor did he imply, that the rates of tax and the levels of allowances would remain unchanging - as the laws of the Medes and Persians. Indeed, by mapping out the path of reform and the corporation tax rates for four years ahead at once, my Right Hon Friend, the Member for Blaby, has done more than has ever been done before to give business the certainty it needs to be able to plan ahead with confidence.]

19. In short, the proposed changes are good for business. The best projects will gain the most, there will be a new freedom to select projects without the distorting effects of the tax system, and the tax on the returns from quality investments will be substantially reduced. In can only assume that all this was ~~has~~ foreseen when the Labour Party proposed these changes in its 1982 economic policy document, and on that basis I look forward to the support of hon Members on the benches opposite.

20. The same approach of removing distortions in the tax system underlies the proposals for the reform of the taxation of savings and investment. The most important components of this one, of course, the withdrawal of life assurance premium relief for new ~~phases on~~ policies in clause 70 and the reduction in the rate of stamp duty to 1 per cent in clause 105. Both changes make share owning more attractive for the ordinary man in the street. During the last 10 years, and indeed for much longer, most of our constituents have been moving away from direct investment in equities - not simply because of the risk involved in equity investment but because it has been expensive and because of the tax advantages of investing via a life policy.

21. A gap has opened by which is bad for society and had for the economy. The real owners of our trading and industrial companies are ordinary people (ordinary voters, ordinary trade unionists). Too often the real owners do not identify their own best interests with the commercial success of these companies. Life insurance will continue to be an important conduit for channelling saver's funds to commercial concerns but a better balance needed to be struck between direct and institutional investment. The cut in the rate of stamp duty reduces substantially the cost of buying shares. A £500 deal on the Stock Exchange cost an investor before the Budget £19.60. Clause 105 brings this cost down to £14.60, a reduction of over 25 per cent. The reduction in stamp duty of course benefits both the institutional and the private investors. But it is the private investor who in the past is more likely to have been put off by the high cost of dealing. Once again, this is a change which has been widely welcomed and for which I trust there will be support in all parts of the House.

22. But I sense already that it may be over-optimistic to expect similar support for the third major component of the Finance Bill - the switch from taxing earnings to taxing spending. The extension of VAT provided by clause 10 of the Bill is a central ~~point~~ part of that strategy. The total yield from taxing building alterations and hot take-away food and drink will be £375 million in 1984-85 and £650 million in a full year, meeting a considerable part of the cost of the increase in income tax allowances above inflation.

23. Of course, no-one welcomes the imposition of a tax charge. But I hope that on reflection ~~non~~ hon Members will see the force of the arguments involved. The House will be aware that, with only about half of consumer expenditure subject to VAT, the United Kingdom's VAT base is the narrowest in the European community. Including building alterations and hot take-away food in the scope of the tax will bring our treatment of these items into line with other EC countries, where they are already subject to a positive rate of tax.

24. Moreover, taxing building alterations will remove a major source of confusion, eliminating the difficult borderline between "repairs" and "alterations" which has been a source of a great deal of unproductive litigation in the past. From 1 June, the standard rate of VAT will apply to all building work, except entirely new construction. The change will not give the great boost to the black economy that some hon Members have suggested. I acknowledge that increasing taxation necessarily increases the incentive to ~~erode~~ evasion; but the removal of the unclear borderline between alterations and repairs will make this very much easier to tackle. The economic effect of taxation on the construction industry should therefore be much less severe than the fears which some

hon Members have expressed on this score might be taken to imply. And it must be borne in mind that three quarters of construction industry output will continue either to be zero-rated or tax deductibleby the purchaser.

25. Similarly taxing hot take-away food and drink will result in the same VAT treatment being applied to this area of expenditure as to other forms of catering, which have always been subject to the standard rate of tax.

26. There have been some suggestions in the press and elsewhere that the taxation of hot take-away food will give rise to anomalies. Inevitably there will be some potential borderline difficulties - no tax involving exemptions and reliefs can be without them. But these difficulties should not be exaggerated; the fact is that most people can recognise hot food when they see it or sell it. For example, there has been some concern by bakers concerning the pies they sell. We have assured the trade associations concerned that items such as pies which are sold hot only because they are just out of the oven will remain zero-rated, while VAT will apply to pies which are advertised or held out for sale as hot, or otherwise deliberately aimed at the hot take-away food trade by, for example, being sold from a hot cabinet.

27. Various concerns have been expressed about the extension of VAT to building alterations. Among these is the effect of the removal of zero-rating on projects involving the substantial reconstruction of properties particularly those which incorporated facades and other features of historic interest. Again, I can assure the House that that where all that is left of an existing building is one wall such as a front facade, a building making use of that single wall would be zero-rated as a new building. Where some other parts of the building remain standing, the case will have to be considered on its own particular facts. To provide a special relief for historic or listed buildings generally would lead to pressure for other reliefs, and a wide range of exceptions would defeat the objectives of greter simplicity and a shift in the burden of taxation which my rt hon Friend proposed in his Budget. To the extent that it is public policy to assist the retention of such buildings, it is better that the true cost of this should be identified through the payment of grants in appropriate cases, subject always to normal public expenditure considerations.

28. There are, however, one or two changes in the VAT area which I am sure the House will welcome. These are the extensions to the VAT reliefs for the Royal National Lifeboat Institution, and for the disabled. Both extensions will be made by Orders which will come into operation on 1 May. First, the relief for lifeboats is being extended to lifeboat carriage and launching equipment supplied to the RNLI. This is a small concession, but a useful one, for which the RNLI made strong representations before the

Budget, and I am sure it is a change which the House generally will welcome. Second, the existing VAT zero-rating for "personal ambulances" is being extended to cover vehicles designed or adapted for carrying a handicapped person in a wheelchair or on a stretcher - in effect the extension dispenses with the former restriction that a personal ambulance should have no seats to the rear of the driver if it to qualify for zero-rating. I must however make it clear that the extension of the relief does not, as some of the organisations representing the interests of the disabled seem to have thought, cover cars which are merely adapted for the use of a handicapped person by the provision of hand controls. To extend VAT relief to cars used by disabled people in this way would be very costly, and would also - I am afraid - be open to considerable abuse. [Nor have we thought it justified to provide more generally for recovery by charities of VAT on their non-business purchases. A general scheme of relief like this would be costly in revenue and expensive to administer. And, most seriously, it would give relief indiscriminating to a very wide range of bodies without regard to whether these were the sort of activities which taxpayers at large would want to support. For let us be in no doubt, reliefs from taxtion for any sector mean higher taxes for all the rest.]

29. The final area I would like to mention is the increase in income tax allowances in clause 21 of the Bill. The changes, by contrast with other ~~points~~ parts of the Bill, are not a radical once-for-all reform: they are part of a long-term strategy which we have pursued since 1979, and intend to continue in future years. Tax thresholds before the Budget already stood around 8 per cent higher in real terms than their 1978-79 level: we now propose a further increase in the basic allowances - for people of working age - of about 12½ per cent, some 7½ percentage points more than required by the statutory indexation provisions.

30. This is impressive progress - pushing basic thresholds up some 16 per cent in real terms so far - but not so impressive that we can afford to stop there. This is because keeping abreast of inflation, even getting ahead of inflation, is not by itself enough to make any useful impact on the real structural problem - that tax thresholds have fallen in relation to earnings and in relation to the level of social benefits. For example, the threshold for a married man has fallen from 38 per cent of average earnings as recently as 1972-73 to little better than 31 per cent in 1978-79.

31. This erosion of the tax threshold has of course greatly exacerbated the special problems of the poverty and unemployment traps: but it is right also to remember that these traps are only a symptom of the more fundamental problem that taxpayers generally - and the low-paid in particular - are required to pay too much income tax, or to pay tax when they should not be paying it at all.

32. We have started to push up thresholds for a married man to 33 per cent or so of average earnings in 1984-85: but we have a long way to go before we reach the levels we were used to only a decade or so ago. That is why we see this year's increases as only a step in a longer-term programme to get thresholds up to a more sensible level.

33. It is also why we cannot agree that the money - some £1100m in a full year more than indexation - might have been better spent in other ways. One proposal we will no doubt hear more of is the reintroduction of a reduced rate band of the sort we got rid of in 1980-81. Of course we see the attractions of a reduced entry rate of tax: but given the choice between higher thresholds and a reduced rate band, there is now wide agreement that higher real thresholds are the better choice - they take some people out of tax altogether - about 850,000 of them this year; for those still in the tax net they are worth as much for those with the lowest pay as for anyone else liable at basic rate; and they save complications for taxpayers and their employers and staff for the Inland Revenue.

34. It has also been suggested that the Government should not be aiming for tax reductions at all but instead increasing public expenditure on CB. The child benefit uprating will be announced along with the other new benefit levels in June and it would be wrong for me to anticipate those announcements. But I can say something about the suggestion that child benefit is uniquely effective in tackling the poverty trap. That would be more persuasive if we were concerned <u>only</u> with the poverty trap and even then concerned only with getting people <u>out of</u> the trap and not at all with improving the lot of those still in it. Because it is often forgotten that an increase in child benefit can only alleviate the trap when it replacs existing means-tested benefits and so <u>denies</u> the families in the trap - those at the bottom of the income scale - the increase in income which would go to families with children generally. And of course they do nothing at all to improve the incentives or increase the income of any of those houeholds - the large majority - who get no child benefit to start with.

35. By contrast, this year's threshold increase takes some people out of the trap <u>and</u> gives them and every other taxpayer an increase in their net income, whether or not they have chldren and whether or not they are in the trap. The effects in a single year may not be dramatic - although reducing the number of FIS recipients liable to tax this year by 6 per cent is not to be ignored - but in the longer term, we are clear that steady progress towardds a more sensible level of thresholds offers the most appropriate solution not only to the problems of the poverty and unemployment traps, but also to the problem of the income tax burden generally. That is why again I would hope for widespread support for the changes introduced in the Bill.

36. The Finance Bill thus provides a significant reduction in tax on personal income in 1984-85, within a broadly revenue-neutral Budget as a whole. In 1985-86 the Bill's provisions will reduce taxation by over £1.75 billion, including a substantial reduction in tax on businesses. With firm control of public expenditure there is the prospect of further tax reductions on future years. The Bill not only reduces taxes, but reforms the system in a number of important areas, ~~on~~ in ways which will assist the more efficient working of the economy, a sustained increase in output and the creation of jobs. In those respects ~~of~~ if no other, the Bill is monumental and I commend it to the House.

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

From: P G WILMOTT
Date: 4 April 1984

PS/FINANCIAL SECRETARY

cc PS/Chancellor
PS/Chief Secretary
PS/Minister of State
PS/Economic Secretary
Mr Cassell
Mr Monck
Mr Battishill
Mr Monger
Mr Folger
Mr Portillo
Mr Lord

FINANCE BILL SECOND READING : FINANCIAL SECRETARY'S WINDING-UP SPEECH

As requested in your note of 2 April to Mr Martin, I attach factsheets and lines to take on the following items:

19. VAT registration threshold
20. VAT on imports
26. VAT on hot take-away food
27. Motability
28. Beer/wine
29. Future intentions on VAT

I also attach a factsheet and lines to take on VAT on building alterations which might be used either separately or as part of the construction briefing.

P G WILMOTT

Internal distribution: CPS, Mr Knox, Mr Jefferson Smith, Mr Harris, Mr Freedman, Mr Boxall, Mr Cockerell, Mr Taylor, Mr Jenkins, Mr Smith, Mr Battle

FACTSHEET

19. VAT REGISTRATION THRESHOLD

Facts

- New limit £18700 (old: £18000)

- Cost: negligible

Positive

- Nearly 40,000 traders will be able to deregister if they wish

- Helps keep new businesses out of VAT net as long as possible

- Fifth successive year that threshold raised

Defensive

- Maximum increase possible under EC rules

- [If necessary: Government rejects Commission claim that UK limit too high]

Further details

- Budget brief M4

LINES TO TAKE

19. VAT REGISTRATION THRESHOLD

As a further measure to help small firms the Chancellor raised the VAT registration threshold from £18,000 to £18,700. This is the fifth successive year that it has been raised.

POSSIBLE SUPPLEMENTARIES

Why increase it by an odd amount - why not £19,000

Increases in the registration threshold are limited by the EC Sixth VAT Directive. This increase is the maximum permitted on the most favourable interpretation of the Directive, which only allows increases in line with inflation since the introduction of the tax. [Note: the UK does not accept the EC Commission view that increases must be limited to inflation since January 1978 or 1979]

Why not increase the limit to, say, £100,000

Such a large increase in the limit would cause considerable distortion of trade between registered and unregistered businesses and of course there would be a significant revenue loss, although since the change would involve up to about 1 millionregistered traders it is impossible to estimate it accurately. It would also be contrary to our EC obligations.

FACT SHEET

20. VAT ON IMPORTS

Facts

- Present system suspended from 1 October 1984

- Once-for-all revenue boost of £1.2 billion

- Continuing financing benefit to PSBR (about £120 million at current interest rates)

- At present postponed accounting for VAT available also for imported and some UK goods* leaving warehouse

Positive

- Abolishes 'free Government finance' currently given to importers : UK producers now on more equal footing

- Not against EC rules : coming into line with major EC competitors

- 4 weeks deferment available for most importers

Defensive

- Chancellor's commitment to revert to present system if EC agrees to harmonise on it

- Business gains overall from "Budget for 2 years" (link to NIS)

- No "Brenner Pass blockage" : natural break in transport at sea/air boundaries into which customs control fit

- No decision yet taken on treatment of UK goods in warehouse - being discussed with trade interests

- Many UK goods not affected by change: if not sold in warehouse, VAT not due on withdrawal. True of most big whisky and oil traders (VAT payable on subsequent sale in same way as on any other UK transaction)

- Some oil products - fuel oil, gas oil and kerosene - zero-rated for VAT in any case

* VAT is only due on UK goods if they were sold while in warehouse

20. VAT ON IMPORTS

LINE TO TAKE

My rt hon Friends decision to withdraw the present arrangements for accounting for VAT on imports from 1 October 1984 has been generally welcomed in the House. This brings us into line with our main European Community trading partners and puts UK producers on a more equal competitive footing with importers.

POSSIBLE SUPPLEMENTARIES

Isn't it contrary to our EC obligations

No. Our main trading partners in the Community already operate a similar system. The Community obliges us not to discriminate against imports from other Member States but there is no reason why we should discriminate in favour of them by giving them additional credit not enjoyed by domestic manufacturers.

Doesn't it ruin harmonisation hopes

The Commission wants our existing system to be adopted throughout the Community. If other countries refuse, there is no reason why we should extend to their exporters advantages which they do not extend to ours. If, however, they agree to the change, then the UK will re-introduce the present system.

Why not retain the present system for raw materials

It would be administratively impractical, and could contravene our EC obligations.

New arrangements will cause "Brenner Pass" blockade at Dover

There may be more chance of congestion at some ports where pressure is already heavy. However, most importers will not have to pay VAT on the spot. They will be able to defer it in the same way as Customs duties. During the period up to 1 October Customs will be discussing the problems with trade interests, to iron out practical difficulties. Additional staff are being allocated to operate the new system.

FACT SHEET

26. VAT ON HOT TAKE-AWAY FOOD AND DRINK

Facts

- Hot take-away food and drink taxed at 15% from 1 May

- Revenue yield: £125 million (1984/5), £200 million (full year)

- RPI impact effect - about 0.1%, included in Budget forecast

Positive

- Extension of VAT base gives revenue needed for tax cuts elsewhere

- Will help to alleviate distortion between take-away and eat-in meals and snacks, both of which include a substantial service element

Defensive

- Food generally remains zero-rated

- Removes present difficult borderline between hot food eaten on the premises (taxable) and off (zero-rated)

- Raising (full year) revenue elsewhere would require eg extra 4p on a gallon of petrol

- Zero-rating of fish and chips would create distortion of competition and impossible borderline

- Continued zero-rating of cold take-aways desirable to avoid borderline problems with ordinary groceries

- No effect on UK own resources contribution

- 'Meals on wheels' generally provided by local authorities do not attract VAT - when provided to a local authority by a private contractor the local authority can recover the VAT

LINES TO TAKE

26. VAT ON HOT TAKE-AWAY FOOD AND DRINK

Taxing hot take-away food and drink will result in the same VAT treatment being applied to this area of expenditure as to other forms of catering, which have always been subject to the standard rate of tax.

There have been some suggestions in the press and elsewhere that the taxation of hot take-away food will give rise to anomalies. Inevitably there will be some potential borderline difficulties - no tax involving exemptions and reliefs can be without them. But these difficulties should not be exaggerated; the fact is that most people can recognise hot food when they see it or sell it.

POSSIBLE SUPPLEMENTARIES

Many fish and chip shops will be forced to close

I know that many proprietors of fish and chip shops are worried about the effect on their sales. The price increase is bound to have some effect, but I am sure that fish and chips will maintain their popularity despite the tax.

Why exclude cold take-aways?

The simple answer is that it would be difficult, if not impossible, to define the scope of such a provision in such a way as to avoid including a wide range of food which would more normally be regarded as ordinary grocery items.

The change will affect poor/working mothers/single parents more severely

We are aware that the relief for food is important to the less well-off and the majority of basic foodstuffs still enjoy relief. In the case of hot take-away food it is fair to say that the price charged reflects more than just the basic cost of the food. It inevitably includes an additional element to cover the higher cost of preparation and service. The change need not adversely affect the less well off because food generally, including convenience and other cold prepared food, is outside the scope of the extension.

Anomalies and borderline problems

While some food is taxed and some relieved, there are bound to be some borderline difficulties and people who find themselves on the wrong side of the borderline will regard themselves as being in an anomalous position. But these problems should not be exaggerated. The fact is that most people can recognise hot food when they see it. Moreover, Customs and Excise are holding discussions with interested trade associations to help iron out any technical problems they foresee.

Tax avoidance schemes

We know that the Press have had something of a field day in reporting schemes which are claimed to avoid tax in this area. Even if these schemes might work in theory, it is quite another matter whether they can be operated successfully in practice.

27 MOTABILITY

Line to take

Motability's concerns have been strongly expressed to the Chancellor, who is considering them.

Background

Motability, an independent charity set up with Government support with the aim of enabling the disabled to have personal use of a car by means of either leasing or special hire purchase. Under the scheme, recipients of mobility allowance use their allowance (£19 a week) to lease or purchase their cars.

In addition to relief from vehicle excise duty (which applies to recipients of mobility allowance) Motability enjoys relief from VAT payment on the purchase of cars for leasing (input tax on cars is normally blocked). It has pressed since 1976 for complete exemption from VAT and Car Tax on the vehicles it purchases, and for relief from VAT on leasing charges.

Motability was particularly disappointed by this year's Budget, and the Vice Chairman, Mr Jeffrey Sterling has made this clear to the Chancellor. Their concern is partly that the extension of VAT and Car Tax reliefs for vehicles only applies to specially designed or substantially adapted vehicles capable of carrying a person in a wheelchair or on a stretcher; very few of the cars they supply meet these criteria. Secondly the phasing out of first year allowance has a substantial effect on the rental Motability will have to charge. They have calculated that this year the initial rental would have to be increased from £19 to £248, next year to £449 and the following year to £783 to allow for the phasing out of the allowance. They are therefore pressing the case for some offsetting compensation through indirect tax relief.

It has not yet been decided what if anything should be done, and revised figures are currently expected from Motability. There are strong policy objections to relief from car tax on vehicles acquired by Motability or from VAT on cars sold under hire purchase. But the possibility of a concession on leasing was considered as a Budget lollipop and kept in reserve. This would be worth £2.48 per week, which over a three year rental would amount to £387. It would more than compensate for the first year effect of the capital allowance change.

28. WINE/BEER

Facts

- Beer increased by 2p per pint of average strength
- Table wine reduced by 18p a 70cl bottle
- Changes took effect on clearances from warehouse from midnight Budget Day
- Full year revenue yield from changes : + £180 million from beer; - £60 million from all wine/made-wine changes (NB fortified wines increased by 10p a bottle)

Positive

- Full year revenue yield from all drinks changes (+£145 million) equivalent to effect of across-the-board revalorisation
- Wine/beer duty ratio of 2.98:1 complies fully with European Court judgment
- Brewers Society quoted as saying the Chancellor had made a fair decision on wine and beer (FT 14 March 1984)

Defensive

- Alternative solutions could have required up to 7p on beer : 2p strikes fair balance between revenue needs and compliance with Court judgment
- Wine/beer ratio could not be phased : would have been open to legal action by wine importers under European Communities Act 1972
- Benefit to UK drinks industry in observing rule of law : discrimination against Scotch Whisky exports ended in France, and Italy has undertaken to remove discrimination in line with Court rulings
- Solution favours claret over beer but change essential and balance struck by Chancellor widely welcomed as "fair"

LINES TO TAKE

28. WINE/BEER

It is in the interests of the UK drinks industry that the rule of law in this field should be observed: our important Scotch whisky industry gains much from the removal of discriminating taxation in the European Community. Change in the relative taxation of wine and beer was therefore inevitable. There were many options open to the Government but the one chosen by the Chancellor struck the right balance between revenue needs and compliance with the European Court judgment. It is significant that the solution has been widely welcomed as 'fair' by all sides of the drinks industry.

POSSIBLE SUPPLEMENTARIES

Why didn't the Government phase implementation of the Court judgment?

Phasing would not have been appropriate: it would have been open to legal action by wine importers as being contrary to the European Communities Act 1972.

What action has Italy taken to comply with Court judgments on discrimination against Scotch whisky?

As my rt. hon. Friend said in his Budget statement: the Italian Government have given us an undertaking that they will comply with earlier Court rulings on discrimination against Scotch whisky. We are awaiting the precise details of how they intend to change the relative taxation of Scotch whisky and other spirits.

[NB. FURTHER INFORMATION MAY BE TO HAND BY THE TIME OF THE SECOND READING DEBATE]

29. FUTURE INTENTIONS ON VAT

FACT SHEET

(i) Just over half of consumer expenditure is subject to VAT at standard rate of 15%.

(ii) The main items currently zero-rated are food, books, newspapers etc, fuel and power, new building, transport and young children's clothing.

(iii) The UK has the narrowest VAT base in the EC. Most other EC countries (except Ireland) give relief through exemptions (ie <u>not</u> zero-rating) and by lower, but positive, tax rates.

(iv) The Commission has threatened infraction proceedings on certain zero-rates (notably commercial construction), but they have taken no formal action as yet.

(v) Government well aware of the importance of many of the remaining zero-rated items to families and the less well-off and would not contemplate lightly any move that imposed a heavy burden on ordinary family budgets. But can make no commitment to retain the VAT structure in its present form.

29. FUTURE INTENTIONS ON VAT

LINES TO TAKE

General

We must continue the process of shifting the burden of taxation from earnings to spending if we are to make further worthwhile cuts in direct tax. The UK has a very narrow VAT base compared to most other EC countries - just under half of consumer expenditure is not subject to VAT - and although we would not contemplate lightly any move that imposed a heavy burden on ordinary family budgets we can make no commitment to retain the VAT structure in its present form.

Will you give a commitment that food will not be taxed

We have no plans at present to extend the tax to food, but nevertheless we could not give any permanent commitment.

Will the Government succumb to EC pressure to abandon zero rates

No. The Government will continue to resist any attempt by the Commission to force us to phase out our zero-rates. But that is not a commitment to retain all existing zero-rates indefinitely.

FACTSHEET

8. CONSTRUCTION:

VAT ON BUILDING ALTERATIONS

Facts

- Alterations to existing buildings taxed at 15% from 1 June

- Revenue yield : £250 million (1984/5), £450 million (full year)

- RPI impact effect - nil (alterations not in index)

Positive

- Extension of VAT base gives revenue needed for tax cuts elsewhere

- Removes absurd borderline between (taxed) repairs/maintenance and (untaxed) alterations

- Progressive

Defensive

- ¾ of construction industry output still zero-rated or tax deductible by purchaser

- Not result of EC pressure

- No effect on UK own resources contribution

- Raising (full year) revenue elsewhere would call for eg extra 5p on a pint of beer

- (Black economy) maybe increased incentive to fraud, but this part of VAT base now easier to police (no blurred borderlines)

- Building alterations taxed in rest of EC

- Zero-rating still available for construction which amounts effectively to new buildings: eg use of an existing facade would be zero-rated as a new building, but where more was retained the case would have to be considered on its merits.

LINES TO TAKE

8. CONSTRUCTION: VAT ON BUILDING ALTERATIONS

The extension of the VAT base to building alterations is a central part of my rt. hon. Friend's strategy of switching from taxes on earnings to taxes on spending. The economic effects on the construction industry should be much less severe than has been suggested as about three quarters of construction industry output will continue to be either zero-rated or tax deductible by the purchaser. The construction industry will also benefit from other Budget measures particularly the reduction in the rate of stamp duty and the abolition of NIS.

POSSIBLE SUPPLEMENTARIES

Taxing building alterations will damage heritage by encouraging demolition as opposed to renovation.

Various concerns have expressed fears about this, but I can assure the House that where all that is left of an existing building is one wall such as a front facade, a building making use of that single wall would be zero-rated as a new building. Where more of a building is retained the case would have to be considered on its merits. However, to provide a special relief for all historic or listed buildings is just not on.

The proposals will encourage the black economy.

It is true that there may be an increased incentive to evade the tax, but the removal of the unclear borderline between alterations and repairs will make this very much easier to tackle.

The starting date should be deferred.

The 1 June date offers considerable scope for the construction industry and its clients to mitigate the effects of the tax. Any work paid for by 1 June, even if it has not been started, will not be charged with VAT. Even with a later date not all of the problems would be solved, and revenue needed to finance desirable measures elsewhere would be lost.

<u>The proposals will inhibit local authority spending.</u>

Local authorities will be able to reclaim VAT on their purchases of alteration services.

<u>The proposals will have a particularly severe impact on charities and the disabled.</u>

It is not possible to provide a general relief for building alterations for the disabled or charities as this would be expensive, would lead to pressure for other reliefs (eg repairs) and would defeat the objectives of greater simplicity. Nevertheless the Government has decided to extend the VAT reliefs available to handicapped people to include certain alterations to buildings designed to facilitate access for handicapped people.

FROM: MISS J C SIMPSON
DATE: 4 APRIL 1984

PS/Chief Secretary

cc PS/FST
PS/MST
PS/EST
Mr Cassell
Mr Monck
Mr Monger
Mr Battishill
Mr Folger
Mr R I G Allen
Mr Griffiths
Mr Martin
Mr Lord
PS/IR
Mr Kucyze - IR
PS/C & E
Mr Wilmot - C & E

FINANCE BILL SECOND READING DEBATE: CHIEF SECRETARY'S SPEECH

As I told you on the telephone this morning, the Chancellor has a couple of structural comments on the draft speech attached to Mr Martin's minute of 3 April:-

a. para 18 should be omitted: if the Government is attacked for lack of consultation during the course of the debates, the Financial Secretary could say something about it in his wind-up speech;

b. paras 34 and 35 on the poverty and unemployment traps should come earlier on. He suggests immediately following the present para 29. He also suggests that the text needs to be substantially strengthened, along the lines of the paper which Mr Monger has just produced for forwarding to the TCSC.

JS

MISS J C SIMPSON
Private Secretary

~~Mr~~ Max Wilkinson's hostile round-up in Saturday's FT (page 1). The CST will need to be aware of this — & prepare rebuttal.

2. He is, of course, keen that F v. D is kept in the speech. But do we really have to say X? This could well [illegible] against us, & we know [illegible] [illegible] this. [illegible] very clear [illegible] [illegible] better to omit this statistic & state the general principle with statistics instead. [illegible]

FROM: JOHN GIEVE

6 April 1984

MR MARTIN

cc
PS/Inland Revenue
Mr Kucyzs - IR
PS/Customs & Excise
Mr Wilmott - C&E
Mr Isaac - IR
Chancellor
Financial Secretary
Economic Secretary
Minister of State
Mr Cassell
Mr Monck
Mr Monger
Mr Battishill
Mr Folger
Mr R I G Allen
Mr Hartley
Mr Griffiths
Mr Lord
Mr Portillo
Mr Makeham

C/ Note pp. 12, 14A-B, 20 (F v. D - the IR objected violently to the [illegible] of their original drafts so this has been altered again) poverty trap

FINANCE BILL SECOND READING DEBATE

I attach a further revised draft of the Chief Secretary's Speech reflecting most of your suggested amendments and other comments.

2. The Chief Secretary will work on this over the weekend. It will need to be shortened and he will consider how best that could be done.

3. Any further comments by lunchtime on Monday please.

JG

JOHN GIEVE

SECOND READING FINANCE BILL

INTRODUCTION

A month ago, when Mr RHF presented his Budget to the House he set it in the framework of a financial strategy for this Parliament and beyond. I cannot recall a Budget in recent years that has received a more enthusiastic response and that was the more remarkable because it was not a "give away" Budget but a Budget that took forward the firm financial policies we have applied since 1979. What rightly caught the imagination of the House and the commentators was the combination of that firmness of the purpose on financial strategy and the radical and imaginative reform of our tax structure.

The debate that followed the Budget rightly concentrated on the broad strategy but we start today on the more technical and prosaic process of examining the Finance Bill. In full this runs to 123 Clauses and 23 Schedules. I do not intend to take the House through them one by one but rather to show how they reflect the main themes from the Budget.

I should point how at the outset, however, that this year's Finance Bill contains rather more than the Budget proposals. Because of the General Election last year, it includes a number of the provisions introduced originally in the 1983 Bill. As a result, some 44 Clauses and 10 Schedules - nearly half the total Bill - have already been the subject of public consultation. I am sure our debates in the coming weeks will be better informed as a result.

We are fortunate today to have available the Treasury and Civil Service Select Committee's report on the Budget. I am sure that the House will wish to join me in congratulating the RHG for Worthing and the members of the Committee on producing the document so speedily. Naturally the House will wish to study it carefully. Whilst I may not be able to agree with all the Committee say, I was encouraged that they found a number of measures in my RHF's Budget both imaginative and welcome. I shall come to some of these later.

The Economic Background

The Budget was indeed imaginative and radical. But the reforms were set within the financial framework we have pursued over the last 5 years and are determined to continue. We shall continue to reduce the rate of monetary growth and the level of public borrowing as a proportion of national output. This will maintain the pressure to reduce inflation and interest rates and thus to provide the financial stability which is vital to our private enterprise economy.

At the same time, we intend to maintain firm control of public expenditure. This should permit reductions in taxation in the coming years and that in turn will improve incentives and assist the continuing improvement in the 'supply-side' performance of our economy.

In these ways, the Budget provides the basis for the sustained non-inflationary growth that has been the aim of all Governments since the war.

It is three years now since the trough of the Economic Recession. By the end of 1983, output was some 7½ per cent above its low point in 1981 Over a similar period, total fixed investment was up over 11%. Manufacturing productivity is also more than 11% higher than its pre-recession peak. At the same time, inflation has continued to fall and so have interest rates. This progress has been punctuated by debates in this House during which successive Opposition spokesmen have sought to argue that the Economy wasn't recovering, or, if it was, that the recovery was about to stop.

Well the evidence continues to accumulate that the Economy is growing strongly and the prospect is good. In the last month, we have seen:

(a) a cut in UK bank base rates, which are now at their lowest level for six years. At the same time US prime rates have risen. Our short term interest rates are now some 1½% below these in New York;

(b) a 1% cut in mortgage interest rates;

(c) the publication of the figures for exports in February which - at over £6 billion - were an all time record and included very encouraging figures for manufactured exports;

(d) the latest CBI monthly trends enquiry confirmed widespread recovery in manufacturing with expected increases in manufacturing investment of about 8% in both 1984 and 1985;

(e) there has been continuing good news on inflation with retail prices up only 5.1 per cent in the year to February;

(f) figures for the last quarter half of 1983 which confirm a healthy and necessary rise in company profits. /Industrial and commercial companies' profits in 1983 were about 20 per cent higher in real terms than in 1979./

In the light of these figures, I think there is general agreement that the Government's forecasts on both output and inflation are realistic and reasonable. Outside forecasters who claimed 6 months ago that the Treasury was over-optimistic are bringing their own forecasts closer into line with ours.

On the jobs front, there has been an increase in the employed labour force over the last year and that trend should continue. The formation of jobs in a growing economy will be encouraged by the impact of the individual Budget measures, notably the abolition of the National Insurance Surcharge. However the recent figures for unemployment are undoubtedly disappointing. Like our predecessors in other governments, we do not make predictions of unemployment and I am not going to guess now when unemployment will turn down. But I would emphasise this. Sustained improvement of the employment situation can only result from sustained economic growth and that depends above all on a vigorous, confident, and enterprising private sector.

We will no doubt hear again today calls for extra public spending and a 'so called' fiscal expansion. The RHG for Hillhead will no doubt argue that the PSBR should be £1 billion bigger than we plan. Perhaps the RHS for Sparkbrook will suggest a somewhat higher figure. We believe that the figure of £7¼ billion is right. This is not the occasion to repeat the arguments we have had on the point. But nobody - not even its most ardent advocate - believes that traditional fiscal reflation is the answer to the unemployment problem. What matters in the long term is the strength of our private sector and its ability to compete successfully at home and abroad. That strength will not be produced by any short term boosts that Government can arrange. There is no certain route to success but the best and essential aim for Government must be to engender confidence in the prospects for even lower inflation by producing a stable financial framework and to do what it can in the tax field as in others to encourage enterprise, enabling the economy to function better and setting business on the road to profitable expansion.

Those are the main themes of this Budget. That is why this is a Budget which improves the prospects for jobs.

Finance Bill Themes

It is the implementation of the Budget strategy in the tax field that is the heart of this Bill. There are two main themes:

i) a modest shift from taxing people's income to taxing their spending through an extension of the VAT base on one hand and an impressive real increase in basic income tax allowances on the other; and

ii) a simplification of the tax system intended to remove undesirable distortions notably in the field of corporate taxation but not restricted to that.

I hope it will help the House if I follow the general ordering of the Bill in exemplifying these themes and bringing out the major points of interest.

In Chapter 1 we propose to raise most excise duties in line with inflation with the exception of tobacco and the balance between wine and beer duties. Our proposals have generally been accepted as fair. Within that general approach might I mention Clause 5 which proposes the exemtpion from vehicle excise duty of recipients of the war pensioners mobility supplement and Clause 8 which (with Schedule 4) provides for the freeports foreshadowed in the Budget speech last year and announced in February.

The next Chapter deals with VAT, in particular the extension of VAT to ~~holding~~ building alterations and hot take away food and drink.

Of course, no-one welcomes the imposition or extension of any tax and I am under no illusions on that. But it is important to look at the matter in the round. First the total yield from the extending VAT to these areas of consumer spending will be £650m in a full year, meeting a considerable part of the cost of the increase in income tax allowances above inflation. Those increases will be of great benefit especially to those on low incomes, and VAT itself is not a tax on the poor - nor are these extensions. VAT remains to quote one of my distinguished predecessors the Noble Lord Barnett, "mildly progressive".

Second, even after these changes, only half of consumer spending will be subject to VAT in the UK, the lowest proportion in Europe.

Third, the extensions we have announced will both remove difficult borderlines which have been a source of confusion and anomaly. There is little rhyme or reason in the present distinction between take-away food and food eaten on the premises. The extension of VAT will permit fairer competition between different forms of catering. There is really no sensible reason for taxing a hamburger consumed inside MacDonald's at 15% but exempting those eaten on the pavement outside-

Of course, every borderline has its difficulties and the press has had a field day in conjuring up images of cold chips and warm bread. They are entitled to their fun but the reality is not like that of course. The public can readily understand the distinction between cooked food eaten in a cafe or taken away and raw materials bought at a shop. But I can assure the House that Customs & Excise are very ready to give guidance on cases of genuine doubt.

Omit, I'd suggest.

/In fact I was amused to see that they drew my attention to the fact that hot pies - and possibly leaks - will be subjected to tax if they are deliberately aimed at the take away trade by, for example, being sold from a hot cabinet./

The extension of VAT to building alterations will also remove a major source of confusion by eliminating the borderline between repairs and alterations which has been the source of a great deal of unproductive litigation in the past. It has also made it very difficult to tackle the evasion of VAT in the construction field. For that reason, I do not believe the change will give the great boost to the black economy that some honourable Members have suggested.

Nor does the existing division have much to recommend it. At present, for example, replacing a roof can sometimes count as a repair and sometimes as an alteration while rebuilding a wall counts as repair. Rewiring a house counts as a repair, while adding an additional socket to an existing ring main would be an alteration. Similarly, adding an additional radiator to an existing central heating system is an alteration, while replacing the central heating boiler is a repair or maintenance.

I do not expect the building industry to applaud this measure but I do ask them to see it alongside other elements of the Budget which will be of great benefit to their industry - the abolition of NIS, the reform of corporation tax, the cut in stamp duty and development land tax, in particular.

No doubt the House will wish to consider the detail of the extensions in Committee. But I would like to take this opportunity to mention two minor extensions to VAT reliefs. First, the relief for lifeboats is being extended to lifeboat carriage and launching equipment supplied to the Royal National Lifeboat Institution. This is a change for which the Institution pressed strongly before the Budget and I am sure the House will generally welcome it. Second, my HF, the Minister of State, has announced that the existing VAT zero-rating and relief from car tax for "personal ambulances" is being extended to cover all family cars designed or adapted to carrying a handicapped person in a wheel-chair or on a stretcher. While this extension does not go as far as some honourable Members would like, it is a useful measure in itself and dispenses with the former restriction that to qualify the zero-rating a vehicle should have no seats behind the driver.

Clauses 17 to 21 are a goldmine - they contain some of the brightest nuggets of this Budget - income tax and corporation tax. First income tax.

Increase in Thresholds

The revenue obtained from broadening the VAT base has been used to help raise the basic income tax allowances, set out in Clause 21. The increase of about 12½% in the basic allowances is some 7 percentage points more than required to meet statutory indexation provisions. It is one more step in a course we have pursued since 1979 and intend to continue in future years. Basic income tax thresholds are now some 16% higher in real terms than they were in 1978-79.

Indeed, some HMs will recall that it was Conservative votes that put ~~even~~ the indexation provisions on the Statute Book and that was done against the opposition of the then Labour Government - although we were joined on that occasion by the HM for Perry Barr. I am sure he applauds our continued progress since then.

But while we have made some progress to taking the low paid out of tax, we need and intend to go further.

So far as there has been criticism of this part of the Budget it has been that we should have used the funds not to increase the thresholds but to increase Child Benefit.

... child benefit. The argument is that this is a more effective way of tackling the poverty and unemployment traps. Of course, no decision has been made about the level of child benefit from November: that will be decided at the proper time, as we have told the House before. But, leaving that aside, I detect a good deal of misunderstanding, if not confusion, in discussion of the poverty and unemployment traps. And I would like to spend a few moments examining the facts.

Let me start with the poverty trap. What most people mean by this is the situation where low-paid workers may be paying income tax and receiving means-tested benefits at the same time. Consequently, if they earn more, the effect of income tax and loss of benefit may mean that their net income hardly rises at all, and may even fall. Marginal rates in this sense are highest where there is an overlap between income tax, national insurance contributions and family income supplement - FIS.

So how can we ease the problem for these people? Increasing child benefit by itself has no effect on marginal rates in the poverty trap. It does not affect either the rate at which tax is charged or at which means-tested benefits are withdrawn. Nor does an increase in child benefit reduce the numbers in the trap. It neither changes the number of taxpayers nor the number of recipients of means-tested benefits. Only when higher child benefit is accompanied by a reduction in means-tested benefits is the number of families in the poverty trap reduced. In practice, what this means is reducing the prescribed amounts for FIS so that some families lose their entitlement to FIS altogether.

But, of course, there is an inevitable corollary. Families removed from the trap in this way see no improvement in their net income even though child benefit goes up. The poverty trap is improved, but only by denying families taken out of it the extra child benefit going to families who are better off.

By contrast, raising tax allowances has two advantages. It frees some families from the poverty trap by taking them out of tax altogether. And it does so in a way that enables them to benefit from the tax reductions available to other people.

The simple fact is that increasing child benefit rather than tax allowances would leave these families worse off than under my rt hon Friend's Budget. And there is a second, important, point. Compared with raising tax thresholds an increase in child benefit would actually have worsened the unemployment trap for families affected, because of the reduction in FIS. And, of course, raising child benefit rather than tax thresholds would have done nothing for all those without children. These represent 85 per cent of the unemployed. In sharp contrast, raising tax allowances increases net income from work right across the board. So, far from worsening the unemployment trap, this improves it for everyone.

So much for the criticisms of my rt hon Friend's priority in raising tax thresholds. Let me now put some numbers to what I have said. Altogether, only six million families stand to receive an increase in child benefit, compared with twenty million families and single people who gain from higher tax allowances. Without the real improvement in tax allowances in the Budget some 400,000 people - including 100,000 married men and 15,000 single parents, would have remained in the tax net this year. Instead they will now be below the threshold.

No-one pretends there is an easy solution to the poverty and unemployment traps. But raising tax allowances provides effective help, and does so in a way which helps very large numbers living on low incomes.

Next I turn to the measures designed to remove distortions and simplify the structure of company taxation.

Clause 18 of the Bill provides for the progressive reduction in the main rate of corporation tax to 35% by 1986-87, Clause 20 provide for the immediate reduction of the small firms rate to 30%. Clause 47 abolishes stock relief, Clause 57 and Schedule 12 provide for the progressive removal of first year and initial capital allowances and their replacement by a system of writing-down allowances has been regretted in some quarters. But as the CBI and others have made plain, the package as a whole is an attractive one for companies, for two main reasons. First, businessmen prefer a system of tax with low rates and few and simple reliefs to one with high rates offset by complex and indiscriminate reliefs. I am sure they are right to do so. It is in no-one's interest for decisions on investment projects to depend so much on the details of tax legislation and the advice of tax lawyers rather than the commercial appraisal and the business acumen of those engaged in manufacturing and trade.

For too long, businessmen have found their plans judged on tax implication and their sighs of relief when these measures were announced were reflected, I note, in the welcome given to these measures in evidence to the Select Committee. /For example, the General Secretary of the TUC said that "there are a lot of nonsenses in the way corporation tax has operated" and that the TUC "would not argue with the need to reform the structure of corporation tax", while Sir James Cleminson of the CBI said that "the new tax system will be more favourable than the old" and that the Budget "has made it more possible for business to achieve the growth that we need"./

The reduction in UK corporation tax rates leave them at a level below that of most of our developed competitors both in Europe and in America. The UK will become a good place to make a profit and not a place to make a loss as it has been in the past. This will be good for business, good for enterprise and good for jobs.

The stark fact is that the system of generous tax incentives for capital investment we have had in this country has not lived up to expectations. ~~Of course,~~ The level of UK investment has been well up to that of our main competitors - with such generous tax subsidies it would be surprising if that were not so. But the returns from that investment have been significantly lower than in competitor countries. In future companies will need to pay more attention to the real profitability of investment and less to tax considerations. And with the abolition of NIS too, they need no longer do so against a fiscal bias in favour of capital investment and against jobs.

In order to give business the certainty they need to plan investment, we have taken the unusual step of including in these Clauses provisions for three years ahead.

Until the recovery over the last year or so, we have seen a decade of declinign profits for the private sector. This is now being reversed and the measures on corporation tax will help to sustain and accelerate that process.

Chapter 3 contains much else ~~of interest to companies. Indeed there are a number of changes~~ which should have long lasting benefits for companies. Share option schemes are improved in clauses 38 and 39. The new relief proposed for approved share options, by replacing the income tax charge with a capital gains charge on disposal of shares, should help companies in attracting and motivating the key managers on whom so much depends. The corporate finance package [Clauses 35, 36, 41, 62] includes a number of measures which should give companies greater flexibility in raising finance, giving a modest stimulus to a revival in the corporate bond market.

We will look at the detailed improvement s to the tax structure in the Bill in Committee. I would, however, pick out the minor improvements in capital gains tax (Clauses 61 to 69). These include a useful provision to allow gifts to heritage maintenance funds to be treated like other gifts, in Clause 66, as has been urged by the Historic Houses Association. The insurance sector is affected by Clauses 70 to 74; in particular the withdrawal of life assurance premium relief for new policies in Clause 70. The oil and gas industry is affected by improvements in the Corporation tax regime in Clauses 75 to 79, and by Clauses 109 to 112 which include minor changes in petroleum revenue tax.

The next two lengthy sections of the bill are devoted to legislation to counter abuse. Clauses 80 to 89, together with Schedules 16 to 18, deal with controlled foreign companies. Clauses 90 to 97, and Schedules 19 and 20, are concerned with offshore funds. Both those major pieces of legislation were subject to full consultation in advance. As a result, the controlled foreign companies provisions have been substantially modified, while we will be bringing forward amendments on offshore funds at Committee stage.

In this context I should also touch on the implications on the recent decision of the House of Lords in Furniss v Dawson. Following on the decisions in Ramsay, the whole principle established in the 30s in the Duke of Westminster's case that the courts should look at the form rather than the substance for transaction must now be regarded as largely invalid.

No X It is too early to state with complete confidence how the principle in Furniss v Dawson will be applied. I can however say that it does not in any way call in question the tax treatment of straightforward commercial transactions. Nor is there any question of the Inland Revenue challenging the tax treatment of covenants, leasing transactions, and straightforward transfers of assets between group members. We will also see how far practice rules can be devised and stated for the guidance of taxpayers and their advisers.

Better to open the door with something like this

The principle in Furniss v Dawson should lead in future to a greater simplicity in our tax system and will I hope enable us over a course of time to prune out provisions which own their existence to the complexities of a high rate - some might say a confiscatory rate - tax system with a multiplicity of special reliefs. I am sure the whole House would welcome that.

~~The need to counter tax abuse reflects the complexity of our tax system and creates that complexity itself. The main route to greater simplification is that adopted in the Budget measures. Namely to reduce rates of taxation and, at the same time to remove reliefs which were required only because of the high rates.~~

The changes we propose in capital transfer tax, Clauses 98 to 104, and stamp duty, Clauses 105 to 108, reflect our determination to simplify the system and lighten the burden of tax. We shall be returning to CTT but the simplification and reduction in top rates of CTT improve the situation meanwhile. The changes in development land tax similarly improve the incidence of taxation and will assist industrial and commercial development.

But this Finance Bill hasn't just changed the structure and simplified. It has abolished taxes too. The Finance Bill does not mention excise duties on kerosene or the Investment Income Surcharge. They have gone.

The abolition of the Surcharge ~~will~~ should not be lamented. It ~~It~~ discrimated against investment and was an unfair impost on many retired people who could not by any stretch of the imagination be called rich. It was particularly damaging in that it discriminated against those who had retired from self-employment with no prospect of a company pension and who had to rely on income from the proceeds of selling their businesses or professional practices.

Finally this Bill sees the end of the National Insurance Surcharge in Clause 113. I will not labour the case for its abolition. It never had many enthusiastic supporters even in the desperate times of the last Labour Government. However, I would like to repeat that the reduction of this tax on jobs since 1979 from 3½ per cent to 0 per cent is worth some £3 billion a year to employers and has removed a major inducement to employers to keep down employment.

Conclusion

I hope that the whole House will applaud the objective of the system of direct taxation based on lower rates and a simpler structure. It was inevitable that in a neutral Budget the Chancellor had put to balance the reliefs offered against extensions in other areas. I ask the House, to view the Finance Bill in the round, to recognise what it might achieve. To see it as another step in a continuing process of reform. On that basis I ask my HFs to secure for it a second reading tonight.

10-15

FROM: P MAKEHAM
DATE: 6 APRIL 1984

1. MR BATTISHILL
2. MR HUDSON

cc PS/Chancellor
PS/Chief Secretary
Mr Monger
Mr Scholar
Mr Folger
Mr Ridley o/r
Mr Lord o/r
Mr Portillo

FINANCE BILL SECOND READING: FINANCIAL SECRETARY'S WIND-UP SPEECH

You asked for a short piece which could be used to tackle Sir Ian Gilmour in case he repeats his criticisms made in the Budget debate.

2. The attached draft deals with the "strategy" he put forward. He did not specifically propose demand management but a piece is attached should he return to the fiscal reflation theme.

Peter Makeham

P MAKEHAM

SIR IAN GILMOUR

STRATEGY

My RHF the member for Chesham and Amersham repeated the criticisms he made in the Budget debate. I looked back at his speech in search of his alternative strategy. In vain. He has no strategy. What he proposes is a string of unrelated points

- he wants an increase in investment. So do I and we have it, investment in 1983 was over 10 per cent higher than in 1981 and is expected to increase by over 6 per cent in 1984
- he wants a climate of good will with trade unionists; so do I but I do not expect that to prevent inflation. I remember Mr Solomon Binding's past efforts
- he wants international co-operation; so do I but that should not distract us from competing in world markets.

FISCAL REFLATION

The idea that unemployment can somehow be cured by means of a "stimulus to demand" simply ignores the lessons of history. What are the facts? During the 1970s, under the impetus of so-called demand-management, total money GDP grew by 312 per cent yet output rose by only 25 per cent. In this recovery there is a very much healthier division between inflation and real growth; in 1983, total money incomes grew by about 8 per cent of which 3 per cent represented real growth in output.

Everyone recognises that our recovery started in 1981. This is important because in 1981-82 the PSBR was substantially lower as a percentage of GDP than it had been in the immediately preceding years: 3½ per cent compared with 4¾ per cent in 1979-80 and 5¾ per cent in 1980-81. This sharp reduction in the PSBR as a percentage of GDP has been sustained in subsequent years. The timing of the recovery is consistent with our view that it has been generated primarily by lower inflation and by the accompanying reduction in interest rates. It is simply not consistent with the view that the recovery was brought about by a process of fiscal relaxation.

2.72

(puf)

FROM: MISS J C SIMPSON

DATE: 9 April 1984

cc PS/Financial Secretary
PS/Minister of State
PS/Economic Secretary
Mr Cassell
Mr Monck
Mr Monger
Mr Battishill
Mr Folger
Mr R I G Allen
Mr Hartley
Mr Griffiths
Mr Martin
Mr Lord
Mr Portillo
Mr Makeham
PS/IR
Mr Isaac - IR
Mr Kucyzs - IR
PS/C&E
Mr Wilmott - C&E

PS/CHIEF SECRETARY

FINANCE BILL SECOND READING DEBATE

The Chancellor has seen the latest draft of the Chief Secretary's second reading speech attached to your minute of 6 April, and has two comments - one general and one particular - to offer. The general is to draw the Chief Secretary's attention to Max Wilkinson's piece on the front page of Saturday's Financial Times. There is, of course, a standard rebuttal to this. The particular point relates to the passage on Furniss and Dawson. The Chancellor is clear that the reference to this should stay in the speech, but he is very unhappy at the idea of saying, as the opening sentence of the final paragraph on page 20 does, that "it is too early to state with complete confidence how the principle in Furniss v Dawson will be applied". He thinks this would be of no help at all in ending speculation about what exactly the implications of the judgement are, and that at the very least, it would be better to omit the sentence and start the paragraph with something on the lines of the final sentence instead.

JS

MISS J C SIMPSON

(pup)

CHIEF SECRETARY TO THE TREASURY

FROM: J GIEVE
DATE: 10 April 1984

MR MARTIN

cc Chancellor
Financial Secretary
Economic Secretary
Minister of State
Mr Cassell
Mr Monck
Mr Monger
Mr Battishill
Mr Folger
Mr R I G Allen
Mr Hall
Mr Monaghan
Mr Smee
Mr Griffiths
Mr Lord
Mr Portillo
Mr Makeham

PS/Inland Revenue
Mr Kucyzs - IR
PS/Customs & Excise
Mr Wilmott - C & E

FINANCE BILL SECOND READING DEBATE

I attach the final draft of the speech tonight. It should be checked against delivery.

JG

J GIEVE

FINANCE BILL THEMES

IT IS HOWEVER THE IMPLEMENTATION OF THE BUDGET STRATEGY IN THE TAX FIELD THAT IS THE HEART OF THIS BILL. THERE ARE TWO MAIN THEMES:

(i) A MODEST SHIFT FROM TAXING PEOPLE'S INCOME TO TAXING THEIR SPENDING THROUGH AN EXTENSION OF THE VAT BASE ON THE ONE HAND AND AN IMPRESSIVE REAL INCREASE IN BASIC INCOME TAX ALLOWANCES ON THE OTHER; and

(ii) A SIMPLIFICATION OF THE TAX SYSTEM AND THE REMOVAL OF UNDESIRABLE DISTORTIONS - PARTICULARLY IN THE FIELD OF CORPORATE TAXATION BUT NOT RESTRICTED TO THAT.

I HOPE IT WILL HELP THE HOUSE IF I FOLLOW THE GENERAL ORDERING OF THE BILL IN EXEMPLIFYING THESE THEMES AND BRINGING OUT THE MAJOR POINTS OF INTEREST.

IN CHAPTER 1 WE PROPOSE TO RAISE MOST EXCISE DUTIES IN LINE WITH INFLATION - WITH THE EXCEPTION OF TOBACCO AND THE BALANCE BETWEEN WINE AND BEER DUTIES. I HOPE THE HOUSE WILL

ACCEPT OUR PROPOSALS AS FAIR.

WITHIN OUR GENERAL APPROACH I WOULD LIKE TO DRAW THE HOUSE'S ATTENTION TO CLAUSE 5 WHICH PROPOSES EXEMPTION FROM VEHICLE EXCISE DUTY OF RECIPIENTS OF WAR PENSIONERS' MOBILITY SUPPLEMENT AND CLAUSE 8 WHICH PROVIDES FOR THE FREEPORTS FORESHADOWED IN THE BUDGET SPEECH LAST YEAR AND ANNOUNCED IN FEBRUARY.

THE NEXT CHAPTER DEALS WITH VAT - IN PARTICULAR THE EXTENSION OF VAT TO BUILDING ALTERATIONS AND HOT TAKE-AWAY FOOD AND DRINK.

OF COURSE IT WOULD BE NAIVE TO IMAGINE THAT THE IMPOSITION OR EXTENSION OF A TAX IN THIS WAY WILL BE UNIVERSALLY WELCOMED. BUT I HOPE THAT THE HOUSE AND THE COUNTRY WILL LOOK AT THE MATTER IN THE ROUND . FIRST I SHOULD EMPHASISE THAT THE TOTAL YIELD FROM THESE EXTENSIONS WILL BE £650 MILLION IN A FULL YEAR, MAKING IN OTHER WORDS A MAJOR CONTRIBUTION TO THE COST OF INCREASING THE INCOME TAX THRESHOLDS. I SHOULD ALSO EMPHASISE - RETURNING TO A POINT WHICH WAS MUCH DEBATED IN THE SUMMER OF 1979 - THAT VAT IS NOT A TAX ON THE POOR, NOR IS IT A TAX ON NECESSITIES. VAT REMAINS, TO QUOTE ONE OF MY DISTINGUISHED PREDECESSORS, THE NOBLE LORD BARNETT, "MILDLY PROGRESSIVE". AGAIN, EVEN AFTER THESE CHANGES, ONLY HALF OF CONSUMERS' SPENDING WILL BE SUBJECT TO VAT IN THE UNITED KINGDOM - THE LOWEST PROPORTION IN THE EUROPEAN COMMUNITY.

THE EXTENSIONS WE HAVE ANNOUNCED WILL BOTH REMOVE DIFFICULT BORDERLINES WHICH HAVE BEEN A SOURCE

OF CONFUSION AND ANOMALY. THERE IS REALLY NO SENSIBLE REASON FOR TAXING A HAMBURGER CONSUMED INSIDE MACDONALDS OR WIMPEY AT 15 PER CENT, BUT ZERO-RATING THOSE EATEN OUTSIDE. OF COURSE EVERY BORDERLINE HAS ITS DIFFICULTIES AND THE PRESS HAS HAD A FIELD DAY IN CONJURING UP IMAGES OF COLD CHIPS AND WARM BREAD. NABARRO WOULDS'T THAT THOU HAD BEEN LIVING AT THIS HOUR! BUT I BELIEVE THAT THE PUBLIC CAN READILY UNDERSTAND THE DISTINCTION BETWEEN COOKED FOOD EATEN IN A CAFE OR TAKEN AWAY AND RAW MATERIALS BOUGHT AT A SHOP.

THE EXTENSION OF VAT TO BUILDING ALTERATIONS WILL ALSO REMOVE A MAJOR SOURCE OF CONFUSION BY ELIMINATING THE BORDERLINE BETWEEN REPAIRS AND ALTERATIONS. THIS HAS BEEN THE SOURCE OF A GREAT DEAL OF UNPRODUCTIVE LITIGATION IN THE PAST. WE HAVE BEEN TOLD THAT EVERY INCREASE OR EXTENSION OF VAT WILL BOOST THE BLACK ECONOMY. I HAVE TO SAY THAT BY REMOVING THESE DIFFICULT BORDERLINES THE CHANGES SHOULD MAKE IT EASIER TO TACKLE EVASION IN THE CONSTRUCTION FIELD.

I HAVE TO REMIND THE HOUSE THAT AT PRESENT, FOR EXAMPLE, REPLACING A ROOF CAN SOMETIMES COUNT AS A REPAIR AND SOMETIMES AS AN ALTERATION, WHILE REBUILDING A WALL COUNTS AS A REPAIR.

REWIRING A HOUSE COUNTS AS A REPAIR, WHILE ADDING AN ADDITIONAL SOCKET TO A RING MAIN WOULD BE AN ALTERATION. SIMILARLY, ADDING AN ADDITIONAL RADIATOR TO AN EXISTING CENTRAL HEATING SYSTEM IS AN ALTERATION, WHILE REPLACING THE CENTRAL HEATING BOILER IS A REPAIR OR MAINTENANCE.

I DO NOT EXPECT THE BUILDING INDUSTRY TO APPLAUD THIS EXTENSION, BUT I DO ASK THEM TO SEE IT ALONGSIDE OTHER ELEMENTS OF THE BUDGET WHICH WILL BE OF BENEFIT TO THAT INDUSTRY - THE ABOLITION OF NIS, THE REFORM OF CORPORATION TAX, THE CUT IN STAMP DUTY AND THE RAISING OF THE THRESHOLD FOR DEVELOPMENT LAND TAX, IN PARTICULAR.

I HAVE NO DOUBT THE HOUSE WILL WISH TO CONSIDER THE DETAILS OF THESE MEASURES IN COMMITTEE. BUT I WOULD LIKE TO TAKE THIS OPPORTUNITY TO MENTION 2 SMALL EXTENSIONS ON EXISTING RELIEFS.

FIRST THE RELIEF FOR LIFEBOATS IS BEING EXTENDED TO LIFEBOAT CARRIAGE AND LAUNCHING EQUIPMENT SUPPLIED TO THE ROYAL NATIONAL LIFEBOAT INSTITUTION.

SECOND, THE EXISTING VAT RELIEF FOR MOTOR VEHICLES DESIGNED OR ADAPTED FOR USE BY THE HANDICAPPED WILL BE EXTENDED, AND MATCHEDBY A NEW CAR TAX RELIEF. THE EFFECT WILL BE THAT NEITHER VAT NOR CAR TAX WILL APPLY TO FAMILY CARS DESIGNED FOR DISABLED PEOPLE OR SUBSTANTIALLY ADAPTED FOR THEIR USE.

CHRISTOPHER HAWKINS
HIGH PEAK

THESE WERE THE WORDS THAT MY RHF USED ON BUDGET DAY. FOLLOWING EXISTING PRACTICE, THEY WERE AMPLIFIED IN A PRESS STATEMENT BY THE CUSTOMS AND EXCISE ISSUED ON BUDGET DAY WITH MY RHF'S APPROVAL.

IT IS NOT MY RHF'S INTENTION THAT THE NEW RELIEF SHOULD COVER CARS WHICH ARE MERELY ADAPTED FOR THE USE OF A HANDICAPPED PERSON, FOR EXAMPLE BY THE PROVISION OF HAND CONTROLS OR WIDENED DOORS. I AM SORRY THIS IDEA HAS GAINED CURRENCY. THERE IS NO QUESTION OF CUSTOMS AND EXCISE HAVING TRIED TO CUT DOWN ON RELIEFS.

NOR I'M AFRAID COULD WE AGREE TO AN EXTENSION OF THE RELIEF IN SUCH A WAY. TO EXTEND VAT RELIEF TO ALL CARS USED BY DISABLED PEOPLE, OR TO CARS WITH ONLY MINIMAL ADAPTATIONS TO THE CONTROLS, WOULD BE VERY COSTLY AND WOULD OPEN THE WAY TO CONSIDERABLE ABUSE.

THE RELIEF IS DESIGNED TO COVER ALL FAMILY CARS DESIGNED OR SUBSTANTIALLY ADAPTED TO CARRY A DISABLED PERSON EITHER IN A WHEELCHAIR OR ON A STRETCHER WHETHER AS DRIVER OR PASSENGER. THE NEW RELIEF REMOVES THE FORMER RESTRICTION THAT THERE MUST BE NO SEATS TO THE REAR OF THE DRIVER AND THUS EXTENDS THE RELIEF TO ALLOW A DISABLED PERSON TO TRAVEL WITH HIS FAMILY OR FRIENDS - AS LONG AS THE CAR IS DESIGNED OR ADAPTED TO CARRY THE DISABLED PERSON IN A WHEELCHAIR OR ON A STRETCHER. RELIEF ON CAR TAX WILL APPLY SUBJECT TO THE SAME CONDITIONS.

INCOME AND CORPORATION TAX

I HOPE THAT I CAN SAY WITHOUT EXAGGERATION THAT CLAUSES 17 TO 21 ARE SOME OF THE BRIGHTER JEWELS IN THE BUDGETARY CROWN. FIRST, INCOME TAX.

INCREASE IN THRESHOLDS

THE REVENUE OBTAINED FROM BROADENING THE VAT BASE HAS BEEN USED TO HELP RAISE THE BASIC INCOME TAX ALLOWANCES. THE DETAILS ARE SET OUT IN CLAUSE 21. THE INCREASE OF ABOUT 12½ PER CENT IN THE BASIC ALLOWANCES IS SOME 7 PERCENTAGE POINTS MORE THAN REQUIRED FOR INDEXATION. IT IS ONE MORE STEP ON A PATH WE HAVE PURSUED SINCE 1979 AS RESOURCES HAVE PERMITTED AND INTEND TO CONTINUE IN FUTURE YEARS. BASIC INCOME TAX THRESHOLDS ARE NOW SOME 16 PER CENT HIGHER IN REAL TERMS THAN THEY WERE IN 1978-79.

INDEED SOME HMs WILL RECALL THAT IT WAS CONSERVATIVE VOTES THAT PUT THE INDEXATION PROVISIONS ON THE STATUTE BOOK. THAT WAS DONE AGAINST THE OPPOSITION OF THE THEN LABOUR GOVERNMENT - ALTHOUGH, AND OF COURSE I AM HAPPY TO PAY TRIBUTE TO HIM, WE WERE JOINED ON THAT OCCASION BY HM FOR PERRY BARR. I AM SURE HE APPLAUDS OUR CONTINUED PROGRESS SINCE THEN AND WILL SUPPORT US IN WHAT WE ARE DOING TONIGHT.

BUT WHILE WE HAVE MADE SOME PROGRESS IN TAKING THE LOW-PAID OUT OF TAX, WE NEED AND INTEND TO GO FURTHER.

THERE HAS BEEN SOME CRITICISM THAT WE SHOULD HAVE USED THE FUNDS AVAILABLE NOT TO INCREASE THE THRESHOLDS BUT TO INCREASE CHILD BENEFIT IN ORDER TO MAKE A BIGGER IMPACT ON THE POVERTY TRAP. I SHOULD STRESS, AS I STRESSED IN THE BUDGET DEBATE, THAT THE DECISION ABOUT CHILD BENEFITS WILL BE TAKEN AT THE PROPER TIME - AFTER THE MAY RPI FIGURES BECOME AVAILABLE IN JUNE.

BUT THERE IS I SUSPECT SOME MISUNDERSTANDING ABOUT THE INTERACTION OF CHILD BENEFIT AND TAX. I HOPE THE HOUSE WILL ALLOW ME TO EXAMINE BRIEFLY THE FACTS.

LET ME START WITH THE POVERTY TRAP - THE POSITION FACING SOME PEOPLE IN EMPLOYMENT WHO PAY INCOME TAX AND RECEIVE MEANS-TESTED BENEFITS AT THE SAME TIME. IF THEY EARN MORE - UP TO A CERTAIN POINT - THE LOSS OF BENEFIT COUPLED WITH INCREASED TAX MAY MEAN THAT THEIR NET INCOME HARDLY RISES - AND IN EXTREME CASES MAY EVEN FALL. THE MARGINAL RATES ARE HIGHEST FOR FAMILIES RECEIVING FIS.

AN INCREASE IN CHILD BENEFIT BY ITSELF WILL NOT TOUCH THIS PROBLEM. IT DOES NOT AFFECT THE RATE AT WHICH TAX IS CHARGED OR MEANS-TESTED BENEFITS WITHDRAWN. NOR WILL IT REDUCE THE NUMBER OF PEOPLE IN THE TAX/FIS TRAP.

ONLY IF AN INCREASE IN CHILD BENEFIT IS ACCOMPANIED BY A REDUCTION IN MEANS-TESTED BENEFITS WILL THE NUMBER OF FAMILIES IN THE TRAP BE REDUCED. IN PRACTICE THIS WOULD MEAN REDUCING THE AMOUNT OF FIS. BUT IF THAT WERE DONE, THEN THE INCOMES OF THE FAMILIES INVOLVED WOULD NOT RISE TO REFLECT THE INCREASE IN CHILD BENEFIT.- AND THAT APPROACH WOULD NOT IMPROVE THE UNEMPLOYMENT TRAP. I DOUBT WHETHER THAT IS WHAT ENTHUSIASTS FOR CHILD BENEFIT INTEND.

BY CONTRAST RAISING TAX ALLOWANCES HAS A NUMBER OF ADVANTAGES:

(a) IT RELIEVES SOME FAMILIES FROM THE POVERTY TRAP BY TAKING THEM OUT OF TAX ALTOGETHER.

(b) IT BENEFITS ALL TAXPAYERS, WHETHER OR NOT THEY ARE IN THE POVERTY TRAP, AND WHETHER OR NOT THEY HAVE CHILDREN - [AND 85 PER CENT OF THE UNEMPLOYED FOR INSTANCE HAVE NO CHILDREN] 6 MILLION FAMILIES RECEIVE CHILD BENEFITS. 20 MILLION FAMILIES AND SINGLE PEOPLE BENEFIT FROM AN INCREASE IN TAX THRESHOLDS.

(c) IT IMPROVES THE UNEMPLOYMENT TRAP BY RAISING INCOME FROM WORK ACROSS THE BOARD.

I DO NOT PRETEND THAT WHAT WE HAVE DONE SOLVES THE PROBLEM. BUT IT MAKES A REAL STEP FORWARD - A MORE EFFECTIVE STEP THAN AN EXCLUSIVE CONCENTRATION ON CHILD BENEFITS.

NEXT I TURN TO THE MEASURES DESIGNED TO REMOVE DISTORTIONS AND SIMPLIFY THE STRUCTURE OF COMPANY TAXATION.

CLAUSE 18 OF THE BILL PROVIDES FOR THE PROGRESSIVE REDUCTION IN THE MAIN RATE OF CORPORATION TAX TO 35 PER CENT BY 1986-87. CLAUSE 20 PROVIDES FOR THE IMMEDIATE REDUCTION OF THE SMALL COMPANY RATE TO 30 PER CENT. CLAUSE 47 ABOLISHES STOCK RELIEF. CLAUSE 57 AND SCHEDULE 12 PROVIDE FOR THE PROGRESSIVE REMOVAL OF FIRST YEAR AND INITIAL CAPITAL ALLOWANCES AND THEIR REPLACEMENT BY A SYSTEM OF WRITING DOWN ALLOWANCES. THIS HAS INEVITABLY BEEN REGRETTED IN SOME QUARTERS. BUT AS THE CBI AND TO AN EXTENT THE TUC - AND OTHERS HAVE MADE PLAIN THE PACKAGE AS A WHOLE IS AN ATTRACTIVE ONE FOR COMPANIES.

A SYSTEM OF CORPORATION TAX WITH LOW RATES AND FEW AND SIMPLE RELIEFS MUST BE PREFERABLE TO ONE WITH HIGH RATES OFFSET BY COMPLEX AND INDISCRIMINATE RELIEFS. IT IS IN NO-ONE'S INTEREST THAT DECISIONS ON INVESTMENT PROJECTS SHOULD DEPEND SO MUCH ON THE DETAILS OF TAX LEGISLATION AND THE ADVICE OF LAWYERS AND ACCOUNTANTS RATHER THAN THE COMMERCIAL APPRAISAL AND BUSINESS ACUMEN OF THOSE ENGAGED IN MANUFACTURE AND TRADE.

THE HOUSE WILL NOTE THAT THE GENERAL SECRETARY OF THE TUC IN EVIDENCE TO THE SELECT COMMITTEE SAID THAT

"THERE ARE A LOT OF NONSENSES IN THE WAY CORPORATION TAX IS OPERATED" AND THAT THE TUC " WOULD NOT ARGUE WITH THE NEED TO REFORM THE STRUCTURE OF CORPORATION TAX", WHILE SIR JAMES CLEMINSON OF THE CBI SAID THAT "THE NEW TAX SYSTEM WILL BE MORE FAVOURABLE THAN THE OLD" AND THAT THE BUDGET " HAS MADE IT MORE POSSIBLE FOR BUSINESS TO ACHIEVE THE GROWTH THAT WE NEED".

THE REDUCTION IN UK CORPORATION TAX RATES LEAVES THE LEVELS BELOW THAT OF MOST OF OUR DEVELOPED COMPETITORS BOTH IN EUROPE AND IN AMERICA. IT IS WORTH REFLECTING THAT THESE MEASURES COUPLED WITH THOSE IN CHAPTER VI ON CONTROLLED FOREIGN COMPANIES WILL MAKE IT MORE ATTRACTIVE TO TAKE A PROFIT HERE THAN OVERSEAS. THESE MEASURES WILL BE GOOD FOR BUSINESS, GOOD FOR ENTERPRISE AND GOOD FOR JOBS.

PART II CONTAINS MUCH ELSE WHICH SHOULD HAVE LASTING BENEFITS FOR COMPANIES.

SHARE OPTION SCHEMES ARE IMPROVED IN CLAUSES 38-39. THE NEW RELIEF PROPOSED FOR APPROVED SHARE OPTIONS BY REPLACING THE INCOME TAX CHARGE WITH A CAPITAL GAINS TAX ON DISPOSAL OF SHARES SHOULD HELP COMPANIES IN ATTRACTING AND MOTIVATING THE KEY MANAGERS ON WHOM SO MUCH DEPENDS.

THE CORPORATE FINANCE PACKAGE (CLAUSES 35, 36, 41 and 62) INCLUDES A NUMBER OF MEASURES WHICH SHOULD GIVE COMPANIES GREATER FLEXIBILITY IN RAISING FINANCE AND SO GIVE A

MODEST STIMULUS TO A REVIVAL IN THE CORPORATE BOND MARKET.

WE SHALL BE ABLE TO SCRUTINISE THE DETAILS OF THE BILL IN COMMITTEE. IN THE FIELD OF CAPITAL GAINS TAX I WOULD HOWEVER LIKE TO DRAW THE HOUSE'S ATTENTION TO THE PROVISION WHICH WILL ALLOW GIFTS TO HERITAGE MAINTENANCE FUNDS TO BE TREATED AS OTHER GIFTS (CLAUSE 66) AS HAS BEEN URGED BY THE HISTORIC HOUSES ASSOCIATION.

THERE ARE THEN THE PROVISIONS DESIGNED TO REMOVE DISTORTIONS IN THE FIELD OF SAVINGS AND INVESTMENT. THE PROVISIONS RELATING TO LIFE ASSURANCE PREMIUM RELIEF ARE CONTAINED IN CLAUSE 70.

THERE ARE ADJUSTMENTS IN THE CORPORATION TAX REGIME FOR THE OIL AND GAS INDUSTRY CONTAINED IN CLAUSES 75 TO 79 AND THERE ARE MINOR CHANGES IN PETROLEUM REVENUE TAX IN CLAUSE 109 TO 112.

THE NEXT 2 LENGTHY SECTIONS OF THE BILL CONTAIN MEASURES TO COUNTER TAX AVOIDANCE. CLAUSES 80 TO 89, TOGETHER WITH SCHEDULE 16 TO 18, DEAL WITH CONTROLLED FOREIGN COMPANIES. CLAUSES 90 TO 97 AND SCHEDULES 19 AND 20, ARE CONCERNED WITH OFFSHORE FUNDS. BOTH THESE MAJOR PIECES OF LEGISLATION HAVE BEEN THE SUBJECT OF FULL CONSULTATION IN ADVANCE. AND IN THE LIGHT OF LATE REPRESENTATIONS WE WILL BE BRINGING FORWARD FURTHER AMENDMENTS ON OFFSHORE FUNDS AT THE COMMITTEE STAGE.

ON THIS SUBJECT I SHOULD ALSO TOUCH ON THE IMPLICATIONS OF THE RECENT DECISION OF THE HOUSE OF LORDS IN FURNISS -V- DAWSON. TAKEN WITH THE DECISION IN RAMSAY'S CASE IT IS NOW CLEAR THAT THE WIDESPREAD ASSUMPTION BASED ON THE DUKE OF WESTMINSTER'S CASE IN THE 1930s THAT THE COURTS WILL ALWAYS LOOK AT THE FORM RATHER THAN THE SUBSTANCE OF A TRANSACTION OR VARIOUS TRANSACTIONS IS NO LONGER VALID. // THE HOUSE OF LORDS MADE CLEAR THAT THIS IS AN EVOLVING FIELD OF LAW. BUT THE EMERGING PRINCIPLES DO NOT IN ANY WAY CALL IN QUESTION THE TAX TREATMENT OF AND OTHER STRAIGHTFORWARD COMMERCIAL TRANSACTIONS. NOR IS THERE ANY QUESTION OF INLAND REVENUE CHALLENGING, FOR EXAMPLE, THE TAX TREATMENT OF COVENANTS, LEASING TRANSACTIONS ~~AND~~ STRAIGHTFORWARD TRANSFERS OF ASSETS BETWEEN MEMBERS OF THE SAME GROUP OF COMPANIES. I ASSURE THE HOUSE ALSO THAT IN ACCORDANCE WITH NORMAL PRACTICE THE INLAND REVENUE WILL NOT SEEK TO RE-OPEN CASES WHERE ASSESSMENTS WERE PROPERLY SETTLED IN ACCORDANCE WITH PREVAILING PRACTICE AND BECAME FINAL BEFORE THAT DECISION.

THE BOARD OF INLAND REVENUE WILL ALSO SEE WHETHER CLEARANCE FOR TYPES OF CASE OF PARTICULAR IMPORTANCE OR GENERAL GUIDANCE FOR THE BENEFIT OF TAXPAYERS AND THEIR ADVISORS CAN BE GIVEN.

THE PRINCIPLE IN FURNISS -V- DAWSON SHOULD LEAD IN FUTURE TO A GREATER SIMPLICITY IN OUR TAX SYSTEM AND WILL I HOPE ENABLE US OVER THE COURSE OF TIME TO PRUNE OUT PROVISIONS WHICH OWE THEIR EXISTENCE TO THE COMPLEXITIES OF A HIGH RATE - SOME MIGHT SAY A CONFISCATORY RATE - TAX SYSTEM WITH THE MULTIPLICITY OF SPECIAL RELIEFS. I AM SURE THE WHOLE HOUSE WOULD WELCOME THAT.

THE CHANGES WE PROPOSE IN CAPITAL TRANSFER TAX (CLAUSES 98 TO 104) AND STAMP DUTY (CLAUSES 105 TO 108) REFLECT OUR DETERMINATION TO SIMPLIFY THE SYSTEM AND LIGHTEN THE BURDEN OF TAX.

THE CHANGES IN DEVELOPMENT LAND TAX (CLAUSES 114 TO 118) SIMILARLY REDUCE THE INCIDENCE OF TAXATION AND SHOULD ASSIST INDUSTRIAL AND COMMERCIAL DEVELOPMENT.

BUT THIS FINANCE BILL HAS NOT JUST CHANGED AND SIMPLIFIED THE STRUCTURE. IT HAS ABOLISHED TAXES TOO. EXCISE DUTIES ON KEROSENE AND THE INVESTMENT INCOME SURCHARGE HAVE GONE. THE ABOLITION OF INVESTMENT INCOME SURCHARGE WILL I HOPE BE RECEIVED WITH ENTHUSIASM - AND CERTAINLY WITHOUT REGRET.
IT DISCRIMINATED AGAINST INVESTMENT. IT WAS UNFAIR TO MANY RETIRED PEOPLE WHO COULD NOT BY ANY STRETCH OF THE IMAGINATION BE CALLED RICH. IT WAS PARTICULARLY DISCRIMINATORY AGAINST THOSE WHO

RETIRED FROM SELF-EMPLOYMENT WITH NO PROSPECT OF A COMPANY PENSION AND WHO HAD TO RELY ON INCOME TAX FROM THE PROCEEDS - SOMETIMES IN THE FORM OF ANNUITIES - OF SELLING THEIR BUSINESSES OR PROFESSIONAL PRACTICES.

FINALLY THIS FINANCE BILL SEES THE END OF THE NATIONAL INSURANCE SURCHARGE (CLAUSE 113). I WILL NOT LABOUR THE CASE FOR ABOLITION. I DOUBT WHETHER THIS TAX EVER HAD MANY ENTHUSIASTIC SUPPORTERS
DARKEST HOURS
EVEN DURING THE DESPERATE TIMES OF THE LAST LABOUR GOVERNMENT. HOWEVER I WOULD LIKE TO REPEAT THAT THE REDUCTION OF THIS TAX ON JOBS SINCE 1979 FROM 3½ PER CENT TO ZERO PER CENT IS WORTH SOME £3 BILLION A YEAR TO EMPLOYERS AND HAS REMOVED A SUBSTANTIAL INDUCEMENT TO EMPLOYERS TO KEEP DOWN EMPLOYMENT. I HOPE THAT IT WILL BE COMMON GROUND BETWEEN US THAT THIS IS A TAX WE SHOULD BE WITHOUT.

FROM: J GIEVE
DATE: 10 April 1984

MR MARTIN

cc Chancellor
Financial Secretary
Economic Secretary
Minister of State
Mr Cassell
Mr Monck
Mr Monger
Mr Battishill
Mr Folger
Mr R I G Allen
Mr Hall
Mr Monaghan
Mr Smee
Mr Griffiths
Mr Lord
Mr Portillo
Mr Makeham

PS/Inland Revenue
Mr Kucyzs - IR
PS/Customs & Excise
Mr Wilmott - C & E

FINANCE BILL SECOND READING DEBATE

I attach the final draft of the speech tonight. It should be checked against delivery.

JG

J GIEVE

SECOND READING: FINANCE BILL

I BEG TO MOVE THAT THE BILL BE READ A SECOND TIME.

A MONTH AGO, WHEN MY RHF PRESENTED HIS BUDGET TO THE HOUSE, HE SET IT IN THE FRAMEWORK OF A FINANCIAL STRATEGY FOR THIS PARLIAMENT AND BEYOND. I THINK IT IS FAIR TO SAY THAT THE BUDGET CAUGHT THE IMAGINATION OF THE HOUSE - OR AT LEAST OF A MAJORITY OF THE HOUSE - AND THE COUNTRY , NOT BECAUSE IT WAS A GIVE AWAY BUDGET - IT WAS NOT - BUT BECAUSE IT SHOWED A FIRMNESS OF PURPOSE ON FINANCIAL STRATEGY AND A DETERMINATION TO INITIATE RADICAL AND IMAGINATIVE REFORM OF OUR TAX STRUCTURE.

THE DEBATE THAT FOLLOWED THE BUDGET RIGHTLY CONCENTRATED ON THE BROAD STRATEGY. TONIGHT WE START ON THE MORE TECHNICAL AND PROSAIC PROCESS OF EXAMINING THE FINANCE BILL. IT RUNS TO 123 CLAUSES AND 23 SCHEDULES. THE HOUSE WILL BE RELIEVED TO HEAR THAT I DO NOT INTEND TO TAKE IT THROUGH THEM ONE BY ONE BUT RATHER TO SHOW HOW THEY REFLECT THE MAIN THEMES OF THE BUDGET.

I SHOULDPOINT OUT HOWEVER AT THE OUTSET THAT THIS YEAR'S FINANCE BILL CONTAINS RATHER MORE THAN THE BUDGET PROPOSALS. BECAUSE OF THE GENERAL ELECTION LAST YEAR IT INCLUDES A NUMBER OF THE PROVISIONS INTRODUCED ORIGINALLY IN THE 1983 BILL. AS A RESULT, SOME 44 CLAUSES AND 10 SCHEDULES - NEARLY HALF THE TOTAL BILL - HAVE ALREADY BEEN THE SUBJECT OF PUBLIC EXPOSURE AND PUBLIC CONSULTATION. I AM SURE THAT OUR DEBATES IN THE COMING WEEK WILL BE BETTER INFORMED AS A RESULT.

WE ARE ALSO FORTUNATE TODAY TO HAVE AVAILABLE THE TREASURY AND CIVIL SERVICE SELECT COMMITTEE'S REPORT ON THE BUDGET. I AM SURE THE HOUSE WILL WISH TO JOIN ME IN CONGRATULATING MY RHF FOR WORTHING AND THE OTHER HMs OF THE COMMITTEE ON PRODUCING A REPORT SO SPEEDILY. WE WILL ALL WISH TO STUDY IT CAREFULLY AND AT LEISURE. FOR THE MOMENT, WHILE I MAY NOT BE ABLE TO AGREE WITH ALL THE COMMITTEE'S CONCLUSIONS, I WAS ENCOURAGED THAT THEY FOUND A NUMBER OF MEASURES IN MY RHF'S BUDGET BOTH IMAGINATIVE AND WELCOME. I SHALL REFER TO OTHER CONCLUSIONS LATER.

MAY I ALSO SAY THAT WE UNDERSTAND AND RESPECT THE REASONS WHICH MAKE IT IMPOSSIBLE FOR THE RHG MEMBER FOR SPARKBROOK TO BE HERE TONIGHT. I AM SORRY THAT WE SHALL NOT HAVE HIS CONTRIBUTION TO THE DEBATE

THE ECONOMIC BACKGROUND

THE BUDGET WAS INDEED IMAGINATIVE AND RADICAL. BUT THE REFORMS WERE SET WITHIN THE FINANCIAL FRAMEWORK WE HAVE PURSUED OVER THE LAST 5 YEARS AND ARE DETERMINED TO CONTINUE. WE SHALL CONTINUE TO REDUCE THE RATE OF MONETARY GROWTH AND THE LEVEL OF PUBLIC BORROWING AS A PROPORTION OF NATIONAL OUTPUT. THIS WILL MAINTAIN THE PRESSURE TO REDUCE INFLATION AND INTEREST RATES AND SO PROVIDE THE FINANCIAL STABILITY WHICH IS CRUCIAL FOR OUR PRIVATE ENTERPRISE ECONOMY.

AT THE SAME TIME WE INTEND - LET THERE BE NO DOUBT ABOUT THIS - TO MAINTAIN FIRM CONTROL OF PUBLIC EXPENDITURE. WE DO REALISE OF COURSE THE DIFFICULTIES TO WHICH THE SELECT COMMITTEE HAVE DRAWN ATTENTION. BUT WE ARE DETERMINED NOT TO RELAX OUR GRIP AND THUS TO KEEP OPEN THE POSSIBILITY OF

A SUSTAINED POLICY OF TAX CUTS WHICH WOULD IMPROVE INCENTIVES AND ASSIST THE CONTINUING IMPROVEMENT IN THE SUPPLY SIDE PERFORMANCE OF OUR ECONOMY.

IN THESE WAYS THE BUDGET PROVIDES THE CONTINUING BASIS FOR THE SUSTAINED NON-INFLATIONARY GROWTH THAT HAS I THINK BEEN THE AIM OF ALL GOVERNMENTS SINCE THE WAR.

I HOPE THAT THE HOUSE WILL ALLOW ME TO REMIND IT OF WHAT HAS BEEN ACHIEVED SO FAR. IT IS 3 YEARS NOW SINCE THE TROUGH OF THE RECESSION. BY THE END OF 1983 OUTPUT WAS 7½ PER CENT ABOVE ITS LOW POINT, FIXED INVESTMENT WAS UP BY ABOUT 13 PER CENT AND MANUFACTURING PRODUCTIVITY UP BY 11½ PER CENT. AT THE SAME TIME INFLATION AND INTEREST RATES HAVE CONTINUED TO FALL.

IN THE MONTH SINCE THE BUDGET FURTHER EVIDENCE HAS ACCUMULATED OF THE STRENGTH OF THE RECOVERY. WE HAVE SEEN A CUT IN UK SHORT TERM RATES - NOW 1½ PER CENT BELOW U.S SHORT TERM RATES - A CUT IN THE MORTGAGE INTEREST RATE, CONTINUING GOOD NEWS ABOUT INFLATION, RECORD FIGURES FOR EXPORTS IN FEBRUARY - WITH ENCOURAGING FIGURES FOR MANUFACTURING EXPORTS - AND FURTHER EVIDENCE OF A HEALTHY AND NECESSARY RISE IN COMPANY PROFITS.

OUTSIDE FORECASTERS WHO CLAIMED 6 MONTHS AGO THAT TREASURY FORECASTS WERE OVEROPTIMISTIC

ARE NOW BRINGING THEIR OWN FORECASTS CLOSER INTO LINE WITH OURS.

ON THE JOBS FRONT, WHILE THERE HAS BEEN AN ENCOURAGING INCREASE IN THE EMPLOYED LABOUR FORCE OVER THE LAST YEAR THE RECENT FIGURES ON UNEMPLOYMENT HAVE BEEN DISAPPOINTING.

THIS BILL CONTAINS MEASURES - NOTABLY THE ABOLITION OF NIS AND THE CORPORATION TAX PACKAGE - WHICH WILL DIRECTLY ENCOURAGE JOB CREATION. MORE IMPORTANT HOWEVER IT REFLECTS A STRATEGY WHICH TACKLES THE PROBLEMS AT ITS ROOTS.

FOR SUSTAINED IMPROVEMENT ON THE JOBS FRONT DEPENDS ABOVE ALL ON OUR SUCCESS IN FOSTERING A VIGOROUS, CONFIDENT AND ENTERPRISING PRIVATE SECTOR ABLE TO COMPETE SUCCESSFULLY AT HOME AND ABROAD AND EAGER TO EXPLOIT OPPORTUNITIES. THAT STRENGTH WILL NOT BE PRODUCED BY ANY SHORT TERM BOOSTS THAT GOVERNMENT CAN ARRANGE. THERE IS NO CERTAIN ROUTE TO SUCCESS BUT THE BEST AND ESSENTIAL AIM FOR GOVERNMENT MUST BE TO ENGENDER CONFIDENCE IN THE PROSPECTS

FOR EVEN LOWER INFLATION BY PRODUCING A STABLE FINANCIAL FRAMEWORK AND TO DO WHAT IT CAN IN THE TAX FIELD AS IN OTHERS TO ENCOURAGE ENTERPRISE. THIS WILL ENABLE THE ECONOMY TO FUNCTION BETTER AND SETTING BUSINESS ON THE ROAD TO PROFITABLE EXPANSION.

THAT IS THE OBJECTIVE OF MY RHF'S BUDGET. THAT IS WHY THIS IS A BUDGET WHICH IMPROVES THE PROSPECTS FOR JOBS.

UNCLASSIFIED

(rg)

FROM: A P HUDSON

DATE: 10 April 1984

MR HALL

c/
Martin sees no objection – provided you're content.
MOM
10/4

cc PS/Chancellor
Sir P Middleton
Mr Battishill
Mr Monger
Mr Ridley o/r
Mr Lord
PS/IR

TIMES CONFERENCE ON THE BUDGET

OK
M

Told FST's office.

1. I attach a note of a telephone conversation with Kenneth Fleet of the Times.

2. The Financial Secretary is inclined to accept this invitation, subject, of course, to your advice and the Chancellor's agreement.

3. If he does take up the invitation, he thinks it would be best for him to give the opening address, and not to answer questions. I mentioned to Mr Fleet the possibility of the Financial Secretary's speaking first, if he did it at all, and Mr Fleet was happy with this.

APH

A P HUDSON

PHONE CALL FROM KENNETH FLEET

1. Kenneth Fleet of the Times rang this afternoon (9 April) asking to speak to the Financial Secretary.

2. He told me that the Times is trying to get back into the business of organising conferences. They plan their first, entitled "The Times 1984 Budget Briefing", for 21 or 22 May, in the Dorchester Hotel.

3. They would like the Financial Secretary to speak for a few minutes on the thinking behind the personal and corporate tax strategy.

4. Other speakers will be accountants, stockbrokers, etc talking about particular tax changes and issues. The headings he mentioned were:

- How should funds be raised?
- How should money be invested?
- How should income be received?
- The taxation of enterprise
- The individual as taxpayer
- The individual as investor.

5. The Times hope to get a high-powered audience, to get their conferences off to a successful start.

APH

A P HUDSON

PS/Chancellor

INLAND REVENUE

WITH COMPLIMENTS

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HOUSE OF COMMONS DEBATES — Vol 58 No 138
FINANCE BILL SECOND READING DEBATE — TUESDAY 10 APRIL 1984

Summary of Revenue points (Part 1)

Col 249	Mr Peter Rees (CST)	Policy of tax cuts to be sustained
		NIS and corporation tax measures will encourage job creation
		Two main themes in Budget: - 1(a) shift from taxing income to taxing spending through increase in VAT base (b) real increase in income tax allowances - 2. simplification of tax system and removal of distortions, especially in corporate field
		Chapter 1: excise duties up in line with inflation, but clauses 5 and 8 give certain exemptions.
Col 250		Chapter 2: VAT extension should be seen in wider context. Yield will help finance increase in income tax thresholds
	Mr Robert Sheldon (Lab)	Further VAT extensions/increases planned?
	Mr Peter Rees (CST)	Shouldn't anticipate future measures. Present extensions modest.
	Dr Keith Hampson (C)	VAT on building alterations - will builders in private sector be caught but not those in public sector?
	Mr Rees (CST)	Local authorities relieved but not Govt.Departments. VAT still low in UK compared with other countries. Extensions simplify system by removing anomalies.
Col 251		Relief for Lifeboats and vehicles for handicapped extended.
		Income tax allowance increases more than in line with inflation. Thresholds 16% higher in real terms than in 1978/9.

Col 252		Child benefit increase wouldn't relieve poverty trap without reduction in means-tested benefits (eg FIS). Rise in tax allowances preferable - relieves unemployment trap and benefits more people.
Col 253	Mr Ralph Howell (C)	Why fewer people taken out of tax this year?
	Mr Rees (CST)	Because rate of increase in incomes not of same order.
		Corporation tax measures (Clauses 18, 20, 47, 57, Schedule 12) commended.
		Share option schemes relief (38,39) will help companies, also corporate finance package (35, 36, 41, 62)
		CGT measure on gifts to heritage maintenance funds commended. Other provisions also remove distortions in investment eg life assurance
Col 254		measure (70). Relief to be introduced (in Committee) for industrial assurance policies before 14 March 1984.
	Mr Ian Wrigglesworth (SDP)	Govt. should consult industry to ensure equality of treatment for savings
	Mr Rees (CST)	Clause 75-9 on changes for oil and gas, petroleum revenue tax.
		Clauses 80-9 90-7, Schedules 16-20: deal with tax avoidance. Has been full consultation on these. More on offshore funds in Committee.
		Furniss v Dawson: won't affect covenants, leasing and straightforward commercial transactions, or transfer of assets within a group of companies. IR will not reopen assessments settled prior to

		F v D. Clearance may be given in some cases. F v D should lead to simplification.
Col 255		CTT and stamp duty measures simplify and lighten tax. DLT changes reduce incidence of taxation.
		Commended abolition of tax on kerosene, IIS, NIS.
Col 256	Mr Jeff Rooker (Lab)	Opposition will scrutinise Govt amendments. Should have been more consultation in advance rather than amendments later eg on Lifeboats.
		Bill makes tax burden heavier. Yield in 1984-5 £22.5 billion higher in real terms than under Labour. Corporation tax, North Sea tax, capital taxes, stamp duty, NICs, rates, expenditure taxes all up in real terms under Conservatives. Only income tax and NIS down. Gave figures to prove burden of tax higher in real terms under Conservatives (Cols 257-61)
Col 260		Rooker-Wise amendment should have been tied to higher of wages or earnings.
	Mr Christopher Hawkins (C)	Reduction in top rate tax linked with incentives.
	Mr Rooker (Lab)	Cuts haven't brought entrepreneurs back from tax havens.
Col 261		Labour will oppose IIS abolition, though no clause on this in Bill. NICs not paid on investment income.
		Age allowance increase too small.
Col 262		Criticised abolition of life assurance relief - hits low earners.

Col 263		<u>Poverty trap</u> could be relieved by raising <u>child benefit</u> more than other benefits. Proportion of families in poverty trap same after Budget. Effective marginal rate of tax 60% for some of these.
		"Taking people out of tax" a myth.
Col 264		<u>UK's competitors</u> still tax high incomes and investment income severely but industry doesn't suffer.
		<u>Indirect taxes</u> higher in real terms than under Labour (quoted various figures). Hits low paid. Govt
Col 265		reneging on <u>1979 manifesto commitment</u>. Mentioned article in <u>New Statesman</u> 23 March re Govt's plans for <u>VAT on food</u>.
Col 266		<u>VAT on takeaways</u> - rejected international comparison figures in written answer 7 February. Proposals full of anomalies.
Col 267		<u>VAT on building alterations</u>: no significant anomalies. Endangers historic building renovation. Uncertainty for recipients of home improvement grants.
Col 268	Mr John Maxton (Lab)	VAT also hits renewing of <u>lead pipes</u> and <u>energy conservation</u>
	<u>Mr Rooker</u> (Lab)	<u>VAT on charities</u> - relief would have all-party support. Should at least revert to 1979 rate of 8%.
Col 269		<u>Company taxation</u>: many manufacturing industries will pay more. Profits won't offset loss of <u>first year allowances</u> when <u>inflation</u> low. Squeeze on <u>corporate liquidity</u> during <u>transitional period</u>.

Col 270		Clause 20(3) unfair: relative increase in tax on industrial and provident societies (reduction in rate less). Opposition will raise in Committee.
		Oil revenues badly used.
Col 271		NIS - why not abolished earlier? but abolition won't be opposed (Col 273).
Col 272		CTT cuts - no justification.
Col 273		Stamp duty changes: 90% of first-time house buyers won't pay it, and so won't benefit from reduction.
Col 274	Mr Terence Higgins (C)	Welcomed NIS abolition
Col 276		Govt. stance slacker, according to Select Committee on Treasury and Civil Service eg VAT change on imports - a once-for-all measure. Budget will involve future tax reduction.
		Corporate tax measures remove distortions from labour-capital cost ratio.
Col 277		Welcomed "medium-term tax strategy" - should be extended to other taxes.
Col 278	Mr Robert Sheldon (Lab)	Govt. denying agreement to raise child benefit in line with tax allowances.
Col 279		Welcomed Clauses 80-9, 90-7 on foreign companies and offshore funds, but should go further.
		Welcomed CST's comments on Furniss v Dawson.
Col 280		CTT and CGT and IIS measures and higher rates of income tax mean UK will be financially rather than industrially oriented. Rich unfairly favoured.

		IIS: earned/unearned income distinction makes sense. Criticised restriction of relief for expenses of earning income.
		Capital allowances measure discriminates against manufacturing
Col 281		Oil revenue increase badly used
Col 282		Corporation tax reduction and IIS abolition paid for by change in VAT on imports. Could this change be extended eg to banks, oil, etc? Duty on tobacco and spirits deferred; this is inconsistent.
Col 283		Welcomed life assurance change. Should abolish mortgage interest relief.
		VAT changes merely substitute one set of anomalies for another.
Col 283	Mr Graham Bright (C)	Welcomed reform of personal taxation, especially CGT and CTT measures. Further reforms needed e.g. to integrate income tax and CGT. Should replace CTT with accessions tax. Criticised reliefs previously available for investment in insurance and pension funds.
		Welcomed phase-out of capital allowances: permits better allocation of resources.
		Proposed enterprise bond scheme to allow small firms a deduction for these costs.
Col 285	Mr Brynmor John (Lab)	Clause 10 (VAT on home improvements): together with cut in improvement grants this is very damaging for home owners. Govt. imposing hardship in quest of logic. Incentive to black economy.

Col 286 Poverty trap: rise in
thresholds ineffective for
families with children.
Col 287 Inquiries into benefits must
take account of fiscal
aspects. Should simply
Col 288 index thresholds and use money
to increase child benefit.
Hoped no plans to means-test
child benefit.

PS/Chancellor

INLAND REVENUE

WITH COMPLIMENTS

Miss C. M. Brand
Inland Revenue
POLICY DIVISION
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HOUSE OF COMMONS DEBATES
FINANCE BILL SECOND READING DEBATE

Vol 58 No 139
Tuesday 10 April 1984

Summary of Revenue Points (Part 2)

Col 289	Mr Colin Shepherd (C)	VAT on cider too high: cider doesn't compete unfairly with beer. Industry will suffer and revenue go down.
Col 291	Mr Archy Kirkwood (Lib)	Budget unfair to poor and in shift to indirect taxation.
Col 292		Expenditure has determined taxation in recent past.
Col 293		Increase in petrol prices and vehicle excise duty unfair on rural areas.
		VAT on building alterations will boost black economy and put construction workers on the dole.
		VAT on takeaways penalises children.
		Furnished holiday lettings change will only compound problems. Changes needed in Committee.
		Alliance will look for redress of anomalies in Schedule B/D tax on woodlands.
		Life assurance change will invalidate some actuarial calculations. What about policies with in-built changes?
		Tax clawback from people working overseas unjustified.
Col 294		Age allowance should be increased more, earnings rule abolished.
		Budget has worsened poverty trap - personal allowance changes don't help. £1 increase in child benefit needed.

	Thresholds still below poverty line. Increase helps well-off most. Structural reform of personal allowances needed.
	Something should be done for share ownership schemes cf French Monory system. Would require removal of stamp duty on share transfers, plus other tax incentives.
Col 295	Should have tax credit system with accessions tax.
Col 295 Mr Christopher Hawkins (C)	Welcomed concession to disabled, but C & E interpreting it too strictly.
Col 297 Mr Brian Sedgemore (Lab)	Should have a "competition tax" to prevent overseas contracts without proper tendering (ie Oman).
Col 307	Import duties needed.
Col 310	Oil revenues wasted.
Col 310	Child benefit increase should be preferred to rise in thresholds.
Col 311	Tax reliefs ("a second welfare state") should be looked at.
Col 311 Mr Eric Cockeram (C)	Welcomed rise in thresholds, abolition of IIS and NIS.
Col 312	Criticised tax on bank interest: some non-taxpayers will now pay tax. Anomalous to exempt national savings and deposits over £50,000.
	Welcomed Clause 43 (trustee savings banks).

Col 315	Mr Austin Mitchell (Lab)	Select Committee on Treasury and Civil Service doubtful that capital allowance change would bring about transfer from machines to labour. Investment will simply fall.
Col 322		Oil revenues wasted.
Col 323		Budget contains nothing solid for small businesses - only for personal interests of businessmen. Caravan makers suffer from high interest rates.
Col 325		VAT increase to 15 per cent accelerated inflation to over 20 per cent.
Col 326		New overseas investment in Britian "from fly-by-night operations" wanting to avoid tax.
Col 330		Government commitment on child benefit unfulfilled. Should be increased to 95p in line with allowances, or to 130p and made taxable. Cost of latter would be £2.5 bn. Increase in tax thresholds too expensive - doesn't target help on poverty trap.
Col 331		NICs too high, threshold too low. A regressive tax. Should be replaced by a social security tax to be paid by employers. VAT on takeaways will hit the industry, the poor in inner-city areas, pensioners, school children, students, one-parent families, ethnic minorities, Labour voters and small businesses. Many anomalies involved. What about meals-on-wheels?

Question put:

House divided: Ayes 218, Nos 121

Question accordingly agreed to.

Clauses 10, 17, 18, 20, 21, 27, 57, 98, 105, 113 and Schedules 6 to 8 and 12 committed to a Committee of the Whole House. Opposition recorded that they would have wished to add Clauses 1, 2, 3, 4, 5, 8, 9, 19, 28, 39, 40, 58, 59, 60, 66 and 70.

FROM: F MARTIN
DATE: 12 APRIL 1984

FINANCIAL SECRETARY

cc PS/Chancellor
PS/Chief Secretary
PS/Economic Secretary
PS/Minister of State
Mr Monger
Mr Battishill
Mr Lovell
Mr Lord
Mr Portillo

PS/Inland Revenue
Mr S Jones - IR
PS/Customs & Excise
Mr P Smith - C&E

POST-BUDGET CONTACTS: ASSOCIATION OF INDEPENDENT BUSINESSES

As part of the programme of post-Budget contacts you are meeting a delegation from the Association of Independent Businsses at 10.30 am on Friday 13 April. The AIB team will be Mr John Cochrane, Mr Richard Roberts and Mr Phillip Bayliss. Mr Stephen Jones of Inland Revenue, Mr Peter Smith of Customs & Excise and I will be in support.

<u>The AIB's response to the Budget</u>

2. Attached at Annex A is a copy of the AIB's press release commenting on the Budget. It contains only adverse comment, being strongly critical of the change in VAT on imports and the corporation tax changes.

3. A note on VAT on imports is attached at Annex B. In addition, you might wish to point out that it is <u>not</u> the case, as the AIB suggest, that the change provides "no economic benefit". Quite apart from removing a discrimination against UK suppliers, enabling them to compete with imports on a more equal footing, it provides revenue which enables substantial reductions in 1984-85 in both business taxation(for example, NIS abolition, the reduction in the small companies rate of corporation tax) and personal taxation.

4. A note on the corporation tax changes is at Annex C. In addition, you might remind Mr Cochrane of his own criticisms of the present system at the AIB's pre-Budget meeting with you on 15 February.

The minutes of the meeting record that,

> "Mr Cochrane was very concerned that the present corporation tax system worked, unintentionally, very much against the interests of smaller firms. In particular, it led to many smaller businesses seeking relief by unnecessary expenditure".

As regards the AIB complaint about capital allowances and commercial buildings, you might simply point out that the Budget changes substantially reduce the previous bias against investment in commercial buildings.

5. The AIB press notice also mentions the AIB complaint about PIID forms, a topic also discussed at the 15 February meeting. A note on this is attached at Annex D.

<u>Other points for discussion</u>

6. Since the AIB's response is so grudging and partial, you may wish to emphasize to them the importance of looking at the Budget measures <u>as a whole</u>. You might point out that it provides a radical programme of tax reform - including the outright abolition of two major taxes, NIS and IIS - both for business taxation and the taxation of savings and investment, coupled with a substantial real increase in income tax allowances as a start in restoring thresholds to sensible levels. The Budget measures will significantly reduce taxation over the next two years, while monetary and public expenditure policies are designed to provide scope for <u>further</u> tax reductions in future Budgets. The measures will also sustain all current recovery which must be good for all businesses. Since it is inevitable that there will be carping criticism from political opponents, it is important that all those who share these basic aims - lower tax, more efficient economic performance - should give the Budget measures <u>in the round</u> fair consideration.

7. In addition, you might point out to the AIB that the Budget contained a fair number of the things they asked for in their pre-Budget representations (attached at Annex E). These comprise:

- the reduction in stamp duty (paragraph 2 of the representation);

- the substantial increase in income tax allowances, in part financed by an increase in indirect taxation (paragraph 4);

- a lower rate of tax on companies' profits (paragraph 6); and

- a reduction in the burden of capital transfer tax (paragraph 10).

Again, this would support the point that it would be helpful if in their public comments on the Budget they could look at the measures as a whole.

F Martin

F MARTIN

ANNEX A

Association of Independent Businesses

(formerly the Smaller Businesses Association)

Trowbray House, 108 Weston Street, London SE1 3QB
Telephone: 01-403 4066

PRESS RELEASE

DATE: 21st MARCH 1984

RELEASE: IMMEDIATE

INDEPENDENT BUSINESSMEN POINT OUT GOVERNMENT VAT SWINDLE SWINDLE

The Association of Independent Businesses' National Council meeting in London the week after the Budget strongly criticised Government proposals to end the Postponed Accounting System (PAS) for VAT on imports in the Autumn. No economic benefit will accrue from this change and the AIB doubts the size of the one-off revenue gain which has apparently attracted Mr Lawson's attention.

The AIB has five main concerns on the end of PAS:-

* Delays at ports of entry will create additional costs for all imports and exports, be they manufactured goods or raw materials whether or not they are subject to VAT, as the staff of forwarding agents and others are increased and the extra overheads have to be translated into higher fees. Some agents suggest a 40% increase. One EEC estimate last year concluded delays at EEC frontiers cost £7,000m. The Retail Consortium estimate an increase of 1.7% in costs as a result of this change in the autumn of this year.
* the Government appear to have made no allowance in their estimates of the one-off increase in revenue for extra Customs and Excise

costs of collecting the VAT at point of entry, nor the reduction in imports generally that will result.

* it seems ludicrous to change a VAT system to harmonise with other EEC member states when (under the 14th VAT directive) the Commission are trying to get everyone else to harmonise with us!
* especially during the initial phase of the end of PAS, confusion and delays at ports of entry will be immense, as the experience of Ireland which made the change recently shows and other representative bodies, like the British Shippers Council, point out.
* the effect on small and independent firms cash flow over the months during which PAS is withdrawn could be immense. Firms will have to finance the VAT outgoings before they receive the payment for the goods they imported and onsold. One member has estimated that this will affect his cash flow by £15,000 this year and small businesses generally will be forced to borrow more or reduce expansion out of the recession for lack of funds.

Hence the AIB will call on the Chancellor to retain PAS and balance the Budget by curtailment of public expenditure elsewhere.

Other points on the Budget of concern include the failure of the Chancellor to reduce the bureaucracy to employers and the unjust tax treatment on employees caused by P11D; the abolition of stock relief which will, if inflation continues at 4½%, erode one third of the benefit of the reduction of the small firms rate of Corporation Tax from 38% to 30% for a typical small firm; the phasing out of first year allowances while Corporation Tax for the smaller firm is still at a high rate and the injustice to the service industry sector by Mr Lawson's refusal to include all commercial buildings in Industrial Building Allowances.

ENDS

../...

VAT ON IMPORTS

Delays at ports

There will be increased potential for congestion at ports where facilities are already under heavy pressure. But few importers will have to pay VAT on the spot : most will defer it in same way as customs duties. No reason, therefore, for goods to be held up while VAT is paid.

100 extra staff will be deployed to cope with extra work generated by change in system. But important to remember that UK customs controls generally fit into natural break in transport mode (eg ship/air to road/rail) : little likelihood of 'Bremner Pass' style blockages. Change not operative till 1 October. Customs will be discussing practical problems with operators between now and then, and expect to iron out any serious difficulties in good time.

Increased costs

Imported goods will probably become slightly dearer. But some of the cost of the change may be shifted to overseas suppliers.

Customs agents could be significantly affected. They will need to increase their duty deferment guarantees to cover VAT due on importation, and will probably have an increased workload. They may pass this on to importers in the form of increased fees. But reports of massive increases (40% or more) seem exaggerated.

Firms' cash flow

Some 50 000 regular importers likely to be affected. Admitted that some firms will have to finance import VAT. But important to see Budget as a whole, and set any disadvantagesagainst boost given to industry by expanding economy and specific measures like NIS.

Customs and Excise Costs

100 extra staff minuscule in relation to £1.2 billion once-for-all benefit (and continuing financing gain to Exchequer - say £120 million p.a.). Staff increase to be found within Chancellor's departments' manpower ceiling - no overall rise in manpower.

EC harmonisation

Change brings UK into line with major EC competitors. Admitted that Commission want to harmonise on basis of present UK system. We acknowledge advantages of this - Chancellor has given firm commitment to revert to it if other EC countries are willing to agree on it as basis for harmonisation. But till then, wrong to continue to put UK industry at disadvantage.

BUSINESS TAXATION CHANGES - GENERAL

Need for reform of business taxation as great as anywhere else in tax system. Rate of corporation tax was too high. Lower rates will stimulate more productive investment and higher output and profits.

Changes proposed in Budget meet several objectives:

- reducing distortions in the tax system between different kinds of investment

- reducing bias in favour of capital and against jobs

- widening tax base and reducing tax rate to improve incentives

- reducing bias in favour of debt and against equity finance.

It is true that some sectors do better than others and that within sectors individual businesses may gain or lose. But all main sectors of business gain overall over the first 2 years from the proposed business tax changes. And business will continue to benefit from low rate of corporation tax and abolition of NIS.

For small companies the cut in the rate to 30% is implemented in full immediately. Some 200,000 companies a year should benefit - and during the transitional period they can still enjoy first year allowances as well.

STOCK RELIEF

Stock relief was introduced in response to high inflation. The Government's strategy is to sustain the reductions in inflation which have already been achieved. It is no part of that strategy to perpetuate a relief which has outlived its purpose: that could impede the progress towards lower tax rates.

The conbination of stock relief and relief for interest paid can be distorting. There is some evidence that this has led to excessive stock levels. So, abolishing stock relief will help produce a better allocation of resources.

The abolition of stock relief does not mean Government is opposed to the accountancy profession's attempt to find an acceptable successor to the current cost account standard SSAP 16. But, as many accountants accept, what is right for accountancy practice is not always right for tax. And accountants themselves are not agreed on a new standard.

CAPITAL ALLOWANCES

Reduction in rates of first year and initial allowances should not be looked at in isolation, must be viewed as part of wider-ranging reform of business taxation - including abolition of NIS and substantial reductions in rate of corporation tax.

No virtue in investment for its own sake. Capital project worthwhile only if return adequately repays original sacrifice. Previously, too much investment has not done so, and was undertaken only because it was subsidised by taxpayers.

While level of United Kingdom investment has been well up to that of main competitors, returns have been significantly lower. In future, unprofitable and uneconomic investment will tend to be replaced by investment in project and assets which are profitable on their own merits. Quality of our investment will improve.

Furthermore, capital allowance changes should be seen as part of budget for jobs. One effect of old regime was to subsidise capital investment which simply took the place of labour. Now, investment which will go ahead will give good economic return, strengthening both the company making it and the economy. In this way, it will add to demand for labour.

FORMS P11D

Factual:

(i) Form P11D is the employer's notification to the Revenue of expenses payments and benefits provided to directors and 'higher-paid' employees, currently defined as those earning at a rate of £8,500 a year or more, where special rules apply. This figure was introduced in 1979 and with the increase in wages, increasing numbers of forms have been received (1979/80 .5M; 1982/83 1.35M - excluding Nil returns).

The AIB's Proposals

(ii) The AIB propose that:

- the threshold should be increased (perhaps to £14,000)

- income for the purpose of the threshold should exclude expense payments where the expense would be tax deductible.

(iii) In addition, the AIB met the Financial Secretary on 15 February and claimed that there was a substantial shortfall between the number of the 'higher-paid' and the number of forms P11D received.

Line to Take

(iv) The threshold does create anomalies in the tax treatment of benefits as the treatment depends on the employee's level of other remuneration. Raising the threshold will, however, perpetuate these anomalies. Benefits are now widespread and the Government's policy is to work towards the abolition of the threshold so that the same treatment applies irrespective of the level of other earnings.

(v) The Revenue is looking at ways to make the form simpler to complete.

(vi) Excluding expense payments where the expenses are tax-deductible would increase administrative costs and uncertainty as it would not be known whether an expense was deductible until the Tax Office had agreed it after the end of the tax year. Employers can at present claim dispensations for expenses which are invariably deductible.

(vii) The figures for 1981/82 indicate that 2.5M P11D's were required (excludes .8M civil servants, etc) of which 1.6M were returned; .7M were assumed to be cases where no benefits arose and .2M were outstanding. The Revenue is at present reviewing its efforts in this field.

Association of Independent Businesses

(formerly the Smaller Businesses Association)

Trowbray House, 108 Weston Street, London SE1 3QB

President:
The Rt.Hon. Lord Lever of Manches

The Rt Hon Nigel Lawson Esq M
Chancellor of the Exchequer,
Treasury Chambers,
Parliament Street,
London SW1P 3AG.

Dear Chancellor

I am writing to reinforce certain of our submissions for the 1984 Budget which were sent to your office on 21 December 1983.

2. The proposals in the doucment follow our National Council's concern that taxes must neither distort the true market economy nor be allowed to discourage the creation of wealth and the promotion of enterprise.

3. Our National Council is further concerned with those taxes which are no longer a significant source of revenue especially those that have a heavy compliance cost. In particular certain stamp duties and the current Capital Gains Tax fall into this category and should, in our view, be abolished in their present form.

4. As in previous years we highlight the need to remove the unemployment trap by a really significant increase in personal allowances or lower rates of tax. We appreicate that this will be expensive but are convinced that any relief you can give must be channelled in this direction. In addition we would recommend that any revenue from increased indirect taxation or from any increase in National Insurance charges for those whose gross income exceeds £12,200 (1983/84) and whose taxable income is less than £14,600 should be used for this purpose.

5. The Government is committed to the reduction of the bureaucratic burden facing the owner of a smaller business. In 1977/8 P11D's had to be completed for one in ten full-time employed men. Failure to increase the threshold for this form means that in 1983/84 it will be needed for 50% of such employees. Not only does this greatly increase the administrative task of record keeping and preparation of the form but by including genuine reimbursable expenses when calculating the threshold for P11D the Government has allowed a situation to develop where two men, on identical moderate salaries and benefits, but one is in receipt of reimbursable expenes, have a different ultimate tax burden. This

.../...

must be wrong and was never the intention of Parliament.

6. Corporation Tax has led to many smaller businesses seeking relief by unnecessary expenditure to obtain capital allowances. The Association is still committed to the simplification of the existing system by imposing a low rate of tax on profits which have been adjusted by a recognised current cost formula with free depreciation. With such a system capital allowances could be abolished. We appreciate that such changes are unlikely to be introduced in the 1984 Budget and have made proposals which will remove the fiscal barriers to growth so often encountered by small successful firms.

7. For most companies, especially after a recession, growth must be preceded by an injection of funds to finance equipment and to build up working capital. Yet finance on acceptable terms is still denied to many. We propose that those who make profits should be able to access the tax paid on them for development finance, asset acquisition and increased working capital. We propose that tax paid should be available for a period of seven years.

cf. home 3 years.

8. A feature of this proposal is that only successful companies are assisted and only if they need assistance. The current ability to go back three years for incorporated and one year for unincorporated companies is nowhere near long enough for small companies where re-equipment of large pieces of plant may only take place every seven or eight years.

9. The Association has always advocated the need to increase equity investment in small firms. The present arrangements whereby dividends have to be paid out of taxed profit, while interest payments on loans are allowed against tax is a disencentive to finance expansion or a start up with equity as the tax bill is greater.

10. We are concerned at the damage done to the unquoted company by Capital Transfer Tax on the death of the owner. Our proposed amendments would go a long way to preventing this and to allowing the business to be passed on to the next generation in a much healther condition.

I, and my colleagues on the AIB's Taxation Committee would be pleased to elaborate on any of these points and I believe that a meeting with you would be most useful.

Yours sincerely

J A Cochrane

J.A. Cochrane
Chairman AIB Taxation Committee.

UNCLASSIFIED

FROM: A M ELLIS
DATE: 13 April 1984

PS/CHIEF SECRETARY

cc PPS
PS/Financial Secretary
PS/Minister of State
Mr Monger
Mr Allen
Mr Griffiths
Mr Martin
Mr Reed
Mr Battishill
Mr Norgrove
Mr Folger
Mr Lord
Mr Portillo
Mr Hall
PS/IR
PS/C&E

FINANCE BILL: COMMITTEE OF THE WHOLE HOUSE

The Economic Secretary has read you minute of 11 April on the allocation of clauses to be taken on the Floor.

He would be content to take on Clause 113 (abolition of NIS) as suggested by the Chief Secretary. His one misgiving would be if it appeared that the tone of the amendments tabled for Clause 27 (composite rate) which follows Clause 113 and which he is also taking appear contentious and time-consuming. He suggests therefore that, if the Minister of State is willing, he might provide cover on Clause 113 for that eventuality.

A M ELLIS

FROM: F MARTIN
DATE: 3 MAY 1984

FINANCIAL SECRETARY

cc PS/Chancellor
PS/Chief Secretary
PS/Economic Secretary
PS/Minister of State
Mr Monger
Mr Battishill
Mr Lord
Mr Portillo

PS/Inland Revenue
Mrs Hubbard - IR

POST-BUDGET CONTACTS: CONSULTATIVE COMMITTEE OF ACCOUNTANCY BODIES

As part of the programme of post-Budget contacts you are meeting a delegation from the Consultative Committee of Accountancy Bodies at 11.30 am on Friday 4 May. The CCAB team will be Mr Roger White (Chairman of the CCAB's Tax Steering Sub-Committee), Mr Philip Hardman, Mr Alan Reid, Mr Ken Duncan (sub-committee members) and Mr Edwin Vidler (sub-committee secretary). Revenue officials and I will be in support.

Points for discussion

2. Attached at Flag A is a list of the topics which the CCAB wish to raise at the meeting. Given the nature of the CCAB it is inevitable that most of their concerns are with fairly specific and detailed areas of the tax regime. Briefing on the various topics listed, prepared by Inland Revenue, is attached at Flag B. In the main I think it will suffice to simply listen to their more detailed points without comment, where necessary asking them to forward, either to you or to the Revenue, a further written explanation of their concerns. You might particularly wish to ask them to forward their ideas on the future of capital gains tax, in the context of the examination announced by the Chancellor, as you did at the 13 April meeting with the Association of Independent Businesses.

3. The CCAB note indicates that they generally welcome the tax reforms introduced in the Budget, and you will no doubt wish to draw their views on this. Depending on how the discussion goes, you might also wish to draw their views on the next steps for tax reform (beyond

those for the capital taxes set out in paragraph 7 of the note). You might point out that the Budget will not only significantly reduce taxation over the next two years, but is in the context of monetary and public expenditure policies designed to provide scope for further tax reductions in future Budgets. What would be their priorities for the use of these resources? And given the Government's objectives in tax reform - a simpler system, with lower rates and fewer complicating and distorting reliefs, to promote increased economic efficiency - what areas would they see as worthy of consideration to forward these objectives?

4. Finally, you may be interested in the cutting attached at Flag C from the latest edition of "Taxation", which reports that, for a trial period of two years, the six bodies represented by the CCAB should make their representations independently rather than jointly. Since the article records that, "this will substantially increase the number of representations and responses made", some mild expression of regret might be in order.

F. Martin

F MARTIN

ANNEX A

PRELIMINARY NOTES FOR MEETING WITH JOHN MOORE MP FRIDAY 4TH MAY 1984

1. General reaction to Budget and Finance Bill 1984

   (a) Individual views.
   (b) Generally welcomed as a reforming Budget.
   (c) Position on the self-employed of withdrawal of reliefs (FYAs and stock relief and overseas earnings) with unchanged tax rates.
   (d) UK corporate rate internationally particularly in light of tax credit refunds to overseas parent companies.

2. The proposals on controlled foreign companies

   (a) Remain opposed to the provisions.
   (b) Particular objection to the list as published with the Finance Bill.

3. Double tax relief

   (a) The application of DTR before ACT is not a real concession. The DTR rules remain narrow and inflexible to UK companies particularly looked at against CFCs.

4. Deep discount securities

   (a) Still too complicated.

5. Offshore funds

   (a) Drawn too widely.

6. Share option schemes

   (a) Welcomed

   (b) Why not go further and also simplify the rules on share ownership by employees and directors.

7. Items to consider for 1985:

   i. retirement relief

   ii. capital gains tax

   iii. capital transfer tax

   (a) What about the repeal of CGT and the replacement by the old short term rules for income treatment for acquisitions and disposals within a year.

   (b) The pressing need for review and improvement to retirement relief.

   (c) Should CTT be improved for the comfortably off (say estate of £100,000).

RJGW/VH - 26th April 1984

ANNEX B

MEETING WITH CCAB 4 MAY 1984

1C UNINCORPORATED BUSINESSES

The point the CCAB are making is that unincorporated businesses lose from some aspects of the Budget - for example the reductions in capital allowances, the abolition of stock relief and the withdrawal of overseas earnings relief, but they cannot gain from reductions in the corporation tax rate.

There may be some self-interest in the CCAB's comments here. As a professional body, their members do not incorporate and it is quite possible that accountants working for the larger international firms at least will have benefited from the overseas earnings relief in the past.

LINE TO TAKE

Other measures in the Finance Bill which benefit unincorporated businesses should not be ignored. For example, abolition of NIS - 10% of which is paid by unincoporated businesses; and the abolition of IIS and the substantial increase in personal tax thresholds.

Taking the income tax and other changes together, the unincorporated will get a substantial gain from the Budget up to and including 1986/87. And the self-employed can look forward to further improvements in income tax. The Chancellor said in the Budget that he intended to carry forward in the lifetime of the present Parliament the progress already made in reducing the burden of personal taxation.

The total gain accruing to the 1.5 million self-employed in 1984/85 from the Budget will be:

- £m275 compared with no change in the personal allowances; and

- £m160 compared with indexation.

Overseas earnings relief was complex, abused and distorted the tax system. Now top tax rates have been reduced it is no longer necessary.

MEETING WITH CCAB 4 MAY 1984

1D UK CT RATE INTERNATIONALLY

The 35% corporation tax rate which will apply from Financial Year 1986 is low by international standards and this should stimulate profitable inward investment. This point has been picked up by a number of commentators, in particular the Monetary Bulletin published by the stockbrokers W Greenwell said that the changes would remove any disincentive for foreign domiciled companies to take profits in the UK.

Under double taxation agreements, tax credit refunds are allowed to parent companies in a small number of overseas countries (including the USA) when their UK subsidiaries remit dividends home. It is not clear what point the CCAB wish to raise on this aspect of the corporation tax changes.

LINE TO TAKE

Inward investment

The attraction of a 35% corporation tax rate will not be lost on multinationals considering the future location of investment in this country, and in the people of this country.

Outward investment

The reduction in the UK corporation tax rate to 35% does not necessarily bear more harshly on overseas investment than on domestic investment. What it does mean is that overseas rates, to the extent that they cease to be absorbed by the UK Exchequer, become a more marked influence in affecting outward investment by multinationals.

Double taxation

It is too early to predict the likely negotiating stance which other countries may adopt in response to our corporation tax reform package. We have had no indication other countries will regard UK as a tax haven. If CCAB have a detailed point on tax credit refunds, could they write?

Point 2A CONTROLLED FOREIGN COMPANIES: GENERAL

1. The CCAB played an active part in the lengthy consultation period which led up to what are now Clauses 80-89 and Schedules 16-18 of the Finance Bill. If anything, their attitude towards the CFC proposals has hardened during this period and in their latest (January 1984) representations they stressed "the proposed legislation is unnecessary and should not be introduced".

2. Their main criticisms largely repeat points made on previous rounds of consultation, viz:

   (i) the "blunderbuss" approach - any legislation should be targetted on known abuses;

   (ii) the potential for damaging the international competitiveness of UK business;

   (iii) the failure to reform (though not necessarily repeal) Section 482 ICTA.

   On a more detailed level, the CCAB also takes issue with the drafting of the current provisions. Unusually their major quarrel seems to be, not with the motive test, but with the rules for computing a CFC's chargeable profits and with the failure to adopt a "deemed dividend" approach.

3. Line to take

   (a) Ministers took full account of the points of principle made by the CCAB and others before deciding to go ahead with legislation this year.

   (b) In the Government's view, legislation broadly on the lines of that now included in the Finance Bill is the only way effectively to deal with what virtually everybody recognises as real abuse, whilst providing specific protection for all "genuine" overseas activity.

   (c) But on the detail of the provisions, Ministers' minds are not closed. Any specific amendments put forward by the CCAB will be sympathetically considered.

   (d) If Section 482 is raised. Ministers accept that, once the CFC legislation is on the statute book, they will need to look again at Section 482.

Part 2B CONTROLLED FOREIGN COMPANIES: LIST OF NON-HAVENS

1. The CCAB's latest comments on the CFC 'packages' predate the appearance (on 29 March) of the revised list of non-havens. In those comments they asked for any such list to be given statutory force, so removing the scope for Revenue "discretion". This, they felt, would reduce the present area of uncertainty.

2. Although the CCAB have not themselves specified their "particular objections" to the revised list, there has been criticism of this list expressed both in the financial press and by a number of the other major representative bodies. This criticism has centred on:

   (i) the existence of the caveat, which effectively removes the protection of the list from "avoidance" cases, and - they say - severely limits the value of the list;

   (ii) the possibility of retrospective changes: and

   (iii) the discretion afforded to the Revenue in operating the list.

   May critics have concluded that the only way to resolve these problems is to make the list statutory.

3. The current list can, we believe be defended. But, given the strength of the criticism, the Revenue will shortly be putting up a note reviewing the various options for change.

4. Line to take

   (a) to listen to what the CCAB have to say on the list [and to assure them that any points they make will be fully considered].

   (b) If called on to justify the inclusion of the caveat. The caveat guards against the possibility of overseas countries changing their tax laws and companies deliberately exploiting that change to avoid UK tax before the list itself can be amended.

(c) As explained before the Budget, alternative approaches - eg a statutory list - were considered. But the conclusion was that such alternatives would necessitate a much shorter list, and as such were considered to be less helpful to the business community [Nonetheless, these options can be looked at again.]

3. DOUBLE TAX RELIEF

The CCAB's complaints

1. Although the CCAB claim that the reversal of set-off of ACT and DRT is not a real concession, nevertheless there was a good deal of support for the change in representations to the Corporation Tax Green Paper suggesting that it will be a useful one.

2. The CCAB describe the present DTR rules as remaining narrow and inflexible. It is assumed that this reflects what were referred to in the CCAB's CT Green Paper representations as the main difficulties which arise with the present DTR system -

a. the narrow source rules, and

b. the absence of any provisions for averaging foreign taxes or for carrying backwards or forwards unused tax credit relief.

3. In its comments on the October 1983 CFC draft clauses the CCAB said that the CFC proposals must be viewed in the light of the more restricted UK system of DTR, as compared with the/ /systems in many competitor countries, including those who have introduced similar proposals (eg the US). The CCAB hoped there would be an immediate review of the present UK system of DTR with a view to liberalising the use of available reliefs.

The present UK system

4. DTR, whether given under a double taxation agreement or under domestic law, is designed to remove the unfair burden when two or more countries impose tax on the same income. The effect of these arrangements is that the UK resident has broadly the same tax burden on income arising overseas as on income arising in the UK, provided that the overseas rate of tax is not higher than the UK rate. Where the overseas rate is higher than the UK rate, credit for the overseas tax is limited to the UK tax payable on the same income ie calculated on a source by source basis. In these circumstances, where there is insufficient UK tax to absorb all the credit for the overseas tax paid, the company can disclaim credit relief and claim a deduction for the foreign tax as an expense in earning the foreign income concerned.

The CCAB's suggestions

5. Aggregating overseas taxes to permit the averaging of foreign tax rates - "pooling" - would give more DTR than is now available. But it would contravene the general principle that relief should be given only for overseas tax borne on the same income. Also, it would tend to distort the pattern of investment by encouraging investment in low tax countries and might lead to the creation of low tax sources through artificial means. Some overseas countries allow pooling in giving relief

for foreign tax, others do not. The USA allows pooling but subject to complex rules and elaborate policing. Adoption of pooling in the UK would undoubtedly require lengthy and complex rules to identify foreign source income and to contain artificial schemes.

6. The suggestion to allow unused DTR to be carried forward or carried back is often associated with pooling, no doubt because pooling enhances its effect. Looked at on its own, the main argument for it is that other reliefs in the corporate sector can be carried forward/back, so why not DTR? But DTR involves allowing overseas tax against UK tax on the same income and it would offend against this principle to allow it against tax on other income of a different year. This argument particularly applies where carry forward/back might have the effect of relieving high tax rates overseas.

Line to take

7. In our view there is no case in principle for abandoning our present source basis of DTR in favour of something akin to the US pooling basis or indeed the French or German exemption system. Because it focusses on only part of the total tax system, the comparison with the DTR rules in other countries which have tax haven legislation can be somewhat misleading. But more generally we should see as serious objections to pooling its breach of DTR principles, its likely cost (possibly in excess of £m200 per annum and rising as profitability returns) and the administrative problems it would create. Similarly carry forward (carry back would breach the principle of only relieving double taxation of the same income).

8. In recommending to the previous Chancellor measures to extend the carry back of unused ACT and reverse the set-off of ACT and DTR (now clauses 51 and 52 of the present Finance Bill) as a response to representations to the CT Green Paper, the then Minister of State minuted that he saw no reason to breach the principle that relief be given only for overseas tax on a source by source basis.

9. In brief, double taxation relief is intended to relieve the burden of the double taxation which would otherwise arise when income arises in one country, flows to another and is taxed in both. That objective is achieved when the UK tax on the income is wholly relieved by the foreign tax paid on the same income and there is no case in principle for allowing any balance of foreign tax (ie excess of UK tax) to be carried forward or back or set-off (by pooling) against other foreign income, thereby shielding businesses from the effects of commercial decisions to invest in high rate countries.

FST MEETING WITH CCAB: FINANCE BILL 1984

4. Deep Discount Securities: legislation still too complex

The proposed new tax treatment of securities issued at a deep discount by companies (Clause 36 and Schedule 9) is that the discount is treated as income arising on a compound yield basis over the life of the security. The issuing company receives a deduction against its profits each year for discount accruing, but holders will only be taxed on disposal of the security (or at redemption) on the discount accrued during their period of ownership. The balance of the proceeds on disposal /redemption will be treated as a capital gain or loss.

The CCAB's criticism echos their representations on the Consultative Document on deep discount securities issued in January 1983. Their main plea was for a simple tax treatment, ideally for a charge to capital gains tax only on disposals, but giving income relief to the issuer. Alternatively, they preferred a straightforward income charge on the difference between the acquisition and disposal proceeds, or, in relation to an accruals basis option, a simple straight-line basis of discount accrual.

The CCAB's views were however in a minority on these latter points. Most representations felt that the profit on disposal should be separated into discount income and capital gain/loss and favoured the (more correct) compound yield basis of discount accrual. The legislation reflects this majority view.

Line to take

The legislation aims at a satisfactory tax regime to enable companies to issue deep discount securities. They will expect to receive relief for the discount against income and it follows that there should be an income charge on investors too (with low-coupon gilts, where capital gains treatment applies for investors there us not the same need to consider the borrower's tax position).

The legislation is admittedly complex but with the aim of providing clear and comprehensive rules. Adopting a straightforward income charge on profits on disposals or a straight-line basis for accruing discount would obviously have been simpler. But, unlike the CCAB, most representations to the Revenue's Consultative Document did not favour these.

5. OFFSHORE FUNDS

The CCAB suggest that the scope of the offshore fund provisions is too wide. They said the same in passing at a recent meeting on other issues with the Inland Revenue, but did not elaborate. and have not taken up an invitation to discuss their worries with officials.

The CCAB may suggest one of two things:-

(i) that the rules should be confined to roll-up money funds, or

(ii) that the provisions catch innocent foreign trading activities.

(i) Confining rules to roll-up money funds

Although the tax loss at which the new rules seek to prevent was concentrated in money funds, Ministers felt it would be wrong to single out a type of fund simply on the basis of the sort of investment it undertook. It would anyway be easy for money funds to disguise themselves as something else.

(ii) The risk of catching innocent foreign trading activities

There has been much fear expressed about this - including by the Law Society. Largely it has reflected misunderstanding. The main worry has been that foreign partnerships and similar arrangements might be caught. They will not be. The new rules build on the capital gains tax charge, and for CGT purposes a partnership is "transparent": its existence is in effect ignored, and a disposal of an interest in a partnership is treated as a disposal of a share of the underlying assets. Foreign partnerships are therefore not within the new rules.

The Financial Secretary may like to say that lengthy discussions between officials and Mr Avery Jones and the Law Society have established that foreign partnerships and similar arrangements are outside the scope of the new rules. But these discussions have identified some more detailed problems in relation to foreign consortia and joint ventures. The Government are looking at these problems urgently and where appropriate will be prepared to table amendments to the Bill.

6.SHARE OPTION SCHEMES

1. The CCAB indicate in their 'preliminary notes' that they welcome the Budget and Finance Bill proposals regarding share option schemes. They ask, however, "why not go further and also simplify the rules on share ownership by employees and directors".

2. This question is unclear, but we assume it is directed to the detailed conditions to be observed by approved share option schemes. These cover a range of matters - eg the particular shares which be used, the eligibility of directors and employees, the size, duration and frequency of exercise of options etc. They have been kept as simple as possible, consistent with the need to prevent or discourage abuse of the very significant tax reliefs provided, and to impose some upper limit on the relief.

3. The question may alternatively refer to Section 79 Finance Act 1972, sometimes suggested to be unduly complex and a source of great difficulty. As an anti avoidance provision, its purpose is to deter a company from setting up employee share schemes in a way that would enable it to pass remuneration to its employees in the form of capital rather than income and therefore income tax free. It is disapplied in the case of approved share schemes. We believe cases of genuine difficulty in this area are already infrequent, and will be more so with the introduction of new approved share option schemes (Section 79 is described more fully in Mrs Ayling's submission of 13 April).

4. Line to take: Budget and Finance Bill proposals on share option schemes have been generally welcomed. Deliberate attempt has been made to keep conditions for approved schemes as simple and few as possible, consistent with need to ensure policy objective is secured, and misuse of tax reliefs prevented. Several detailed points nevertheless have been raised, and any particular CCAB comments will be carefully considered, together with these others.

7. CAPITAL GAINS TAX

As items to consider for 1985, the CCAB suggest -

(i) The repeal of CGT and its replacement by an income tax charge on acquisitions and disposals within a year.

LINE TO TAKE

Ministers accept that the combination of the complexity of CGT and its diminishing yield as the indexation provisions have increasing effect, imposes the need for its early review. In his Budget Speech, the Chancellor said that it was a matter to which he hoped to return next year.

Premature to exclude possible options but experience of a tax on short-term gains (which applied in the UK from 1962 to 1965) is not reassuring - the period is inevitably arbitrary (6 months, 12 months or two years) and distortion to markets without yielding much revenue (since people simply sit out the relevant period).

(ii) Need for review and improvement to retirement relief.

LINE TO TAKE

The Consultative Document on CGT Retirement Relief which was issued on 22 March indicated the ways in which the Government thought the present relief might be amended. The CCAB will no doubt wish to submit its comments (requested by the end of May).

7(c) - ITEMS FOR 1985 - SHOULD CTT BE IMPROVED FOR THE COMFORTABLY OFF (SAY ESTATES OVER £100,000)

Background

The CCAB will probably point out that the CTT threshold has been raised in real terms, although in part by the expedient of abolishing the bottom four rate bands in 1980. The present Finance Bill abolishes the top three rate bands. Relatively little has been done for the middle range, where the real burden of the CTT rates is greater than under the 1975 Healey rate scale (though the CTT reliefs have been significantly improved since the original Healey rate scale was proposed).

Line to take

The CTT threshold is around 40% higher in real terms than in 1978/79. Statutory indexation has since 1983 provided a long-stop against the erosion of the tax bands by inflation; and inflation itself is of course greatly reduced.

The reduction in CTT rates in Clause 98 of this year's Finance Bill brings both financial and presentational benefits. The top rate on lifetime transfers will now be 30% where the donee bears the tax; business and agricultural relief can effectively reduce this to 15%.

The Opposition constantly complain that very substantial sums can be given away by those willing and able to use the existing exemptions and reliefs, though examples quoted are often artificial. What, however, do the CCAB see as the problem areas in CTT?

If the CCAB want reductions in the middle rates of tax, would they accept there is less of a case for generous reliefs (eg for businesses and agriculture) if tax rates come down?

[IF RELEVANT: If the CCAB argue for simplification of CTT, do they accept that there will be anomalies and rough edges? Or might this be too great a price to pay?]

accruing in any previous year of assessment, any allowable losses accruing to that person in any previous year of assessment.'

At this stage it would appear that allowable losses accruing to non-resident trustees may be subtracted from current or future chargeable gains before establishing the amount of gains capable of apportionment under section 42 (2). However, section 23 (6) provides that:

> 'A loss accruing to a person in a year of assessment during no part of which he is resident or ordinarily resident in the United Kingdom shall not be an allowable loss . . . unless, under section 20 (2), he would be chargeable to capital gains tax in respect of a chargeable gain if there had been a gain instead of a loss on that occasion.'

It has previously been considered uncertain whether section 23 (6) precludes losses arising to non-resident trustees being subtracted from chargeable gains realized by those trustees before apportioning the net chargeable gains, if any, to the United Kingdom resident beneficiary. This doubt has now been removed, following the judgment of Mr Justice Nourse in *Ritchie (HM Inspector of Taxes) v McKay*.

In 1968 the wife of the taxpayer settled property on non-resident trustees. During 1974–75 the trustees suffered capital losses of £41,536. In the following year, 1975–76, the trustees realized chargeable gains of £3,405. The settlor's husband was a beneficiary residing in the United Kingdom and, invoking section 42 (2), an assessment was made on him in the sum of £3,405. The taxpayer maintained that the chargeable gain should be reduced to nil by utilizing losses realized in 1974–75.

One of the submissions, advanced by the Crown before the High Court, was that section 42 (2) confined consideration to events taking place in the year of assessment 1975–76. Nourse, J. declined to accept this view as, in his judgment, section 20 (4) produced a different result. It would be unnatural to restrict section 20 (4) by excluding losses from the application of section 23 (6). Therefore, the taxpayer, a beneficiary resident in the United Kingdom, was entitled to subtract losses incurred by the trustees in the previous year, and the chargeable gains apportioned to him for 1975–76 were reduced to nil.

Section 42, Finance Act 1965 was subsequently consolidated in section 17, Capital Gains Tax Act 1979. This latter section ceased to apply for chargeable gains accruing to non-resident trustees after 5 April 1981. It is perhaps significant that section 84 (6), Finance Act 1981, introducing the new legislation, specifically allows unrelieved losses of non-resident trustees to be subtracted from future chargeable gains which may be apportioned to beneficiaries.

CCAB changes

Some criticism has recently been expressed of the cost incurred in maintaining, and also the effectiveness of, the Consultative Committee of Accountancy Bodies. This is a joint body which coordinates submissions and responses made by the six leading accountancy bodies in the United Kingdom. At a recent meeting attended by presidents of the six bodies, it was recommended that, for a trial period of two years, the responsibility for making responses to Government and other organizations in matters arising in the Parliamentary law area should be dealt with by each body independently. This will substantially increase the number of representations and responses made, although it was also recommended that in future office holders of all bodies should meet half-yearly.

Insolvency law

Responding to the Government White Paper, *A Revised Framework for Insolvency Law*, the Society of Company and Commercial Accountants records several reservations. The Society is unable to accept that there has been wide-spread malpractice amongst insolvency practitioners, and urges that, in seeking to curb abuses by a small minority, significant additional costs should not be incurred. In particular, the Society questions whether all practising solicitors and members of accountancy bodies should be accepted as insolvency practitioners, and points out that many have little or no practical experience in this field.

Nor does the Society accept that directors of companies which are wound up by the Courts should be automatically disqualified from being a director of a company. It comments there are advantages in arranging for companies to be wound up by the Courts, as the process is quicker than either a Members' or a Creditors' Voluntary Liquidation, and the practice is widely used, particularly in Scotland.

Automatic disqualification, it is argued, would deter businessmen from accepting directorships of companies which are in trading difficulties. Such companies need the skills of highly qualified businessmen to save them from extinction, to preserve jobs and to minimize losses to creditors. The Society rejects the sweeping statement in the White Paper that 'directors who allow their companies to arrive at a state of affairs where they are wound up compulsorily by the Court have demonstrated that they are not fit to be in control of a company'.

The Society argues that refusal to accept the Cork Report recommendations to improve the position of unsecured creditors should be reconsidered.

TAXATION INDEX

This week's issue contains an index for the issues of *Taxation* falling in the six-month period ended 31 March 1984.

Equitable Life

A great deal of discussion is currently taking place on the 'portability' of pension rights. Contributing to this discussion, the Equitable Life Assurance Society points out that all its individual pension contracts allow complete portability. These contracts are the retirement annuities for the self-employed and for employees in non-pensionable employment, approved under section

astms Economic Review

THE BUDGET

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SPRING 1984 VOLUME 9 No. 1

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ASTMS ECONOMIC REVIEW VOL IX No. 1

Contents

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The Economy

SUMMARY

1. The Chancellor claimed that 'economic recovery is well under way', but unemployment continues to increase and redundancies are still occurring at a high rate.

2. Far from being 'neutral', the recent Budget was deflationary. Its thrust was concealed by a complex juggling of tax rates and promises of future benefits, which the Government is unlikely to be able to deliver.

3. The Government's medium term policy does not seek directly to stimulate the growth of output and employment. It is concerned only to switch resources from public spending into lower taxes and cut borrowing in a fashion which will widen inequality and depress growth prospects.

4. Our deduction, from the Government's economic forecast, is that they expect a growth in output during the next five years which will be insufficient to stop unemployment rising.

5. The rate of growth in consumer spending will be halved in 1984. In 1983, contrary to Ministers' admonitions about 'living within one's means', it was credit which supported higher spending. In 1984, it will be increased earnings, in excess of Government norms, which will provide the main support.

6. Investment in industry is now rising at a modest rate, due to the usual 'too little too late' reaction to increased home demand. Overseas investment by pension funds continues to increase at a high rate, undermining the future security both of the jobs and possibly the pensions of scheme members while undermining the rates and tax base.

7. World markets will grow faster than the UK market in 1984 but despite this, UK imports will continue to grow faster than exports.

8. A further reduction in inflation has been proclaimed as the central objective of the Government's economic strategy However, inflation is likely to be fractionally higher in 1984 than in 1983.

PART I

THE ECONOMY

1 EMPLOYMENT

The Chancellor has claimed that 'economic recovery is well under way', but unemployment continues to increase and redundancies are still occurring at an unacceptably high rate.

1.1 The total number of people unemployed and claiming benefits in March 1984 was 3,143,000, of whom 95,000 were school leavers. This increasingly artificial figure understates the real level of unemployment by one-third.

1.2 At the end of February 1984, 658,000 people were covered by the Government's special employment and training measures. The officially estimated impact of these schemes on the unemployment figures was to reduce them by 460,000, and although they are aimed mainly at young people, the unemployment rate for those under 20 at the end of last year was 27%.

1.3 In the first three months of 1984, unemployment, on the official figures, rose by an average of 23,000 per month. These figures contrasted with the zero average increase recorded in the second half of 1983, which had been an apparent improvement on average increases of 25,000, in the first half of that year.

1.4 While it seems likely that the unemployment trend improved slightly in the second half of 1983, the official figures overstated this for two principal reasons. FIRSTLY, in the period after August, official figures did not allow for men of 60 (or over) who were dropping off the register as a result of changes in benefit regulations. We estimate that this amounted to as many as 10 000 a month in the August to December period. SECONDLY, the number of people, other than school leavers, kept off the register by the Government's special measures increased significantly. Most notably, the number of unemployed 18-24 year olds recruited into Community Programme schemes rose by 50,000 to 115,000 between June and December.

1.5 Re-employment prospects for people losing their jobs remain poor. For example, in the latter part of 1983, statistics on the length of unemployment suggested that over two-fifths of all men aged 50-54 and one-third of all men aged 20-24 who lost their jobs would still be unemployed a year later.

1.6 The Department of Employment estimates that the total number of people employed increased by 40,000 in the third quarter of 1983. This appears to have ended, temporarily, a three and a half year continuous decline in employment during which 2.1 million jobs disappeared.

1.7 Full figures for the last quarter of 1983 are not yet available but it is likely that a further small increase in employment took place. However, even if this proves to be the case, the average number employed in 1983 will still have been 250,000 less than in 1982.

1.8 The change in the trend in employment has taken place because the much reduced rate of job loss in production industries has been more than offset by increased employment in service industries.

1.9 Redundancies are still, however, occurring at a high rate which shows little sign of decelerating. The Manpower Services Commission's figures for redundancies confirmed as occurring and involving more than ten workers in 1983, was 312,000.

1.10 There is likely to be a small increase in employment during 1984, but unemployment will also rise by an average of 10,000-15,000 per month. The Government will continue to present each small change as the indication of economic recovery but in truth has clearly accepted a central core of unemployed people numbering 3-4 million.

2 THE BUDGET

Far from being 'neutral', the recent Budget was deflationary. Its thrust was concealed by a complex juggling of tax rates and promises of future benefits which the Government is unlikely to be able to deliver.

2.1 Prior to the Budget, the Public Sector Borrowing Requirement, expressed as a percentage of GDP, was 35% lower than the average for major OECD countries. If the same comparison were made on an adjusted basis so as to account for higher unemployment and borrowing by nationalised industries, the UK deficit would be even lower in relative terms. Despite this the Chancellor has decided to reduce borrowing even further, i.e to make policy more deflationary.

2.2 If Government borrowing had been held at the same level as last year, it would have been possible to increase public spending and/or cut taxes by over £3 billion (equivalent to 1% of GDP). While the Chancellor claims his Budget is 'neutral', he has in fact retained for the Exchequer the additional taxes paid last year as a result of the increased level of economic activity. This revenue could have been used to sustain rising demand; instead, it is now helping to slow it down.

3.3 The tax increases and tax cuts announced in the Budget were almost equal in effect.

2.4 Income tax allowances were increased in advance of inflation. Those on lower incomes, not subject to the claw-back of means tested benefits, received the greatest benefit relative to their existing income. Increases in indirect taxes were such as to offset most of the income tax cuts. People who continue to smoke, drink beer, buy take-away food (while making alterations to their homes) will pay relatively more tax, whilst wine and spirit drinkers will pay less. Overall, however, the average family will still be paying 5p in the pound more in tax than five years ago.

2.5 Abolition of the investment income surcharge and the reduction in stamp duty will provide a considerable benefit to those on the highest incomes. However, the largest net benefit, in terms of the cost to the Exchequer, goes to business, which will gain by over £600m from the reduction in corporation tax and the abolition of the investment income surcharge. The Chancellor has balanced his books by requiring, as from October, earlier payment of VAT on imports. This in effect gives him fourteen months revenue in one year.

2.6 While total public expenditure is budgeted to rise by 5% in cash terms in 1984/5, the Government is seeking a reduction of 2% in Local Authorities' spending. After allowance for inflation, this would represent a cut in real terms of 7%. This reduction is counterbalanced within the planning total by increases in other programmes, notably Defence and Social Security.

2.7 Local Authorities are being asked to cut expenditure on passenger transport subsidies and concessionary fares by 40%, on education by 7½%, and on social services and road maintenance by 5%. Previous attempts by the Government to force Local Authorities to implement cuts by a general reduction in Government grants and selective financial penalties have met with only partial success. An increased scale of penalties, coupled with the future prospect of rate-capping, will substantially increase Government pressure on Local Authorities.

2.8 A cash limit has now been extended to the total amount budgeted for public expenditure. The Treasury has specified that any new spending measures announced during the year, together with any spending over and above that planned for 'demand-determined' programmes (e.g Social Security), will be met out of the contingency reserve. Previously the reserve had been used to cover overspending on cash limited programmes. Cash limits on public sector pay have also been tightened by the Treasury's policy of seeking to limit increases in the pay bill to 3% after allowing for the effect of manpower savings.

2.9 We anticipate that, despite some higher spending by Local Authorities than the Government would wish, public spending in 1984 will be the same as in 1983.

3 GOVERNMENT STRATEGY

The Government's medium term policy does not seek to stimulate directly the growth of output and employment. It is concerned only to switch resources from public spending into lower taxes and cut borrowing in a fashion which will widen inequality and depress growth prospects.

3.1 In the revised 'Medium Term Financial Strategy' for its second term of office, the Government's central objective is to keep public expenditure at its present level, in real terms. Increased real spending on defence will squeeze other programmes, and Social Security benefits will be frozen in real terms (the effect of this on the longer-term future of the state pension scheme is discussed in the pensions section of this Review.

3.2 The freeze in public spending is designed to make room for a reduction in taxation and also to allow a further cut in Government borrowing as a share of GDP. By holding down Social Security benefits and depleting the social wage while cutting the taxes of those in work, this strategy will dramatically widen inequality. This would fit in with the Government's aim of seeking to make people work for low wages and salaries.

3.3 However, this approach is likely to fail for two principal reasons. FIRSTLY, spending is unlikely to be contained within the prescribed limits, most notably because inflation will not continue to fall as the Government assumes. SECONDLY, economic growth, and hence tax revenues, will fall short of the levels set out in the strategy.

3.4 The Government's strategy has to be judged against the background of their economic forecast, which implies a continuing slow increase in unemployment (see Section below). Despite this the M T F S does not seek to influence directly the level of output and employment in the economy. It seeks only to divide up the increase in tax revenues which accrue from the modest growth in output in this laisser-faire framework. The priorities which they favour in this division, ie tax cuts and reductions in borrowing, are those least likely to boost employment. Tax cuts tend to be spent in large part on imports while reductions in Government borrowing directly reduce demand levels. An increase in public expenditure, the option most effective in increasing employment, is ruled out.

4 Output

Reading between the lines of the Government's economic forecasts, it is apparent that they expect a growth in output during the next five years which will be insufficient to stop unemployment rising.

4.1 The 'Gross Domestic Product' (i.e the economy's overall output), increased by 2% in 1983. The Government claims that the real figure was 3%, but all it has done is to change the statistical measure of growth which was traditionally used without any convincing statistical or economic evidence to support it.

4.2 The output of all production industries was 3.9% higher in the fourth quarter of 1983 than it was in the fourth quarter of 1982, but Table 1 shows that the increase in output 'year on year' was rather less. In addition, this output growth was heavily dependent on North Sea oil and gas development. Table 1 also illustrates how far output remains below 1979 levels.

Table 1 : Output of Production Industries 1983

	Change Since 1979	Change Since 1982
All Production Industries	- 6%	+2.5%
Extraction of North Sea Oil and Gas	+39%	+10%
All Other Production Industries	-12.5%	+1.5%

[Source : C.S.O]

4.3 Manufacturing industries increased their output by 1.4% in 1983, though output in the fourth quarter of 1983 was 3.6% higher than a year earlier. The performance of different sectors of manufacturing industry varied widely, notably within the engineering industries, as shown in Table 2.

Table 2 : Engineering Industries Output in 1983

	Change Since 1979	Change Since 1982	4th Quarter 1982 to 4th Quarter '83
Mechanical Engineering	-22%	-5.4%	-1.5%
Electrical & Instrument Engineering	+2.6%	+7.3%	+8.3%
Motor Vehicles	-27.3%	+5.7%	+9.6%
Other Transport Equipment (Aerospace, Rail, Shipbuilding &c)	+4.8%	-4.2%	-5.5%
Metal Goods (not elsewhere specified)	-21.1%	+2.1%	+5.8%

[Source : C.S.O]

4.4 Exports of manufactured goods fell by 2% in 1983, which means that production for the home market rose by about 2½%. This compares with a 12% increase in the volume of imported manufactures. Diagram 1 focuses on consumer goods and shows how rising imports have pre-empted a revival of UK production in response to rising consumer demand.

4.5 The economy's total output is likely to rise by only 1% from present levels during the course of 1984. This implies a monthly average output level in 1984 which is 2% higher than in 1983.

4.6 The National Institute for Economic and Social Research (NIESR), in their November 1983 review, published an economic forecast for the next five years. On present policies, this showed economic growth averaging only 1½% per annum and an increase in unemployment of 100,000 each year over the period.

4.7 In the Financial Statement and Budget Report (FSBR), the Government projects economic growth as likely to average 2¼% per annum over the next five years, but it makes no forecast for unemployment.

4.8 The difference between NIESR and Government views of economic growth is smaller than is evident at first sight because of the different measures of economic growth used in the forecasts - NIESR use the conventional 'output' measure of GDP growth; the Government has switched to the higher 'average estimate'.

4.9 The FSBR projects productivity gains 'well above' the 1% per annum average rate recorded in the 1973-9 period. The officially projected increase in the size of the labour force over the next five years is 0.5% per annum.

4.10 If these forecasts are put together with those for growth, then the unspoken conclusion for unemployment emerges. This is that the Government recognise that while there may be a small increase in employment, unemployment will continue to rise during the next five years.

5 Consumer spending

The rate of growth in consumer spending will be halved in 1984. In 1983, contrary to Ministers' admonitions about living within one's means, it was credit which supported higher spending. In 1984, it will be increased earnings, in excess of Government norms, which will provide the main support.

5.1 Consumers' expenditure in 1983 was 3.8% higher, in real terms, than in 1982. This increase far exceeded the growth in consumers' real disposable incomes, which appear to have risen by about 1%. The difference was financed by a major increase in consumer borrowing; the amount of credit outstanding rose by almost a quarter during 1983.

5.2 The volume of retail sales rose by 5.3% in 1983. Sales in the last quarter of 1983 were 1.8% higher than in the previous quarter and 6.2% higher than in the last quarter of 1982. In January and February of 1984, retail sales dropped by 2% as compared with sales in the last quarter of 1983 but remained marginally above the monthly average for 1983.

5.3 Average earnings rose by 7¾% in the year ending in December. The underlying level of increase was unchanged in the second half of 1983. Earnings in production industries were 9¼% higher in December than a year earlier, reflecting increased overtime working and a reduced incidence of short time working.

5.4 The level of wage settlements in the private sector has varied considerably, though very few are now below the rate of inflation and there is some evidence of an upward trend. Settlements in the public sector are generally lower and are under pressure from a Government cash limit of 3%.

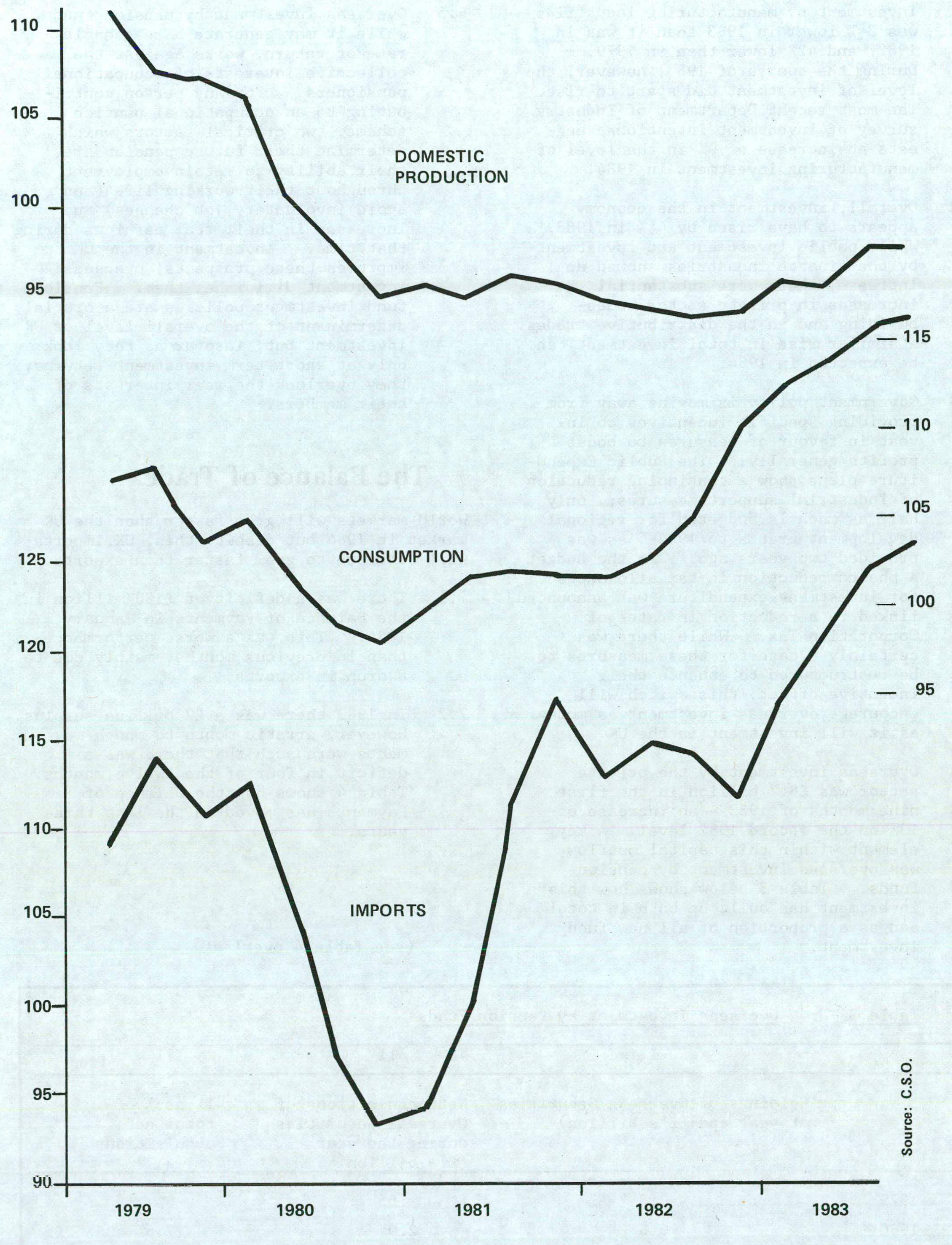
5.5 The Budget will have only a very marginal impact on consumers' purchasing power in 1984. This will be offset by the reduced value of Social Security benefits, resulting from their being increased by 1% less than inflation last November.

5.6 There will be little further growth in consumer spending in 1984. However, because of the increase during 1983, the average level of spending in 1984 will still be 2% higher in 1984. An increase in average earnings rather than a reduction in consumers' net savings, will be the main factor sustaining consumption.

6 Investment

Investment in industry is now rising at a modest rate, i.e the usual 'too little, too late' reaction to increased home demand. Overseas investment by pension funds continues to increase at a high rate, undermining the future security both of the jobs and the pensions of pension scheme members.

DIAGRAM 1: PRODUCTION, CONSUMPTION & IMPORTS OF MANUFACTURED CONSUMER GOODS



6.1 Investment by manufacturing industries was 3½% lower in 1983 than it was in 1982, and 42% lower than in 1979. During the course of 1983, however, the level of investment did start to rise. The most recent Department of Industry survey of investment intentions suggests an increase of 9% in the level of manufacturing investment in 1984.

6.2 Overall, investment in the economy appears to have risen by 4½% in 1983. While public investment and investment by the finance industries showed no increase, there were substantial increases in private sector housebuilding and in the distributive trades. A similar rise in total investment can be expected in 1984.

6.3 Government policy is moving away from providing specific incentives to invest in favour of measures to boost profits generally. The Public Expenditure plans show a continuing reduction of industrial support measures; only half as much is budgeted for regional development grants to 1984-5 as was provided two years ago. In the Budget a phased reduction in tax allowances for investment expenditure was announced, linked to a reduction in rates of Corporation Tax. While there was certainly a case for these measures to be restructured to enhance their incentive effect, this switch will encourage overseas investment as much as it will investment in the UK.

6.4 Overseas investment by the private sector was £8.7 billion in the first nine months of 1983 - an increase of 13% on the record 1982 level. A key element within this capital outflow was overseas investment by pension funds. Table 3 below shows how this investment has built up both in total and as a proportion of all new fund investment.

6.5 Overseas investment by pension funds, while it may generate a reasonable rate of return, works against the collective interests of occupational pensioners. For any person contributing to an occupational pension scheme, two critical factors which determine their future pension are their ability to retain employment throughout their working life (and avoid involuntary job changes) and increases in their real earnings during that time. Investment in the UK improves these prospects, overseas investment diminishes them. Pension fund investment policies are a crucial determinant of the overall level of UK investment but, insofar as they look only at short term investment returns, they overlook the real interests of their members.

7 The Balance of Trade

World markets will grow faster than the UK market in 1984 but despite this, UK imports will continue to grow faster than exports.

7.1 There was a deficit of £130 million in the Balance of Payments in January 1984. This was a worse performance than in previous months, mainly due to a drop in exports.

7.2 In 1983 there was a £2 billion surplus. However, erratic month to month movements were such that there was a deficit in four of the twelve months. Table 4 shows how the Balance of Payments has moved in the last three years.

(see Table 4 overleaf)

Table 3 : Overseas Investment by Pension Funds

	I	II	III
	Holdings of Overseas Securities at year end (£'s billion)	Net Acquisitions of Overseas Securities during the year (£'s billion	II as % of total net acquisitions
1979	3.3	.55	6%
1980	6.6	2.0	17.5%
1981	10.7	2.4	20%
1982	15.9	3.2	25.7%
1983 (nine months)	-	2.2	24%

[Source : Financial Statistics]

Table 4 : Balance of Payments 1981-1983 (All fig's £'s billion)

	Total Trade	Oil	Trade in All Other Goods	'Invisibles'
1981	+6.5	+3.1	+1.4	+2
1982	+5.4	+4.6	-2.5	+3.3
1983	+2.0	+6.9	-7.9	+3

Notes : (1) 'Invisibles' are services and current financial transfers.

(2) '+' figures are trade surpluses

'-' figures are trade deficits.

7.3 The deterioration in UK trade in goods (other than oil), occasioned largely by a massive increase in imports, was equivalent in 1983 to over 2% of the value of the UK output. This is a measure of the degree to which the 'recovery' in demand has bypassed UK industry.

7.4 Imports of manufactures rose by 5% in volume in the last quarter of 1983, and by 12% in 1983 as compared with 1982. Manufactured exports, while they increased by 7% in the last quarter of 1983, were 2% lower in 1983 than in 1982.

7.5 Earlier payment of VAT by importers while helpful to the Chancellor's Budget strategy, will not restrain imports significantly. Insofar as it applies across the board, and therefore covers materials and semi-manufactures, it will be a mixed blessing for UK industry.

7.6 In 1984, exports should be helped by faster growth in world trade; this is expected to increase by 5% as compared with around 1% in 1983. Total UK exports should rise by 3-5%. Imports of manufactures should rise more slowly than in 1983, as consumer spending growth will be lower. We expect total imports to rise by 5-7%. On the basis of these forecasts we anticipate a small deficit of £1 billion on the Balance of Payments in 1984.

8 Inflation

A further reduction in inflation has been proclaimed as the central objective of the Government's economic strategy. However, inflation is likely to be fractionally higher in 1984, than in 1983.

8.1 The increase in prices in the twelve months ending in January 1984 was 5.1%. The average monthly increase in prices in the preceding six months was 0.3% per month.

8.2 Prices of imported goods have been exerting some upward pressure on inflation. Unit values of imports are currently 10% higher than a year ago. This pressure is reflected both in the cost of industry's raw materials, up 7% on the year to January, and in the prices of some finished goods, where importers seem to be taking advantage of a buoyant market.

8.3 The increases in excise duties and the extension of VAT, as announced in the Budget, will add rather less than 1% to the level of retail prices. This is about twice the size of the corresponding impact of increases in expenditure taxes last year. Significantly, the extension of VAT and the withdrawal of tax relief from life assurance barely affect the Retail Price Index. This is because the items affected are either not included at all or are not fully taken into account in the basket of goods whose prices are measured for the purposes of calculating the RPI.

8.4 A smaller average increase in Council rents and rates this Spring than last year, and the cut in building society mortgage rates, announced after the Budget, will serve to reduce inflationary pressure.

8.5 Inflation is likely to remain within a 5-6% range throughout 1984.

Pensions Supplement

INTRODUCTION

Our objectives in this special Pensions Supplement are three-fold. Firstly, to issue a warning. In our view, as a direct result of Government policy now confirmed in the recent Budget, the ability of state and occupational schemes to provide adequate pensions is being questioned. But it is primarily being questioned by a government whose very own policies are directly responsible for speculation, if not a crisis of confidence about the future. This has enabled the Government to begin to justify the breaking of the previous consensus and talk quite openly about changes or solutions to its perception of the problems that will radically alter the way in which our citizens get an income during retirement. As we will demonstrate, their plans and policies are retrogressive and wrong.

Secondly, to comment analytically on the current shortcomings of occupational pension schemes and to put into context the erosion of the value in real terms of the state pension that has occurred during the stewardship of this Government.

Thirdly, to offer our conclusions on the reforms that need to be made in order to provide adequate pensions and in the case of occupational schemes to ensure that schemes become more susceptible to democratic control.

PART II

1 Pensions in Perspective

The ability of the state to provide adequate pensions and that of the private sector to cope with a changing workforce both in terms of its size, shape and constancy, has been pushed nearer to crisis as a direct result of Government policy.

1.1 The depressed economy and the reducing workforce has led to pensions being an increasingly vital issue for hundreds of thousands of our fellow citizens who would not normally have had to worry about their pensions until they approached their normal retirement date.

1.2 Retirement is no longer something that will nearly always occur between 60 and 65. For many people it has been forced upon them many years in advance of their expected normal retirement date.

1.3 Officially, early retirement occurs between 55-60, where employers have persuaded or forced their employees to take "early retirement". The value of both the state and the occupational pension is of immediate concern to these people.

1.4 Unofficially, but with no less an effect on the victims' expectations, hundreds of thousands have been 'retired' by redundancies and closures and will never work again. This concern likewise is with the ultimate worth of the state pension, but if they were members of an occupational scheme they are also, along with the early leaver who takes another job, concerned with the value of the pension left behind in their occupational scheme.

1.5 Occupational schemes are based on relative economic and employment stability and as such have geared their provisions towards the forty year man (and we do mean man). Current and prognosticated economic conditions imply that the numbers who will qualify, or even get close to this mythical status, are declining and will decline still further. This makes the ability to earn the maximum pension to all intents and purposes simply notional. Short periods of service are more likely.

1.6 Today's new starter in even a relatively stable employment, such as insurance, can no longer look forward to a job for life and yet he or she will be offered a pension scheme based on that assumption.

1.7 The economic strategy pursued by the Government and now confirmed in the recent Budget, presupposed in their terms, tighter control of public spending. In our terms, this will mean further actual cuts in public spending. The provision of the state pension is a major component of public spending.

1.8 Each cut, together with depressed domestic investment and an increasing number of persons dependent on benefits even before normal retirement date, will, if it has not already done so, raise the question of the state's ability to provide an adequate pension. Certainly, as we shall demonstrate later, it has already led to a devaluation in real terms of the state pension.

1.9 We may summarise the issues that we should be concerned with as follows :

(i) The state pension is being devalued in real terms.

(ii) The burden of providing adequately on a depressed and non-productive economy will approach crisis point if current policies continue.

(iii) Occupational schemes no longer provide for the changing employment pattern.

(iv) Early leavers from occupational schemes have a legitimate case as casualties of a system which assumed stability.

(v) The general failure of occupational pension schemes to cope with the effect of inflation on deferred pensions and pensions in payment.

(vi) The threat to the majority of occupational scheme members from a move towards portable pensions.

2 The Current Scene

STATE PENSIONS

It is our contention that the Government has deliberately instigated the devaluation in real terms of the state pension. This has been done in such a way as to not only affect the basic state pension, but will, unless countered by subsequent substantial increases in the state pension, affect Earnings Related pensions also.

2.1 We believe that such counter measures are unlikely from a Government which clearly has other priorities and whose own economic strategy will exacerbate the relative costs to the Exchequer of providing civilised pension levels.

2.2 The essential objective of pensions provision is to provide a basic pension which is reasonable relative to the incomes of people in work, and for any individual, an earnings-related or occupational pension which is reasonable relative to his or her own income when they were in work.

2.3 By breaking the link between state pensions increases and earnings increases, the Government has cut off present and prospective recipients of the basic state pension from any increase in general living standards. As a result of this measure there has been an effective cut of £2.85 in the single pension and £4.40 in the married pension in just three years. When pensions are next increased in November 1984, the prospective increase at 5½% will fall short of earnings growth by 2-3%. The Government have also curtailed the ability of pensioners to secure higher earnings-related state pensions and the protection afforded by the GMP.

2.4 Although state pensions have been downgraded, National Insurance contributions have been sharply increased. This is explained by the fact that NI contributors and pensioners are carrying the cost of mass unemployment.

2.5 The recent cuts have fundamental long-term implications. A link between pensions increases and earnings increases keeps pensioners in line with rising living standards. If pensions are linked only to prices, then pensioners' incomes will fall as a proportion of the income of those in work.

2.6 At present the single person's flat rate pension is equivalent to approximately 22% of the amount of Average Earnings. In Table 1 below, we show how this proportion would fall if just a small gap between earnings increases and pension increases persisted.

Table 1 : Flat-rate Pension as a Proportion of Average Earnings

Earnings increases exceed pensions increases by :	Now	In 20 Years	In 40 Years
(a) 1%	(22%)	18%	14%
(b) 2%		16%	10%

2.7 The earnings-related tier of the state pension scheme and the GMP were intended to build, on top of a maintained flat-rate pension, a real advance in pensioners' relative living standards in future years. However, the earnings-related tier's scope is determined by the size of the flat-rate pension. Smaller flat-rate pensions mean that the potential size of earnings-related pensions is reduced.

2.8 In Table 2, below, we show the maximum possible pensions which can be generated under the state scheme on different assumptions about indexation.

2.9 The maximum earnings related pension is equal to 25% of earnings between the Lower Earnings Limit (LEL), equal in amount to the flat-rate pension, and the 'Upper Earnings Limit' (UEL), which is seven times the LEL. If the basic

Table 2 : Maximum State Pensions as a Proportion of Average Earnings

	SCALE OF PENSION	I Equal to Earnings	II 1% less than Earnings II(A) In 20 years	II(B) In 40 years	III 2% less than Earnings III(A) In 20 years	III(B) In 40 years
1	Basic Pension/Lower Earnings Limit	22%	18%	14%	16%	10%
2	Upper Earnings Limit	154%	126%	98%	112%	70%
3	Maximum Earnings Related Pension	33%	30%	28%	29%	27%
4	Maximum Total State Pension	55%	48%	42%	45%	37%

flat-rate pension falls as a proportion of earnings, so also does the range of incomes on which earnings-related pensions can be accumulated. The figure of 25% above, derives from the fact that earnings-related pensions are calculated by adding together 1/80th of the annual earnings between the UEL and LEL in the twenty best years prior to retirement. For this purpose, earnings in the years prior to retirement are revalued in line with the movement in Average Earnings for each year up to retirement date.

3 Occupational Pensions

From a trade union viewpoint, pensions are deferred pay. Pension benefits constitute an integral part of the remuneration package. In the public sector, the value of pension benefits has been recognised explicitly in the process of salary determination.

3.1 The distinction made between employee and employer contributions and between contributory and non-contributory schemes, loses significance in this light. For practical purposes it is best simply to think of pay and deferred pay, where the latter is promised pension benefits or the total pension contribution. In this context there is an implied assumption that the employer will make up the balance of contribution required to meet the cost of schemes' promised benefits.

3.2 A principal difficulty with this approach is that pension schemes' benefits are not exactly specified. For example, most private sector schemes promise only discretionary increases in pensions in payment. However, a scheme providing full indexation requires twice the resources of one providing none. Clearly, the exercise of discretion has a fundamental impact on the required level of contributions.

3.3 The legal position reflects and extends this uncertainty. It is generally held that an employer is not normally liable for their pension scheme's promised benefits. Nor, indeed, is the scheme itself. In practice, a pension scheme's liabilities only exist to the extent that there are funds available to meet them. The only guarantee which scheme members have is that pension will not be less than the Guaranteed Minimum Pension, or that pension which would have accrued had they been contracted-in to the State scheme.

3.4 Employers contributions to pension schemes are normally determined by an actuarial calculation of the level of funding required for the scheme to meet its liabilities as they fall due. There are no fixed standards for these calculations, or supervision of funding levels.

3.5 Schemes are generally funded on a 'going concern' basis rather than an 'accrued benefits' basis. This means funding is at the level which in the long-term will leave them able to discharge their liabilities. The nature of funds is such that this normally means that, in the short-term, resources are insufficient to discharge the present accrued liabilities. This strengthens the case for safeguards on long-term funding levels, so as to minimize any possible short-term deficiency.

3.6 In recent years it has not been uncommon for actuarial valuations to indicate funding deficiencies to employers, not least because returns on investments have not matched expectations. Currently, however, the trend is more toward valuations indicating surpluses. A funding surplus might be welcomed by employees as providing additional security for promised and discretionary benefits, and, going beyond this, as a means of allowing benefits to be improved. However, employers are likely to see surpluses as a pretext for reducing their contributions, and Shell, Marks and Spencer and British Airways, are among those who have done so already.

3.7 Recently, the Inland Revenue opened the door to an even less desirable practice by relaxing the rules which prevent employers reclaiming money from the pension fund. In a recent, publicised example, a loss-making company reclaimed £2 million (equivalent to 5% of its own turnover) from the pension scheme. The Inland Revenue position is that they will not normally object to such practices and are quire prepared to consider applications from companies in financial difficulties, but they have refused to disclose details of the numbers of applications with which they have dealt.

3.8 This sort of practice encourages employers to look upon pension funds as a resource in time of trouble and the temptation is to reduce funding levels to a minimum and even to vary actuarial assumptions to produce surpluses. Safeguards to stop this sort of behaviour are at present either non-existent or inadequate.

3.9 In Table 4 below, are set out the actual employee and employer contributions to occupational pension schemes as a percentage of pensionable earnings in 1982.

Table 4 : Pension Scheme Contributions	Lower Quartile	Average	Upper Quartile
Contributory Schemes			
Employee	3.4%	4.3%	5.4%
Employer	7.3%	11%	13.7%
Non-Contributory Schemes (Employer only)	10.7%	16.3%	21.7%

[Source : NAPF Survey 1982]

NOTE : The figures for employee and employer conrributions cannot be summed to obtain an overall contribution.

3.10 Clearly, the contributions going into pension schemes vary widely and the main element of variation is in the employers' contribution. Inevitably, this has to mean widely differing levels of benefits. Comparisons of schemes promised benefits often do not show this up clearly.

3.11 The recent consultative document produced by the DHSS : 'Greater Security for the Rights and Expectations of members of Occupational Pension Schemes', proposes new requirements for disclosure of information. It rejects imposing obligations on employers to guarantee pensions and controls on funding levels. It will help, therefore, to highlight these problems but will not directly help to resolve them.

4 Pensions and Inflation

Data collected by the National Association of Pension Funds provides a detailed picture of practice as regards the granting of increases in pensions in payment. This tends to reflect the experience of larger schemes, which are generally better than average. In Table 6, are set out the latest NAPF findings as regards guaranteed pension increases.

Table 6 : Guaranteed Increases in Pensions Scheme Providing	Public Sector	Private Sector
(a) No Guaranteed Increase	19%	66%
(b) Guaranteed Increase	81%	34%
of which 3% or less	6%	22%
4-5%	0%	9%
RPI	75%	3%

[Source : NAPF Survey 1982]

4.1 The rules of those schemes not providing guaranteed increases, or providing for guaranteed increases which are less than the RPI, usually provide for periodic, most commonly, annual reviews of pensions. However, most private sector schemes fall a long way short of protecting pensioners against inflation.

4.2 In the three years, 1979-81, NAPF survey figures revealed that 14% of private sector schemes did not increase their pension payments at all. Of the 68% which did provide an increase in pensions, compensation for inflation averaged out at just under half the increase in prices. The residual 18% of schemes which were asked whether they had increased pensions, declined to answer the question. These figures suggest that the average increase for all private sector scheme pensioners, was in the range of 35-40% of the increase in prices. Since increases are, in most cases discretionary, even this poor performance cannot be guaranteed in future.

4.3 This analysis was in terms of numbers of schemes rather than numbers of members. There is evidence that large schemes tend to provide higher increases, e.g., the Scott Committee found that in those organisations used as comparators for the Civil Service, the average protection against inflation in the second half of the 1970's was 50-55%.

5 The Erosion of Pensions

In the five year period, 1979-83, prices rose by 68%, or 11% per annum. An occupational pension increased so as to compensate for 50% of this increase in prices, would have lost

20% of its value. A pension not increased at all would have lost 40%.

5.1 In Table 7 below, we demonstrate how the value of that portion of an occupational pension over and above GMP, could be eroded during periods equivalent to life expectancy.

Table 7 : Erosion of Pension's Value

Pension Increase	Reduction in real value Male (1) 13 years	Pension after 20 Years Female (2) 20 years
(1) 4% p.a	40%	50%
(2) zero increase	63.5%	75%

5.2 The Government Actuary used an 8% inflation rate as a long-term assumption in pensions calculations. For this reason we have used 8% as the figure to assess the effect of price rises on occupational pensions.

5.3 The proportion of pension which is subject to erosion in this manner is related directly to salary level and years of service, and inversely, to the size of GMP. It is also affected by whether an occupational pension scheme makes allowance for the basic state pension (most commonly done by calculating pension and contributions salary over and above flat-rate state pension.

5.4 In Table 8, below, we illustrate how the proportion of total pension which falls outside of statutory inflation protection might vary in future years.

NOTE : The two dates selected - 1988 and 1998 - are ten and twenty years after the inception of the new State pension scheme. The latter date will be the first year when maximum 20/80 state earnings-related pension and GMPs will become payable. In all the examples we have used, one-sixtieth of final salary for each year of service in

Table 8 : Proportion of Total Pension of Occupational Pensioners not Covered by Statutory Guarantees

Qualifying Service	Pension Assumption	Final Salary 7500	10,000	15,000
(A) Retiring in 1998		%	%	%
40 years	(A)(1)	53	55	63
	(A)(2)	43	48	54
	(B)(1)	55	61	73
	(B)(2)	48	55	70
20 years	(A)(1)	25	25	35
	(A)(2)	13	15	29
	(B)(1)	25	33	51
	(B)(2)	16	23	47
(B) Retiring in 1988				
30 years	(B)(1)	51	60	71
	(B)(2)	43	55	69
20 years	(B)(1)	35	47	60
	(B)(2)	26	40	52

Pension Assumptions

(A) State pensions indexed in line with earnings.

(B) State pensions indexed in line with prices rising 2% p.a slower than earnings.

(1) Scheme making no deductions for flat rate pension.

(2) Scheme making a deduction to allow for flat rate pension.

a scheme, as the basis of the occupational pension. The examples are each on two bases, as described in the note to the table.

5.5 The table shows that even at average earnings levels the proportion of occupational pension not covered by statutory provision for indexation can be as high as 50%, and for those with double average earnings, as high as 70%. These results, when combined with those in Table 7, show (on the assumption that the State pension continues to be indexed in line with prices) the potential erosion of the real value of the total pension of occupational pensioners.

5.6 For example, a man retiring in 1988 with an occupational pension based on 30 years qualifying service, in a scheme which makes no deduction for state flat rate pension, will rely on his occupational scheme for indexation of 60% of the value of his pension. This portion of his pension is likely, on the basis of 50% inflation protection, to be reduced by 40% in real value in the course of his thirteen year expected life, implying a reduction in total pension of 25%. If his occupational pension was not increased at all, the reduction would be by 40%.

6 The Indexation of Pensions

In 1981, a Government-instigated inquiry into the value of public sector (inflation proofed) pensions commenced the summary of its findings, known as the Scott Report, with the following words :

" It is a highly desirable social objective that the standard of living of those in retirement should be protected. This is clearly recognised in countries like France and West Germany where the benefits enjoyed are superior to those of this country and the benefits of index-linking are extended alike to both public and private sectors. "

6.1 In 1982, the Occupational Pensions Board, in its report 'Greater Security for the Rights and Expectations of Members of Occupational Pensions Schemes', echoed these sentiments :

" We recommend that all schemes should, as far as possible, seek to maintain the full real value of the retired members' pension income. "

6.2 Inflation protection is costly and the cost is sensitive to long-term assumptions. Actuarial estimates suggest that the pension scheme giving an 8½% annual increase in pensions, the Inland Revenue maximum, requires twice the size of funds of a scheme giving no increases. The fact that a 3% increase in pensions adds only 20% to the size of funds, as compared to a no increase position, illustrates how funding requirements increase disproportionately the larger the size of the pension increases.

6.3 It is not clear at present to what extent schemes plan to compensate for inflation and to what extent pension measured performance due to funding assumptions being negated by actual changes in earnings, prices and investment returns (etc).

6.4 Pensions increases may be funded from outside the pension scheme by the employer on a pay-as-you-go basis, or by lump sum payments into the fund as pensions increases are granted.

6.5 Ideally, as an objective, we would like to see all occupational pensions fully indexed. However, this is so far removed from current experience that achievement in present circumstances is not realistic. As an interim position, the following proposals should be considered :

(i) Occupational pension schemes should be required to guarantee a minimum increase, say 5% or a specified percentage of inflation, to limit the erosion of pension, and this should be funded.

(ii) Schemes should be required to specify the level of inflation protection provided for in the actuarial calculation of funding rates.

(iii) Special rules should govern the calculation of 'pension surpluses' to strengthen inflation guarantees.

(iv) Details of pensions increases granted and policy on increasing pensions should be disclosed annually.

7 The Early Leaver

There is very little statistical information on the extent of the early leaver problem, perhaps because the 'industry' does not wish to highlight a major weakness in current pension provision. However, a large majority of scheme members are early leavers.

7.1 In Table 9, we extrapolate figures for length of service, using data from the 1979 Labour Force Survey. Even for non-manual males, the occupational group likely to have the longest average length of service, only one quarter of those reaching retirement will have 40 years service with their present employer.

Table 9 : Length of Service at Retirement for Non-Manual Males

Year Age	1975 45+	1979 50+	1984 55+	1989 60+
Service in Years				
0-5	19%	15%	19%	15%
5-10	14%	17%	12%	16%
10-15	11%	12%	14%	10%
15-20	10%	10%	10%	12%
20-25		8%	8%	8%
25-30	46%		7%	7%
30-35		37%	31%	6%
35+				26%

[Source : ASTMS Research Department]

7.2 When a person has been an 'early leaver' at some time in a possible forty year plus working life, perhaps at several times, only those years with the final employer will accumulate pension rights based on final salary level at retirement. Pension rights for service with previous employers will be calculated on the basis of previous earnings levels and paid in the form of deferred pensions (or discounted transfer values).

7.3 Many people who change or lose their jobs in the private sector have their pension rights frozen for the 10, 20, or 30 years they have to go to retirement age. The average leaver, who changes jobs two or three times, will finish his/her working life with half as much to live on as the "40 year man".

7.4 Even without inflation the 'early leaver' is at a disadvantage in occupations where it is usual for earnings to rise with age, either through promotion or seniority. The Occupational Pensions Board report on <u>Rights and Expectations of Early Leavers</u> (1981), stated that in a situation where general (real) earnings tend to rise each year, the losses of pension rights among early leavers become almost universal, and tend to become not only losses relative to stayers but also absolute losses in the purchasing power of preserved pensions.

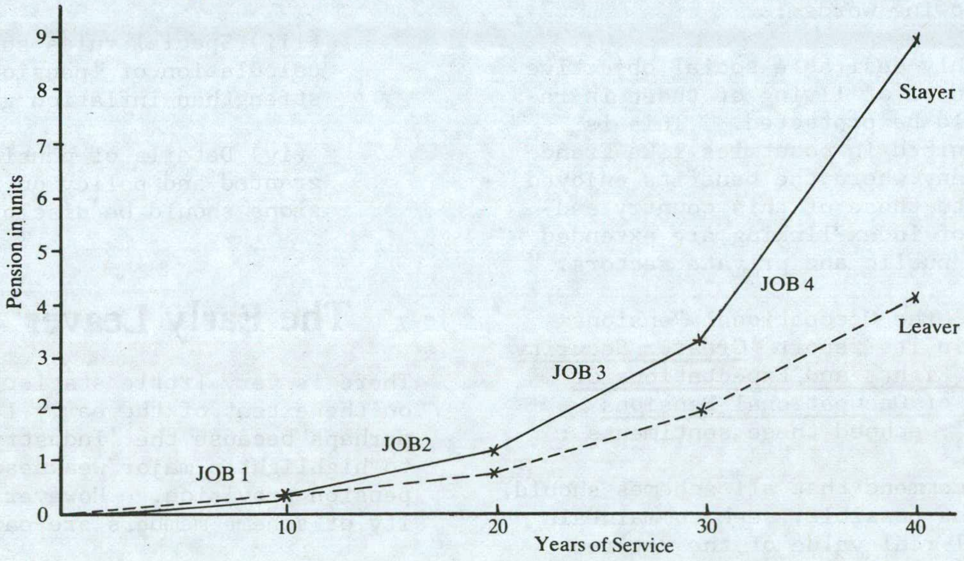
7.5 For the early leavers, the vast majority of occupational pension scheme members, the question of increases in deferred pensions is crucial.

7.6 The 1982 NAPF Survey showed that 75% of private sector pension schemes, covering 56% of members, provide <u>no</u> increases in deferred pension.

7.7 In Diagram 1 we illustrate how job changes reduce the early leavers' pension, given no increases in deferred pension.

Diagram 1 : Build up of Pension Rights for Stayers and Early Leavers at 7½% Per Annum Earnings Growth

Assumptions: Pension calculated at 1/80th final salary. Stayer remains in same employment for 40 years
Leaver changes jobs every 10 years, and takes deferred pension which is not increased.
Starting pay one unit per year.



SOURCE: "IMPROVED PROTECTION for the OCCUPATIONAL PENSION RIGHTS and EXPECTATIONS of EARLY LEAVERS"

A Report of the Occupational Pensions Board

7.8 Despite a consensus that the position of early leavers must be improved, there has been little voluntary action. Opponents of a legislative option still insist on a voluntary evolutionary approach.

7.9 When faced with the possibility of a statutory obligation to increase deferred pensions, the pensions industry, together with the CBI, insist that any improvement in benefits for early leavers must be as a result of the redistribution of resources, i.e the reduction of other benefits.

7.10 However, the Occupational Pensions Board have pointed out that schemes are in a much healthier financial position than they have been for some time and that the resources to increase deferred early leaver pensions should now be available.

7.11 It is clear that legislation must be introduced. The Government appears to accept this view. The OPB's majority recommendation for an increase in the amount of short service benefit up to a ceiling of 5% compound per annum will probably be adopted. ASTMS supports the TUC's proposal, which is based on the OPB's minority recommendation, that deferred pensions should be increased in line with the movements of average earnings, i.e an assumed rate of increase of 8½%.

8 Portable Pensions?

Despite clear evidence of doubts, if not outright opposition from bodies as diverse as the CBI, National Association of Pension Funds (NAPF), Life Offices Association (LOA) and the TUC, the Secretary of State for Social Services has instituted a brief enquiry into the notion of 'portable pensions'. Arising from the deliberations of the Centre for Policy Studies, 'portable pensions' have been suggested as the solution to the Early Leaver problem.

8.1 Essentially, the proposal has been that people might be given the chance to have their own personalised pensions, as if they were self-employed. Money purchase pensions are not new. They have been generally superseded by final salary occupational schemes because they did not provide retirement benefits which would reflect a person's earnings at or near to retirement age. For the pensioner there has always been a significant element of uncertainty as he or she could never be sure of the level of benefits until retirement actually occurred.

8.2 It must be noted, however, that to date no-one has any idea of precisely what the proponents of 'portable pensions' have in mind. As criticisms of the idea are made, so the definition of portable pensions has shifted. However, it is possible to comment on the general idea. Advocates of portable pensions have advanced the following advantages for their idea. We list these below, with our comments.

(a) Control over your Pension

In theory, someone who buys investments has more control over the assets which will eventually produce a pension, but that person has less control over the amount of pension he/she receives than if they were in an occupational scheme.

(b) Greater 'involvement' in Pension Provision

With the new personal portable pensions 'greater involvement' would take place only if an individual took an active role in 'playing the stock market', or monitored and changed unit-linked insurance policies on the basis of performance. This is unlikely.

(c) Creation of a new share-owning class

It is patently obvious that if people are naturally going to secure retirement benefits through institutional investments, a new share-owning class will not emerge.

(d) Redistribution of Wealth

The notion that through portable 'money bought' pension there will be a redistribution of wealth and interest is nonsense. It is also not supported by the evidence available from the USA, where, since 1982, employees have been able to have individual retirement accounts which can be diversely invested. In fact, investment occurs with a very narrow band of financial institutions. Equities are not favoured, as shown in Table 10 below.

Table 10

Institution	US $
Commercial Banks (savings accounts)	28.9
Thrift Institutions	37.0
Money Market	5.1
Equities	6.0
Credit Unions	1.6
Life Insurance (not unit-linked)	5.8

8.3 The advocacy of portable pensions is part of the Government's well advertised philosophy of self-reliance, whereby individuals should not be dependent on the state (or even large private institutions) but should set aside part of their income to provide for their future.

8.4 In this context, it is worth pointing out that since taking office in May, 1979, the Government has twice undermined the attraction of saving. In last year's Budget the amount of the surrender value of Life assurance policies taken into account in assessing social security benefits was increased. In the most recent Budget the Government intends to abolish the 15% tax relief on Life Assurance Premia.

8.5 Where we are concerned with the redistribution of wealth, the practicalities of the 'portable pension' by money purchase will mitigate against it.

8.6 We suggest that the option to purchase one's own pension will not be exercised consistently or adequately to ensure the retirement security of the mass of those who will become early leavers.

8.7 The extra purchase of security in retirement is commonly exercised currently through Life assurance or individual pension plans offered by a wide range of financial institutions.

8.8 This option is most frequently exercised by those with sufficient income while in work to do so. Low income employees will not be able to exercise the money purchase option in a way that will give them security or redistribute wealth. In short, the option will be attractive and practicable for mobile high earners. The ordinary early leaver will remain penalised.

8.9 Portable pensions are not a solution to the early leaver problem. The idea they represent has not been thought through, unless it is the intention of the Government and its advisors to offer a cosmetic which will only help a minority who do not need it.

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Conclusions

1 The link between increases in state pensions and average earnings should be restored. At present, the Government is talking about making reforms while drawing a veil over the fact that it has already fundamentally downgraded the quality of the state scheme.

2 Government proposals, supposedly aimed at providing 'Greater Security for the Rights and Expectations of Members of Occupational Pension Schemes', do nothing to strengthen scheme members legal rights, except insofar as by giving rights to information, they will make more obvious the unacceptably wide variations in the quality of schemes.

3 All occupational schemes should be legally obliged to provide a guaranteed minimum increase in pensions in payment and funding levels should be more rigorously supervised by the OPB in order to ensure their ability to do so.

4 Pension schemes should be obliged by law to increase the deferred pensions of early leavers in line with the increase in average earnings. In principle, this should be possible in current circumstances without reduction of other aspects of benefits.

5 Portable pensions, suggested as an alternative solution to the early leaver problem would threaten the whole basis of pensions based on final salary, in order to offer some advantage to a few mobile high income earners and to divorce employers from a continuing commitment to underwrite pensions for past service.

SPARE

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From the Minister for the Arts

17 April 1984

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury, SW1

CH/EXCHEQUER	
REC.	18 APR 1984
ACTION	Mr Hopkinson
COPIES TO	Mr Monger
	Mr Jefferson-Smith (C+E)
	MST
	PS/CST

for comm by 20C today

Dear Nigel,

IMPACT OF THE BUDGET

I have just seen a copy of Patrick Jenkin's letter of 3 April to you.

I share Patrick's concern about the impact of extending VAT to building alterations. Quite apart from the general implications of this for heritage property, there will be an immediate effect on the national museums' and galleries' building and maintenance programme, which is borne on PSA Votes but charged against the OAL PES programme. A significant part of the building and maintenance work is not new construction but much-needed internal alteration, improvement and refurbishment of ageing historic premises.

The VAT change here will probably cost about £0.8 million in 1984-85, and £1 million or more annually thereafter. Unless other steps are taken, the cost would have to be absorbed at the expense of deferring or abandoning urgent building work, of which there is already a disturbing backlog. This would largely undo the good achieved in last year's PES round when I was granted a modest increase (though less than I had requested or think sufficient) for this programme of work. It would provoke renewed pressure from Peter Carrington and other museum trustee board chairmen who are already extremely worried about the state of their buildings and the pace at which it can be put right.

I do hope it will be possible to find some way of relieving, or compensating, the museums and galleries' programme for this charge - both in 1984-85 where the cash-limited provision is already fixed in the Supply Estimates, and for future years. For the latter, I shall if necessary raise the issue during the 1984 PES exercise: but it is important to have a defensible answer to criticism now.

3.00pm
TODAY

I will be very happy to join Patrick's proposed meeting with you if that will help. I am sending him a copy of this letter.

LORD GOWRIE